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São Tomé and Príncipe: Staff Report for the 1999 Article IV Consultation and Request for an Arrangement Under the Poverty Reduction and Growth Facility

This report was prepared by a staff team of the International Monetary Fund following discussions with the officials of São Tomé and Príncipe on economic developments and policies. The report was then considered by the IMF's Executive Board in the context of the IMF's periodic consultation with São Tomé and Príncipe, as required under Article IV of the IMF Articles of Agreement. The views expressed in the staff report itself are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF or of the authorities of São Tomé and Príncipe; a supplementary statement by IMF staff may also be included. The views of the Executive Board as expressed in the discussion of the Article IV consultation report and as summarized in a Public Information Notice (PIN) are also included. In addition, a statement by the member country authorities may be appended. Further background documentation prepared by IMF staff for the consultation may be published separately at a later date. The policy of publication of Article IV staff reports allows for the deletion of market sensitive information.

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SÃO TOMÉ AND PRÍNCIPE

Staff Report for the 1999 Article IV Consultation and Request for an Arrangement Under the Poverty Reduction and Growth Facility

Prepared by the African Department

(In consultation with the Legal, Monetary and Exchange Affairs, Policy Development and Review, Statistics, and Treasurer's Departments)

Approved by Paul A. Acquah and Christian Brachet

March 24, 2000

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EXECUTIVE SUMMARY

Background

Following a decade of very large macroeconomic imbalances and declining real per capita income, the government successfully implemented a staff-monitored program in 1998-99 that turned around the primary budget balance from deficit to surplus, lowered inflation, and helped improve real GDP growth. However, poverty and social indicators worsened in São Tomé and Príncipe and the country's public external debt remained particularly heavy, with a net present value representing 14 times the total exports of goods and services in 1999.

Performance under the staff-monitored program for 1999

Performance under the staff-monitored program was satisfactory, with seven of the eight quantitative benchmarks for end-September and end-December 1999 observed. The exception was the target on primary expenditures, which was exceeded by a large margin, owing to overruns in the wage bill and public investments. Improvement in tax administration continued to strengthen collection of direct and indirect domestic taxes, including customs duties, and tax revenue performance was stronger than programmed. In addition, all structural benchmarks through end-December were observed, with the exception of the preparation of the government strategy for the privatization of large government agricultural estates and the rationalization of the system of land tenure. The authorities established a timetable for civil service retrenchments, adopted a new public enterprise reform and privatization program, created an administrative unit for the oil sector, and began to submit monthly monetary data to the staff on a timely basis. They also dealt decisively with an attempt to defraud the central bank and achieved good progress in trade liberalization, with the elimination of the practice of allocating foreign exchange and the removal of nontariff barriers.

Program for 2000-02 and key issues for discussion

The program's economic objectives for 2000-02 would be to (a) reduce the end-of-period inflation to 3 percent in 2001-03, and (b) contain the external current account deficit (including official transfers) at 41 percent of GDP by 2002. Real GDP growth is projected to rise to 4 percent by 2002.

In the fiscal area, the program aims at reducing the overall fiscal deficit (including grants) from 26 percent of GDP in 1999 to 16 percent of GDP in 2002, and at increasing the primary budget surplus (excluding foreign-financed investment) from 1.3 percent of GDP in 1999 to 5 percent of GDP in 2002. Government revenue would be raised to 22 percent of GDP in 2002, from 19 percent in 1999. The authorities would limit domestically financed primary expenditures to 17 percent of GDP, while providing adequately for health and education services.

Monetary policy will aim at reducing end-of-period inflation to 5 percent by end-2000 and strengthening the net foreign assets position of the banking system, while maintaining a flexible exchange rate system. The mission encouraged the authorities to accept the obligations of Article VIII of the Fund's Articles of Agreement. Key structural measures include (a) the implementation of a comprehensive civil service reform and retrenchment program; (b) the implementation of a new public enterprise reform and privatization program; (c) the enhancement of transparency, accountability, and good governance, including in the central bank, budget, and oil exploration operations; and (d) the preparation of a poverty reduction strategy and action plan.

Issues raised in the staff appraisal

The staff appraisal raises the following key issues:

- The limited administrative capacity in São Tomé and Príncipe. The authorities will need extensive technical and financial assistance to help prepare and implement the measures required in the areas of civil service reform, public enterprise reform and privatization, oil policy, and statistics, including the development of poverty indicators.

- The need to continue to ensure a prudent and transparent management of public sector resources, including external assistance and oil sector bonuses. It is also essential to contain primary expenditure, including the wage bill and domestically financed public investment.

- The need to remain current on nonreschedulable external debt-service obligations.

- The need to strengthen tax and customs administration and implement the key structural measures.

- The need for the central bank closely to monitor bank portfolio performance, and remain vigilant in framing and implementing the recapitalization and restructuring program for the one bank in difficulty.

- The need to implement the PRGF-supported program in order to establish the three-year track record of policy performance needed for the country to qualify for assistance under the enhanced HIPC Initiative.

São Tomé and Príncipe: Selected Economic Indicators, 1996-2002

	1996	1997	1998 Est.	1999 Est.	2000	2001	2002
						Program	
	(Annual percentage change, unless otherwise specified)						
Real GDP	1.5	1.0	2.5	2.5	3.0	4.0	4.1
Consumer prices (end of period)	51.7	81.1	20.8	12.6	5.0	3.0	3.0
Broad money	82.2	94.5	24.5	3.6	5.0	...	...
Credit to government (net) 1/	59.1	-113.4	18.2	-14.3	-27.2	...	...
Exchange rate (dobras per U.S. dollar; period average)	2,203	4,553	6,927	7,093	...	...	...
	(In percent of GDP, unless otherwise specified)						
Overall fiscal balance (commitment basis)	-32.2	-26.7	-30.5	-25.8	-21.5	-18.2	-15.7
Primary budget balance (commitment basis; excluding foreign-financed investment)	-4.7	-2.2	0.7	1.3	2.3	3.4	5.0
Current account balance							
(excluding official transfers)	-79.3	-74.8	-53.9	-57.2	-62.1	-64.0	-66.2
(including official transfers)	-30.8	-3.6	-21.1	-25.4	-25.2	-38.1	-41.0
Public external debt outstanding	590.0	608.5	721.3	636.0	...	...	...
Net present value of public external debt 2/	1,446.0	1,441.9	1,634.6	1,450.1	...	...	...
External debt-service ratio (before debt relief) 2/	73.5	71.8	83.1	49.7	43.6	39.7	48.2

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ In percent of broad money at beginning of period.
2/ In percent of exports of goods and services.

I. INTRODUCTION

1. In concluding the last Article IV consultation on July 13, 1998,[1] Executive Directors urged the authorities to tighten fiscal and monetary policies and accelerate the pace of structural reforms. They stressed that São Tomé and Príncipe needed to implement rigorously the measures envisaged for 1998 to liberalize the economy, enhance the prospects for higher growth, and help establish a good track record, with a view to paving the way for a Fund-supported program and attracting much needed concessional financing, including debt relief. The government satisfactorily implemented a policy framework in 1998 and a staff-monitored program in 1999[2] that turned around the primary budget balance from deficit to surplus, lowered inflation, and helped raise real GDP growth.

2. In the attached letter, dated March 24, 2000 (Appendix I, Attachment), the Minister of Planning, Finance, and Cooperation of São Tomé and Príncipe requests a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF), in an amount equivalent to SDR 6.657 million (90 percent of quota). Discussions with the authorities of São Tomé and Príncipe regarding this request were held in São Tomé in August-September and November 1999, and were concluded in Washington in January 2000.[3] The authorities were represented by Prime Minister Posser da Costa, the Minister of Planning, Finance, and Cooperation (Mr. Adelino David), the Governor of the Central Bank (Mrs. Maria do Carmo Silveira), and other senior government officials, including the Ministers of Economy, Education, Health, Justice, and Public Administration and Employment. Meetings were held also with President Miguel Trovoada and National Assembly Speaker Francisco Pires, as well as with leaders of the three political parties represented in the National Assembly, and representatives of trade unions, the banks, public enterprises, the chamber of commerce, and the international community in São Tomé.

3. The requested PRGF arrangement is in support of the policies and measures outlined in the government's interim poverty reduction strategy paper (interim PRSP) and policy

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[1] São Tomé and Príncipe is on the standard 12-month consultation cycle.

[2] The staff-monitored program for 1999 was described in a staff report circulated to Executive Directors on March 24, 1999 (EBS/99/47; 3/23/99).

[3] The staff representatives who participated in the discussions were Mr. I. Thiam (head), Mr. Leite, Mr. Santos, Mr. Moissinac, Mr. van den Boogaerde, Mr. Abdoun (all AFR), Ms. Sucharov, and Ms. Haddi (respectively, administrative assistant and assistant-AFR). Mr. Toé, the Fund's resident representative for Gabon and São Tomé and Príncipe assisted the mission in November and January. World Bank and African Development Bank teams participated in the discussions on the government's interim poverty reduction strategy paper (interim PRSP) and policy matrix. Mr. Ondo Mañe, Alternate Executive Director for São Tomé and Príncipe, attended some of the policy discussions in September.

matrix for 2000-02, which were prepared by the authorities following an initial consultation with civil society and with assistance from the staffs of the Fund and the World Bank, and in the memorandum of economic and financial policies (MEFP) for 2000 (Appendix I, Attachment). The interim PRSP and policy matrix will be transmitted to the Managing Director of the Fund and the President of the World Bank in the coming days.[4]

4. The proposed total access under the requested PRGF arrangement takes into account the strength of the program adopted by the authorities, São Tomé and Príncipe's present indebtedness to the Fund, and its projected financing needs over the next three years. Disbursement would be in seven equal semiannual loans (Tables 1 and 2). In June 1999, São Tomé and Príncipe repaid its last debt-service obligations to the Fund on schedule, and, given the prospective improvements in its fiscal and balance of payments positions, the country can be expected to meet its future obligations promptly. To help strengthen program implementation and monitoring, a Fund resident representative has been assigned to São Tomé and Príncipe, effective November 1999.[5]

5. The World Bank, which, except for technical assistance grants, has suspended its lending operations in São Tomé and Príncipe since 1992 (for lack of an appropriate macroeconomic framework), is pursuing discussions on reform programs in the agricultural, energy, and social sectors, as well as in the areas of civil service, privatization, and land tenure. As indicated in the joint staff assessment of the interim PRSP, the Bank is now considering a nonproject credit, which will include a technical assistance component, to help meet the country's external financing requirements and strengthen the government's administrative and economic management capacity. The World Bank will also review its medium-term strategy for São Tomé and Príncipe in the coming weeks and outline a new lending program for the country.

6. São Tomé and Príncipe continues to avail itself of the transitional arrangements of Article XIV. A summary of São Tomé and Príncipe's relations with the Fund is contained in Appendix II; Appendix III describes São Tomé and Príncipe's relations with the World Bank Group; Appendix IV discusses statistical issues; and Appendix V includes basic data

7. São Tomé and Príncipe enjoys a democratic political system, with a freely elected head of state, President Miguel Trovoada, belonging to a party holding a minority

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[4] The authorities have already agreed to publish their interim PRSP, policy matrix, and memorandum of economic and financial policies, following approval by the Executive Board. They have also indicated their intention to participate in the pilot program on release of Article IV staff reports and their consent to the issuance of the Public Information Notice.

[5] Mr. Toé, who also covers Gabon, resides in Libreville and visits São Tomé for one week every month.

representation in parliament. The ten-member government of Prime Minister Posser da Costa was appointed on January 5, 1999 by the party that has been holding the majority of seats in parliament, following a free and transparent legislative election in November 1998.[6] The government has pledged to seek consensus with the President on the major economic and political issues facing São Tomé and Príncipe. The Prime Minister conducted consultations with the three main political parties and trade unions on selected policy issues, including civil service reform and wage policy, before undertaking the preparation of the draft budget for 2000 and finalizing the negotiations on the PRGF-supported program.

II. Background and Performance Under the Staff-Monitored Program

8. São Tomé and Príncipe's performance during the two-year period 1998-99 under the government policy framework and then a staff-monitored program was broadly satisfactory. All quantitative benchmarks for end-September and end-December 1999 were observed, with the exception of the ceiling on primary budget spending, which was exceeded by a large margin because of budgetary overruns on the wage bill and domestically financed public investments. In addition, all structural benchmarks through end-December were observed, with the exception of the preparation of the government strategy for the privatization of large government agricultural estates and the rationalization of the system of land tenure (Tables 3 and 4).

9. In 1998, real GDP growth reached 2.5 percent, up from 1 percent in 1997 (Table 5), led by a recovery in cocoa production and a pickup in the trade and construction sectors. In 1999, cocoa output, the major export crop, fell by 13 percent, world cocoa prices also fell sharply, and import prices for petroleum products rose threefold. However, progress in reforms began to alleviate the structural rigidities, and the impact of the decline in cocoa production was more than offset by a rapid expansion in trade, construction, and tourism, the latter of which became profitable following increased foreign direct investment in hotel facilities. As a result, real GDP growth is estimated to have remained at 2.5 percent in 1999, as projected under the staff-monitored program. The implementation of agreed macroeconomic policies also reduced financial imbalances, and the end-of-period inflation dropped substantially to about 21 percent in December 1998, and further to 13 percent in December 1999, from over 80 percent in 1997.

10. After declining by 13 percent in 1997, the real effective exchange rate based on the consumer price index (CPI) stabilized in 1998-99 (Figure 1). **The nominal exchange rate of**

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[6]The majority party now holds 31 of the 55 seats in the new National Assembly, an increase of 4 seats from the outgoing assembly; the President's party also increased its representation from 14 to 17 seats. A third party, formerly a member of the ruling coalition with the majority party, keeps 7 seats, a decline of 7 from the outgoing assembly.

the dobra is largely determined by market forces;[7] the spread between the official rate of the dobra and the parallel rate narrowed from 6.5 percent in 1996 to less than 1.5 percent during August 1998-December 1999, except in March 1999, when it reached 2.4 percent following the uncovering of a treasury bond fraud attempt.[8] The external current account deficit (excluding official transfers) narrowed from 75 percent of GDP in 1997 to 54 percent of GDP in 1998 but widened to 57 percent of GDP in 1999, reflecting lower cocoa export volumes and prices, as well as higher imports (Figure 2 and Table 6). Including grants, the external current account deficit widened from 4 percent of GDP to 25 percent of GDP during 1997-99.

11. In the fiscal area, **the primary budget balance** (excluding foreign-financed investments) **turned around from a deficit of 2.2 percent of GDP in 1997 to a surplus of 0.7 percent of GDP in 1998 (Db 1.9 billion)**. The primary surplus **is estimated to have increased further** to 1.3 percent of GDP in 1999, as better-than-programmed tax revenue collections offset the noninterest spending overruns (Table 7). On the revenue side, measures have been taken since 1998 to improve tax administration and collections, including the strengthening of the tax audit unit, which contributed to a strong performance of direct and indirect domestic taxes in 1998-99. However, there was a large shortfall in nontax revenue in 1999 because the fishing royalties, which were projected at Db 6 billion in 1999 under the staff-monitored program, did not actually exceed Db 0.9 billion.[9] As a result, the primary budget surplus reached only Db 4.3 billion, or 1.3 percent of GDP in 1999, compared with a projected surplus of Db 9.3 billion (2.8 percent of GDP). Adjusted for the shortfall in the mobilization of fishing royalties, the targets on the primary budget balance for end-September and end-December 1999 were met. Adjusted for the nonmobilization of the special nonproject external grant,[10] the target on the net bank credit to the government was

[7]The official exchange rate at which the central bank conducts its operations is determined on a daily basis as a weighted average of the exchange rates in the *bureaus de change*, parallel market, and commercial banks.

[8] In February 1999, the government uncovered a fraud attempt involving the trading of US$500 million in São Tomé and Príncipe's treasury bonds, which were fraudulently issued by two central bank officers in October 1998. The bonds were seized by the Belgian police, the two officers were removed from their positions, and in March 1999 a judicial process was initiated against them. The case is awaiting trial.

[9] Under the new fishing agreement (signed in June 1999) with the European Union, the fishing royalties for 1999 will amount to € 636,000, or Db 4.8 billion, of which one-half is earmarked for specific projects. The part not earmarked was partially disbursed in 1999.

[10] The nonproject component of the special grant from Taiwan Province of China, which was projected at US$6 million in 1999, was not mobilized. Instead, in accordance with understandings reached in 1999, the grant from Taiwan Province of China has been entirely earmarked for project financing.

also met. On the expenditure side, budgetary overruns on the wage bill occurred because the higher salary scale for the education and health sectors was made effective as of January 1999, or three months ahead of schedule, and because promotions were granted in the military. Domestically financed public investments reflected important road repairs and the renovation of government buildings in São Tomé.

12. Monetary policy remained tight in 1999, as the central bank maintained the reserve requirement ratio at 22 percent and commercial banks kept their savings and lending rates substantially above the central bank reference interest rate.[11] Money supply increased by less than 4 percent, a rate considerably lower than the end-of-period inflation (Tables 8-10). Net bank credit to the government contracted by 14 percent of beginning-of-year broad money, reflecting an increase in deposits made possible by the mobilization of the oil concession rights. Credit to the economy is estimated to have risen by 11 percent of beginning-of-the year broad money (more than programmed), and the net foreign assets of the banking system strengthened by nearly 14 percent of beginning-of-year broad money, in spite of some capital flight caused in March 1999 by the uncovering of the treasury bond fraud attempt. Adjusted for the shortfall in exceptional financial assistance, the floor set under the staff-monitored program on the net international reserves position of the central bank was observed in September and December. However, the position of one of the two banks with regard to prudential and solvency ratios deteriorated during the second half of 1999. In the face of growing liquidity problems, the concentration of credits on a small number of enterprises, and related lending, the central bank has strengthened its monitoring of the concerned bank's credit portfolio to ensure that the largest loans are performing and collateralized. It has also required the bank to limit credit and recapitalize.

13. **On the structural front**, in 1997, the government liquidated the national savings and loans institution (CNPC), for which a loan recovery program was established. In 1998, it partially privatized the petroleum distribution company (ENCO) and placed two hotels under private management (Miramar and Pousada Boa Vista). The authorities also eliminated price controls, completely liberalized domestic trade, including the marketing of agricultural products, and introduced a mechanism to automatically adjust the retail prices of petroleum products in line with changes in international prices.[12] During the same period, they also

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[11] As inflation abated, the central bank progressively reduced its reference interest rate from 29.5 percent in November 1998 to 17 percent in August 1999. However, the two banks maintained savings rates at 24 percent and lending rates at close to 40 percent throughout the year, mainly because of the lack of competition and structural impediments to financial intermediation, including a deficient judicial system that makes it difficult to realize collateral on nonperforming loans.

[12] In response to the rise in prices of petroleum products on world markets, and in accordance with the automatic adjustment mechanism for retail petroleum product prices adopted in 1997, ENCO raised the pump prices for premium grade gasoline, diesel and kerosene, by 10 to 13 percent on October 30, 1999, and further by 35 to 45 percent on February 14, 2000.

eliminated quantitative restrictions on imports, except for allocations of foreign exchange on a preferential basis for imports of consumer staples (essential food products, petroleum products, drugs, and agricultural products). Furthermore, in September 1998, the monetary authorities eliminated the requirement to surrender export receipts to the central bank, after gradually reducing the surrender requirement ratio from 70 percent in 1997 to 30 percent in June 1998. In February 1999, the authorities eliminated the practice of allocating foreign exchange for imports and, in August, they adopted a new foreign exchange legislation that removed all nontariff import barriers and liberalized external current account transactions. With World Bank and French technical assistance, the government also prepared a comprehensive reform of the customs tariff structure and a plan to eliminate export taxes, with a view to implementing both in early 2000. With these trade liberalization reforms, the index of trade policy restrictiveness compiled by Fund staff is estimated to have been reduced to 5 in 1999, down from 10 in 1997-98.

14. In the area of **oil exploration**, the government has established, with assistance from the World Bank and Norway, an administrative unit in the office of the Prime Minister to oversee government policy in the oil sector, prepare the necessary legislation in the wake of oil- production-sharing negotiations with ExxonMobil, and ensure transparency in the handling of future oil operations. In the area of **public investment**, the authorities have initiated a system of three-year rolling investment programming, but sectoral strategies and priorities are not fully reflected yet in this new framework, because of limited capacity in project preparation and monitoring. Progress was also made **regarding civil service reform**. With technical and financial assistance from the World Bank and the United Nations Development Program (UNDP), the authorities approved new organizational and staffing plans for the ten (10) ministries in October-November 1999.[13] In addition, the government published a new public enterprise reform and privatization program in October 1999.[14] However, there were delays in the preparation of the government's strategy for the privatization of large government agricultural estates and the rationalization of the system of land tenure.

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[13] Ministry of Planning, Finance and Cooperation; Ministry of Economy; Ministry of Public Administration and Employment; Ministry of Foreign Affairs; Ministry of Defense; Ministry of Justice; Ministry of Education; Ministry of Health; Ministry of Infrastructure, Natural Resources, and Environment; Ministry of Local Administration and Territorial Affairs.

[14]The government will (a) liquidate two (2) companies, a meat processing concern (ENCAR) and medicine distribution company (ENAMED); (b) privatize two (2) others, a hotel (Pousada Boa Vista) and the coffee plantation (Monte Café); and (c) conduct restructuring/privatization studies for three (3) companies, with a view to deciding on their future--the palm-oil development company (EMOLVE), a construction materiel distribution company (Cunha Gomes), and the national airlines (Air São Tomé).

15. Regarding governance issues, the judicial investigation on the treasury bond fraud attempt has now been enlarged to include all possible fraudulent treasury bonds issued in 1996-98 and all individuals or companies that may attempt to trade such treasury bonds. At the same time, the authorities have issued an information notice, intended for financial institutions in São Tomé and Príncipe and abroad, urging against involvement in any scheme of issuance or trading of these fraudulent treasury bonds. In addition, the central bank hired a reputable firm that conducted in November 1999 an independent external audit of its foreign assets accounts at end-1998. The new central bank management has also issued a detailed report on the fraudulent transfer of foreign assets that occurred in 1994,[15] established responsibility, removed the agents involved, and taken legal action. In addition, it has started strengthening bank supervision, as well as the internal audit and control functions in the central bank, with Fund technical assistance.

16. Notwithstanding the satisfactory progress made under its policy framework in 1998 and under the staff-monitored program in 1999, the economic and financial situation of São Tomé and Príncipe remains difficult. Given the low per capita income and the protracted economic decline through 1997, poverty and social indicators have worsened (Box 1). In addition, São Tomé and Príncipe's external debt amounted to US$296 million (636 percent of GDP) at end-1999, with 58 percent owed to multilateral creditors (Table 11). The net present value of the debt was US$198 million, equivalent to 14 times the value of exports of goods and services. The stock of arrears amounted to US$75 million, of which US$47 million was on short-term debt[16] and US$28 million was on medium- and long-term debt to bilaterals, mainly Paris Club creditors. In 1999, São Tomé and Príncipe eliminated its nonreschedulable external arrears and continued to service its external debt to multilateral institutions.

III. Report on the Discussion and the Adjustment Program for 2000-02

A. Medium-Term Poverty Reduction Strategy

17. Given São Tomé and Príncipe's debt burden which is clearly not sustainable, widespread poverty, and the remaining structural rigidities which impede economic growth, the authorities have decided to reinforce the progress made in restoring macroeconomic stability and to tackle the country's structural problems as a matter of urgency. They have adopted an interim PRSP and launched a participative process with civil society, with a view to finalizing a full PRSP by end-2001 (MEFP, paragraph 27, and the joint assessment of the

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[15] The fraudulent transfer amounted to US$1 million in 1994.

[16] Short-term debt, which is entirely owed to Angola, Italy, and Portugal and is all in arrears, represented 16.1 percent of total debt or more than 4 times the amount of gross international reserves at end-1999.

interim PRSP). The interim PRSP aims at achieving a sustainable growth in per capita income and is based on the implementation of measures, particularly in the education and health sectors, designed to improve the living conditions of the most vulnerable groups of the population. The authorities will establish a committee to oversee the poverty reduction strategy and monitor poverty indicators by end-December 2000.

18. The key objectives of the proposed PRGF-supported program include bringing the economy onto a sustainable growth path, reducing poverty, and making progress toward external viability. Within this framework, the macroeconomic objectives for 2000-02 are to (a) reduce inflation to 5 percent in 2000 and 3 percent during 2001-02 on an end-of-year basis, and (b) contain the external current account deficit (excluding official transfers) at 66 percent of GDP (or below 41 percent of GDP, including official transfers) in 2002, despite the expected start of large scale oil-related foreign investment.[17] Real GDP growth is projected gradually to increase from 2.5 percent in 1998-99 to 4 percent by 2002, allowing per capita income to rise by 1.7 percent a year. Private investment is expected to exceed 30 percent of GDP, and the program seeks to raise national savings to 20 percent of GDP, by 2002.

19. To achieve these objectives, the economic reform efforts are to continue to focus on four key policy components: (a) the pursuit **of a prudent fiscal policy aimed at increasing the primary budget surplus to 5 percent of GDP by 2002**, while allocating increased funding to education, health, and fiscal administration; (b) the pursuit of an **appropriately tight monetary policy to lower inflation** and improve international reserves, in the context of a flexible market-based exchange rate regime; (c) a **deepening of structural reforms to promote private sector development and investment**; and (d) the implementation of an ambitious poverty reduction strategy and action plan.

B. The Program for 2000

20. The first annual program to be supported under the three-year PRGF arrangement covers the year 2000. It aims at reducing the 12-month rate of inflation to 5 percent by December and limiting the external current account deficit (excluding official transfers) to 62 percent of GDP (or 25 percent of GDP, including official transfers). Real GDP growth is projected to increase to 3 percent. The key elements of the program are discussed in the following sections; a more detailed description is provided in the authorities' memorandum

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[17]Petroleum prospects are very promising and oil reserves could be large, on the order of 400 million barrels, with a possible coming onstream of an oil field in 2005. The program projects that investments in oil exploration will increase from US$3 million (6 percent of GDP) in 2000 to US$8 million (13.5 percent of GDP) in 2002. Investments for development, construction, and equipment of oil fields are tentatively expected for the period 2003-05, on the assumptions that maritime border issues are resolved with Nigeria.

of economic and financial policies for 2000. Performance criteria and benchmarks are also set out in the memorandum (MEFP, Tables 1 and 2).

Fiscal policy

21. The program aims at reducing the overall fiscal deficit to 22 percent of GDP and at increasing the primary budget surplus—excluding foreign-financed investment— to 2.3 percent of GDP in 2000. To achieve these objectives, government revenue is to increase by 16.5 percent in 2000 to the equivalent of 20.4 percent of GDP. Expenditure is to be contained, including wages and domestically financed investments, with current primary spending declining from 15.8 percent of GDP in 1999 to 15.6 percent in 2000. The draft 2000 budget, which has been submitted to parliament on March 1, 2000, including the administrative budgets of the central bank and the water and power utility company (EMAE), is in line with these objectives.

22. **On the revenue side**, starting in January 2000, the government eliminated all export taxes, implemented a new customs tariff with three rates (5 percent, 10 percent, and 20 percent) and no zero-rate band,[18] and adjusted specific consumer taxes for refined petroleum products, alcoholic beverages, and tobacco, with the purpose of keeping the reforms revenue neutral for these three groups of merchandises. Measures taken by the government to broaden the tax base and offset the revenue shortfall expected from the implementation of the customs reform (Db 4 billion or about 1 percent of GDP) are described in the memorandum (MEFP, paragraphs 12 and 13). They include (a) conducting a census of all tax and customs exemptions and eliminating all ad hoc tax and customs duty exemptions by April 2000; (b) establishing a monitoring system of import values at customs; (c) making fully operational the computerization program at customs (SYDONIA); and (d) combating fraud and tax evasion.

23. **On the expenditure side**, the budget for 2000 keeps noninterest outlays below 19 percent of GDP, as in 1999, while providing adequately for basic health and education services. The wage bill will be contained at 7.3 percent of GDP in 2000, compared with 7.5 percent of GDP in 1999, despite the selective salary increase granted to public servants who did not benefit from the special wage scales provided under the December 1997 law governing the civil service statute (MEFP, paragraph 15). It reflects the implementation of the organizational and staffing plans in all ministries, which is expected to downsize the civil service starting in July 2000 (Box 2).

24. In 2000, priority outlays for education will increase to 8.5 percent of GDP, from 7.9 percent of GDP in 1999, and for health to 9 percent of GDP, from 8.8 percent of GDP in 1999. As indicated in the memorandum (MEFP, paragraph 16), measures will also be taken

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[18] With the new customs tariff structure, the current unweighted average tariff rate is 12 percent, down from 27 percent in 1999.

to improve the targeting and overall efficiency of social outlays, and the authorities will develop sectoral strategies with technical assistance from the World Bank. Investment expenditure will be established in accordance with the public investment program (PIP) agreed on with the World Bank, and taking into account the overall fiscal objective and the availability of project aid. The priority areas are agriculture, infrastructure, and human resource development.

25. With respect to foreign-financed **capital expenditure**, the authorities will select projects with the highest returns and closely monitor the ongoing projects, including those financed through the grant from Taiwan Province of China. The integrity of the budget will be preserved, and all public investments will be included in the budget and the PIP agreed with the World Bank. In addition, the authorities have established quarterly steering meetings on sectoral strategies and project monitoring, with donor participation, in order to introduce greater transparency, promote accountability, and strengthen project preparation and monitoring.

26. The authorities indicated their commitment to putting in place well-functioning public finance administrations and procedures. They have conducted a study on the role and missions of the Directorate of Finance, with a view to streamlining its operations and establishing separate and autonomous tax, budget, and treasury administrations. Control over expenditure commitments (including investments) will be strengthened. Finally, it is hoped that rescheduling to be sought from Paris Club and other bilateral creditors will allow for the elimination of all external payments arrears during the first year of the program. Domestic arrears are also projected to be eliminated at the same time.

Monetary and exchange rate policy

27. With the implementation of the authorities' tight monetary policy, broad money is projected to increase by 5 percent in 2000, in line with the target for end-of-year inflation. Given the fiscal program, bank credit to the government should fall substantially, allowing credit to the private sector to increase in real terms. The discount rate will be maintained above inflation, and the central bank will introduce open market operations in July 2000, with the technical assistance of the Fund resident advisor, while paying attention to the particularly high bank savings and lending rates (MEFP, paragraph 20).

28. The central bank will strengthen bank supervision and closely monitor the financial situation of the banking system, including its profitability, quality of credit portfolios, and compliance with prudential norms. The bank experiencing difficulties in complying with the central bank prudential requirements has now started discussions with a Portuguese bank with the purpose of opening up its capital to the foreign bank and implementing a

restructuring program. The central bank will closely monitor this restructuring program,[19] and the authorities will strengthen the recovery of the loans made by the national savings and loans institution (CNPC), which is in receivership; publish the list of debtors not current on their obligations to the CNPC; and initiate appropriate civil actions. They will finalize the implementation of the recommendations of the Fund technical assistance mission in the areas of internal control and audit procedures. The authorities will also conduct annual external audits of the central bank's accounts.

29. The government will continue to maintain its flexible, market-based exchange rate regime, and the central bank will cease all administrative interference in commercial banks' exchange operations, allowing for a further reduction of the spread between the official rate and the parallel rate to below 1 percent. Under the circumstances, and given the recent liberalization of external current account transactions, the mission encouraged the authorities to take all remaining actions necessary for accepting the obligations of Article VIII of the Fund's Articles of Agreement.

Structural reforms

30. São Tomé and Príncipe's prospects for sustainable growth hinge on an effective implementation of structural reforms to reduce the economy's dependence on cocoa and encourage private investment. The measures and actions set out under the program, which were prepared in collaboration with the staff of the World Bank, are described in the matrix of policy actions for the period 2000-02 and in the memorandum of economic and financial policies for 2000 (MEFP, paragraphs 24-30).

31. **Price and trade liberalization** will be pursued under the program. The government will continue to allow the petroleum product distribution company (ENCO) to implement the automatic price adjustment mechanism adopted for petroleum product prices in 1997. It will also conduct a review of the cost structure of the water and electricity utility (EMAE), with a view to adopting an automatic adjustment mechanism for water and electricity rates by end-September 2000. In addition, the government will conduct a review of the telecommunication sector, with the aim of eliminating the monopoly of the telephone company.

32. In the area of trade liberalization, in February 2000, the government eliminated all export taxes and implemented a comprehensive reform of the customs tariff structure (paragraph 22). With these trade reforms, the index of trade policy restrictiveness has been reduced further to 3 in 2000, from 5 in 1999. The government will also conduct a review of the business environment in São Tomé and Príncipe, with a view to adopting an action plan

[19] The bank restructuring and recapitalization program is at a very early stage of preparation and no quasi-fiscal costs are expected as the central bank has no claims on banks and the authorities do not intend to participate in the recapitalization.

aimed at promoting private sector investment, including through an overhaul of business legislation and regulation, and the provision of assistance to the judiciary in the area of contract enforcement. Regarding the development of free trade zones in São Tomé and Príncipe, the government has indicated that it will not be involved and will require an environmental impact study before agreeing to any development.

33. **Civil service reform** will be a key element of the program. Progress made in implementing civil service reform and wage policy will be assessed at the time of the first review of the program, particularly regarding identification of redundant staff positions and the assessment of retrenchments.

34. The program calls for the determined implementation of the government's new public enterprise reform and **privatization program** (MEFP, paragraph 25). In addition, the government will adopt a program for the privatization of large government agricultural estates and a strategy for the rationalization of the land tenure system before end-June 2000, with assistance from the World Bank, in order to increase production and reinforce investment incentives. It will also undertake a restructuring/privatization study of EMAE by end-June 2000, with the aim of deciding on its future (privatization or a contracting out of the company's management to the private sector), and will ensure that the accounts of all public enterprises are audited annually by reputable external accounting firms.

35. As regards the prospects for oil exploration, the authorities will pursue negotiations with ExxonMobil on a possible production-sharing contract in 2000 (MEFP, paragraph 26). By end-June 2000, they will prepare the oil legislation for submission to parliament, including provision of a reserve fund for future generations, and, by end-December 2000, adopt its implementing regulations, including a standard production-sharing arrangement with oil companies and measures to protect the environment, in consultation with the Fund and the World Bank. The program would aim at ensuring transparency and accountability in the conduct of oil operations, on which the government will conduct annual independent external audits.

Governance issues

36. The government has indicated its determination to strengthen transparency and good governance, and crack down on fraud and corruption, as illustrated by the treatment of fraudulent transfers of foreign currency assets uncovered in 1994, and of the treasury bond fraud attempt uncovered in February 1999 (MEFP, paragraph 28). The handling of these two fraud cases will be reassessed at the time of the first review of the program. During the program period, transparency and good governance will be enhanced through a number of new measures, such as the annual independent external audits of the accounts of the central bank, public enterprises, and oil operations, the strengthening of internal audit and inspection in the central bank, the simplification of the customs tariff structure, the elimination of ad hoc exemptions, and the strengthening of the internal audit departments of the Directorate of Finance and at customs.

The external sector, debt sustainability, and capacity to repay the Fund

37. The debt sustainability analysis, conducted jointly by the authorities and the staff of the Fund and the World Bank, concluded that São Tomé and Príncipe's debt burden was particularly heavy and would not become sustainable even after full use of traditional debt relief mechanisms.[20] The authorities have made good progress in debt management following the recent update of the debt database, with the assistance of Debt Relief International and the HIPC Capacity-Building Trust financed by bilateral donors. They indicated that they planned to pursue the reconciliation of external debt data with major creditors and to remain current on their external debt-service obligations, once reschedulable debt has been restructured.

38. Assuming a three-year flow rescheduling in 2000-02 on Naples terms involving a 67 percent reduction in the net present value (NPV) of debt to Paris Club creditors, followed by a hypothetical stock-of-debt operation at end-2002, also on Naples terms, the ratio of the NPV of public debt to exports is projected to decline from 1,450 percent in 1999 to 794 percent in 2002, and then to 543 percent in 2005 and 367 percent in 2015 (Figure 3). The ratio of public debt service to exports would decline from 45.3 percent in 1999 to 26.4 percent in 2002, and then to 20 percent by 2015. As a percentage of government revenue, the NPV of public debt would decline from 2,174 percent in 1999 to 1,286 percent in 2002, and to 792 percent in 2015; over the same period, the ratio of debt service to government revenue would decrease from 82 percent to 47.1 percent and 45.6 percent, respectively.

39. Payments to the Fund are expected to peak in 2006, when repayments and charges will total SDR 0.51 million, equivalent to 5 percent of total debt-service obligations, 2.4 percent of projected exports of goods and services, and 4.1 percent of government revenue (Table 12). São Tomé and Príncipe has fully met its debt-service obligations to the Fund in the past, in spite of a mixed overall record of payments. Given the projected improvements in its balance of payments and fiscal positions, it is expected to discharge its future obligations to the Fund in a timely manner.

40. Achieving the program's objectives for the external current account deficit will hinge critically on the ongoing efforts of export diversification. Exports are expected to increase by 11 percent on annual average during 2000-02 in current U.S. dollar terms not only due to cocoa shipments which are projected to increase following the low point reached in 1999, but to a larger extent because of the rapid expansion of tourism and travel services. The increase in imports by 13 percent would be largely financed by foreign direct investment, with growth in capital goods imports led by the start up of oil-related investments. Given the very heavy

[20] Assuming Board approval of the proposed PRGF arrangement and three years of satisfactory program implementation, São Tomé and Príncipe could reach its decision point under the enhanced Initiative for Heavily Indebted Poor Countries (HIPC Initiative) by early 2003.

external debt burden, the authorities should continue to rely on highly concessional external assistance, with a grant element of at least 50 percent. The financing requirements for 2000-02, after private capital inflows, are expected to be covered by concessional assistance from multilateral and bilateral creditors and donors, including IDA and the African Development Fund (AfDF), as well as by Fund assistance under the requested PRGF arrangement and debt relief. There still remains a residual financing gap of US$14.6 million (see Table 6 and interim PRSP, Table 3). For 2000, the financing requirements, after private capital inflows and the government's project financing, are estimated at about US$71.5 million, and the residual financing gap, after flow debt rescheduling and use of PRGF resources, at US$2.4 million (MEFP, paragraph 32).[21] In addition to a three-year flow rescheduling on Naples terms that they will request from the Paris Club once the requested PRGF arrangement has been approved, the authorities are seeking structural adjustment credits from AfDF and IDA. They also intend to organize a UNDP-sponsored donor meeting in São Tomé to help mobilize the necessary multilateral and bilateral project and nonproject support. The completion of the first review of the program will be contingent on the provision of financing assurances by the authorities for the second half of 2000.

Statistical issues

41. Technical assistance received from the Fund in the areas of monetary and balance of payments statistics, and from bilateral donors in the areas of real sector and price data, has laid the groundwork for improved data compilation and reporting. Progress has also been made in recent years in the preparation and updating of fiscal data. However, weaknesses remain in the statistical apparatus, in particular, in compiling real sector and balance of payments statistics. The government has indicated that it will take the necessary steps to improve the reliability and timeliness of statistics, regularly provide the core minimum data to the IMF for the purposes of surveillance, and strengthen program monitoring. It will also conduct a household survey and prepare a series of social and poverty indicators in the context of its poverty reduction strategy, with technical and financial support from the World Bank, AfDB, and UNDP.

Prior actions, performance criteria, benchmarks, and reviews

42. To launch the program in the best conditions, the authorities took several prior actions during October 1999-March 2000, including the following (a) the production of the report on the fraudulent transfer from the central bank's foreign assets; (b) the production of a report on the fraud attempt uncovered in February 1999 involving the issuance and trading of fraudulent treasury bonds; (c) the adoption of a new agricultural development strategy; (d) the establishment of an administrative unit responsible for government petroleum sector policy; (e) the adoption of organizational and staffing plans for the ten ministries; (f) the

[21] This residual gap applies to the second half of 2000; the first half of the program year is fully financed.

publication of a reform and privatization program for nonagricultural public enterprises; (g) the implementation of the new customs tariff, with three rates and the elimination of export taxes; and (h) the submission to parliament of a draft budget for 2000 consistent with program objectives. The report on the independent external audit of the central bank's net foreign assets accounts will also be published by end-March 2000 as a prior action

43. The program includes quantitative performance criteria for end-June and end-December 2000 on (a) the central government primary balance (excluding foreign-financed investments, cumulative); (b) net bank credit to the central government; (c) the net domestic assets of the central bank; (d) the central bank's net international reserves; there is also to be (e) a zero ceiling on the outstanding stock of nonreschedulable external payments arrears of the government; (f) a zero ceiling on the outstanding stock of short-term external credits with maturities of less than one year (excluding normal import-related credits); and (g) a zero ceiling on new nonconcessional government or government-guaranteed borrowing (with a grant element of less than 50 percent) in the case of loans with a maturity of more than one year.[22] Quantitative benchmarks on the variables above have also been established for end-March and end-September 2000. In addition, quantitative quarterly indicators are set on the following key variables: (a) total central government revenue (cumulative); and (b) primary spending, excluding foreign-financed investments, on a commitment basis (cumulative).

44. The program also includes **two structural performance criteria**: (a) the adoption of a privatization program of large government agricultural estates and a law simplifying real property and land ownership; and (b) the adoption of a mechanism by which adjustments in water and electricity rates reflect production and distribution costs; as well as four structural benchmarks: (a) the preparation of a report identifying redundant civil servants and providing the assessment of the civil service downsizing resulting from the implementation of the organizational and staffing plans; (b) the submission to parliament of a draft law on petroleum exploration and production; (c) the adoption of a three-year public investment program for 2001-03 in conformity with the program; and (d) the submission of monthly monetary data by the central bank within six weeks after the end of each month. The first two reviews of the program are scheduled to be completed by end-September 2000 and end-March 2001, respectively. At the time of the second review, quantitative performance criteria will be set for end-June and end-December 2001, as well as quantitative benchmarks for end-March and end-September 2001 and structural benchmarks and performance criteria for 2001.

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[22]The ceilings established for (b), (c), and (d) are subject to asymmetric adjusters for deviations from program assumptions in external financing, and fishing and oil concessions royalties.

IV. Staff Appraisal

45. São Tomé and Príncipe's performance under the government policy framework for 1998 and the staff-monitored program for 1999 was broadly satisfactory. Real GDP recovered and progress was made in strengthening fiscal performance, lowering inflation, liberalizing the price, trade, and exchange regime, and narrowing the spread between the official exchange rate and the parallel market rate of the currency. The government also adopted a civil service reform program, and successfully implemented an important public enterprise divestiture program.

46. Notwithstanding the satisfactory progress made in 1998-99, São Tomé and Príncipe's economic, financial, and social situation remains fragile and difficult, the debt burden relative to exports is the heaviest in the world, and the country, one of the smallest and poorest in the world, continues to depend heavily on external assistance and the monoculture of cocoa. The economy thus remains very vulnerable to terms of trade fluctuations and the availability (or lack) of foreign aid.

47. São Tomé and Príncipe needs now to consolidate the gains achieved in 1998-99 in fiscal and exchange rate stabilization, and move toward economic diversification, with a view to fostering higher growth and reducing poverty. Recent private investment in tourism and construction is leading the way regarding diversification, and the government approved a new agricultural development strategy in 1999 that aims, inter alia, at promoting new export crops and trading foodcrops in the neighboring Central African Economic and Monetary Community (CEMAC) countries. It is crucial for the authorities vigorously to pursue these efforts, develop and implement sectoral strategies in 2000 in accordance with the agreed timetable (including for tourism, education, health, and infrastructures), and adhere to the newly established PIP agreed on with the World Bank and the Fund. Finally, as intended, a full-fledged poverty reduction strategy should be prepared and implemented by end-2001, following a participatory process involving the civil society. To this end, and because the social databases are inadequate and the social and poverty indicators are not readily available, the staff would want to stress the importance for the authorities and concerned donors to conduct the necessary household surveys and poverty assessments and develop an adequate series of social and poverty indicators in a timely manner, taking account of the timetable and participatory process for the preparation of a PRSP.

48. The authorities and the civil society at large perceive the need firmly to implement vigorous macroeconomic and structural policies to improve the prospects for growth and reduce poverty. There is a widespread sense in SãoTomé and Príncipe that the country needs successfully to implement the three-year program to strengthen the authorities' track record of policy performance and qualify for debt relief and support from the international community under the enhanced HIPC Initiative. This has been illustrated by the consensus achieved among authorities, labor unions, and the three main political parties on a cautious budget and wage policy for 2000, and a comprehensive civil service reform agenda, following open consultations in December 1999-January 2000. This process has helped improve national ownership and ensure greater commitment to the successful

implementation of the program. The authorities have also implemented several prior actions before launching the program, including the adoption of a comprehensive customs tariff reform.

49. Moreover, in moving forcefully against the officers involved in the 1994 fraudulent foreign asset transfer and the treasury bond fraud case uncovered in February 1999, and in publishing the report of the independent external audit of the net foreign asset accounts of the central bank, the government has demonstrated its resolve to combat corruption, strengthen transparency in public policy, and steadfastly implement the program, a welcome move at this crucial stage when the prospects for oil development are taking shape. Under the circumstances, the staff believes that the government is committed to opening economic and social policy to public debate within civil society, and is determined to implement the agreed measures in a timely manner.

50. Nevertheless, the proposed PRGF-supported program is comprehensive and there are risks that the very limited administrative capacity in São Tomé and Príncipe could hamper implementation. The authorities will need technical and financial assistance to help prepare and implement the measures required in the areas of civil service reform, public enterprise reform and privatization, oil policy, and statistics and program monitoring, including household surveys and the development of social and poverty indicators. Success in policy implementation will also require continued determination on the part of the authorities to carry out the measures, including in the critical areas of control over expenditure commitment, tax and customs administration, full implementation of the civil service reform program, public enterprise reform and privatization, good governance and transparency in public finance, central bank, and oil operations. Progress in these policy areas will provide further tests of the resolve and ability of the authorities to carry out a comprehensive program.

51. In addition, the authorities should strictly adhere to the fiscal policy stance agreed for 2000, closely monitor ongoing projects, including those financed through the special grant from Taiwan Province of China, and preserve the integrity of the budget by including all public investments in the budget and the PIP discussed with the Fund and the World Bank. In this regard, it is essential to contain primary expenditure, including the wage bill and domestically financed public investment, while providing adequately for education and health, and to remain current on nonreschedulable external debt-service obligations falling due in 2000. In the banking sector, the central bank should continue closely to monitor lending activities and bank portfolio performance, and remain vigilant in framing and implementing the recapitalization and restructuring program needed for the one bank that has been experiencing difficulty since the second half of 1999.

52. The staff urges the authorities successfully to implement the PRGF-supported program in 2000-02 as intended and thus establish the three-year track record of policy performance needed for the country to qualify for assistance under the enhanced HIPC Initiative, with a decision point by early 2003. There also is an urgent need to improve the quality and timeliness of external debt data.

53. With the reduction below 1.5 percent of the spread between the official rate and the parallel market rate, and the commitment of the central bank to cease administrative interference in commercial banks' exchange operations and to compute the official rate as an average of the rates of the parallel, bureau de change, and commercial bank markets, São Tomé and Príncipe exchange rate level appears to be appropriate. In addition, the authorities liberalized external current account transactions in 1999. Following a review of the new law on foreign exchange, the staff will urge the authorities to take the remaining steps required, with a view to accepting the obligations of Article VIII as soon as possible.

54. It is recommended that the next Article IV consultation with São Tomé and Príncipe be held on the standard 12-month cycle.

V. Proposed Decision

55. In view of the foregoing, the following draft decision is proposed for adoption by the Executive Board:

São Tomé and Príncipe: Request for a Three-Year PRGF Arrangement

1. The government of São Tomé and Príncipe has requested a three-year arrangement under the Poverty Reduction and Growth Facility.

2. The Fund notes the interim Poverty Reduction Strategy Paper for São Tomé and Príncipe set forth in EBD/00/--.

3. The Fund approves the arrangement set forth in EBS/00/58.

Box 1. Poverty Assessment

Poverty is widespread in São Tomé and Principe and has worsened dramatically in recent years. As indicated in the interim PRSP, the proportion of the population living under the poverty line (an income of less than US$220 per year) was estimated at 40 percent in 1994 and that of the population lived in extreme poverty (an income of less than US$171 per year, a level insufficient to cover 50 percent of minimum household food requirements). With rapid inflation and steep nominal depreciation of the currency through 1997, income per capita dropped from US$365 in 1994 to US$295 in 1999, considerably reducing the purchasing power of São Tomé and Príncipe's households and leading to a further worsening of the poverty situation. The latest population census (1991) identified three main categories of poor people: plantation workers (21 percent of population at that time), female-headed households (35 percent), and isolated old people.

In addition, with a particularly heavy and unsustainable public external debt burden, social spending fell from 11.5 percent of GDP in 1995 to 4.5 percent of GDP in 1998 for education, while fluctuating from 6.4 percent of GDP in 1995 to 10.2 percent of GDP in 1997 and 7.3 percent of GDP in 1998 for health, reflecting the volatility of disbursements in external project assistance. The compounded adverse impact of the worsening economic situation and reduction in social spending has been reflected in the steady deterioration of available social indicators. Health and nutrition conditions worsened, as witnessed by the rise in infant mortality from 50 per thousand of live births in 1996 to 65 per thousand in 1999; total mortality rate increased from 8.3 per thousand in 1996 to 8.5 per thousand in 1997 and about 78 percent of the population lacked adequate sanitation facilities in 1996. Malaria remains the leading cause of mortality and morbidity. Vaccination coverage also declined during 1996-99 for diphtheria (from 74 to 69 percent of children age 12 to 23 months), polio (from 79 to 69 percent) and measles (from 88 to 69 percent). Malnutrition is believed to be widespread among women and pre-school children. About 17 percent of children under 5 years of age would suffer from malnutrition.

Although still superior to most other sub-Saharan African countries, education indicators have sharply deteriorated in the last decade. Gross primary enrollment decreased from 82.5 percent of the school-age population in 1990 to 60 percent in 1996 and was brought back to 70 percent in 1999. The quality of education has also declined as a result of insufficient classrooms, textbooks, and qualified teachers (only 45 percent of teachers would have proper qualifications). As a result of the scarcity of teachers and classrooms, classes are conducted in double or triple shifts, and children can attend only 4 hours of class per day.

The interim PRSP prepared by the authorities is based on achieving a sustainable growth in income per capita and on the implementation of measures designed to improve the living conditions of the most vulnerable groups of the population. The strategy set by the authorities gives priority to restoring an adequate delivery of public education and health services. It was developed following an initial consultation with civil society and with assistance from the staff of the Fund and the World Bank. The interim PRSP identifies increased public management capacity and good governance as critical factors for achieving the authorities' poverty reduction objectives. The full PRSP, which is expected to be completed by end-March 2001, will be prepared through an open participatory process.

Box 2. Civil Service Reform and Wage Policy

To improve efficiency in public administration, the authorities will implement the new organizational and staffing plans for all ministries, starting in March 2000, reduce the size of the civil service (about 4,000 agents), prepare a new compensation and promotion system based on performance, and effectively contain the wage bill. They believe that a small number of well motivated staff can more effectively carry out the missions of the public administration than a large group of less motivated civil servants.[1] More specifically, the authorities have already suspended the application of the law on the statute of the civil service adopted in December 1997, abrogated the decree on pre-retirement, as of January 2000, and strictly enforced the rules governing retirement. In addition, they will:

(a) identify redundant staff positions and assess the civil service downsizing that will result from the implementation of the organizational and staffing plans by end-April 2000;

(b) establish a single computerized system for civil service and payroll management, also by end-June 2000;[2]

(c) limit new recruitments to 90 in 2000, all of whom are teachers for the elementary schools;

(d) adopt a new compensation scheme and salary scale for the civil service based on performance, and revise the law on the civil service statute, by end-December 2000.

The authorities intend to assess progress made in implementing their civil service reform and wage policy at the time of the discussions of the first review of the program in July 2000.

With the implementation of this wage policy, the wage bill will increase by 7.4 percent in 2000, the same rate as average annual inflation, and be contained at 7.3 percent of GDP (0.2 percentage point below the level of 1998-99).

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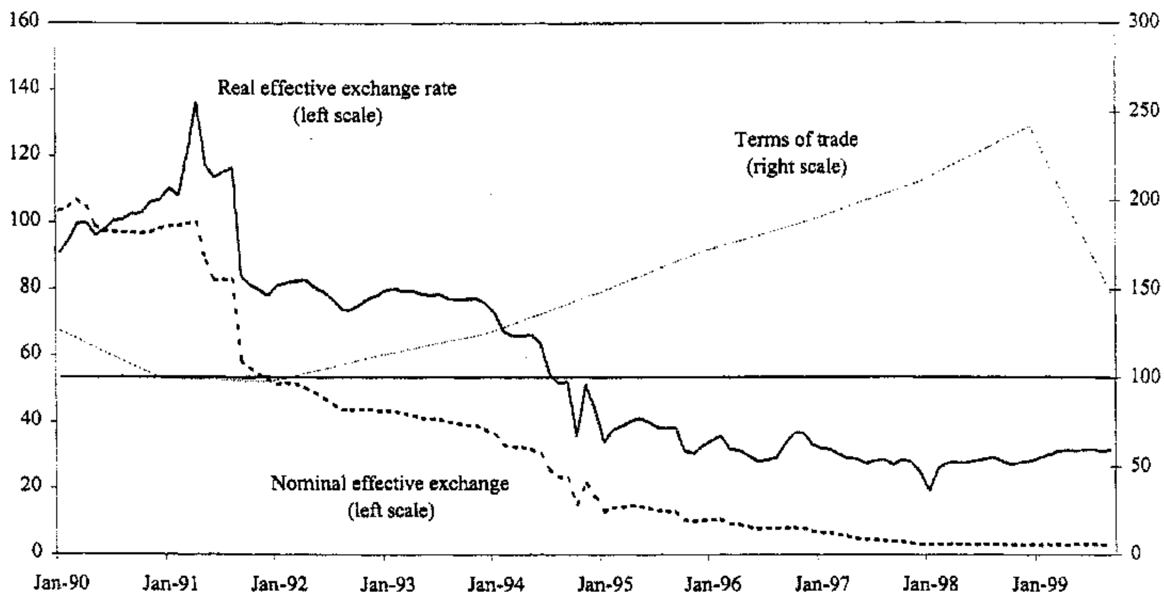
[1] The authorities have implemented a selective salary increase averaging Db 80,000 (about US$12) in February 2000 for 1,100 civil servants that did not benefit from the December 1997 law on the civil service statute and the special wage scales.

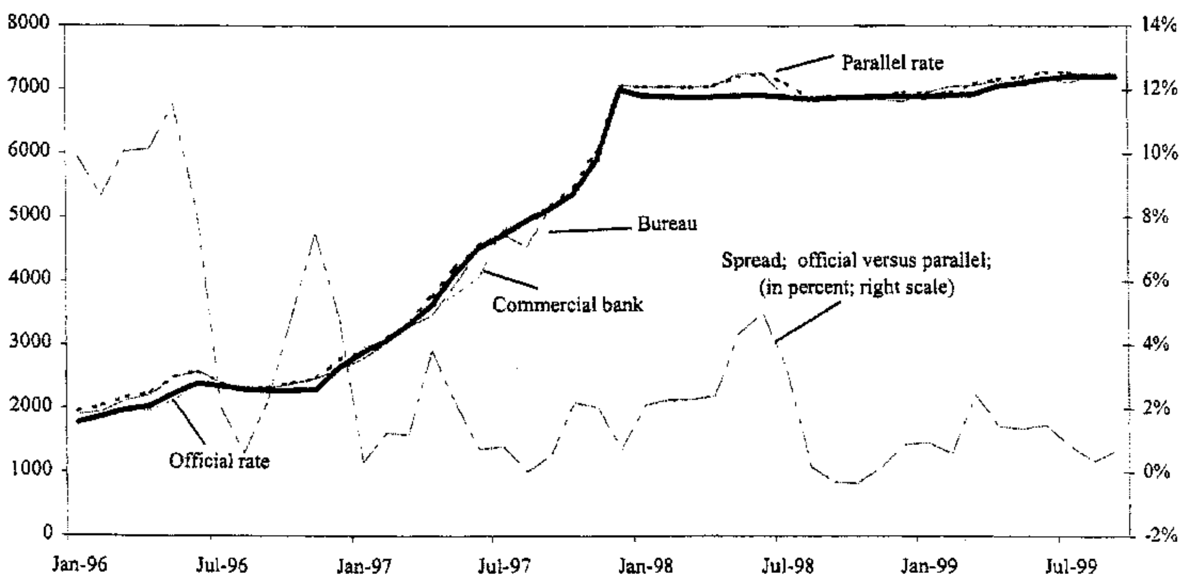
[2] The amount of the severance package for each retrenched civil servant will be equivalent to the base salary multiplied by the number of year spent in the civil service.

Figure 1. São Tomé and Príncipe: Exchange Rates and Terms of Trade, 1990-99

Effective Exchange Rate and Terms of Trade, January 1990- September 1999
(Index, 1990=100)

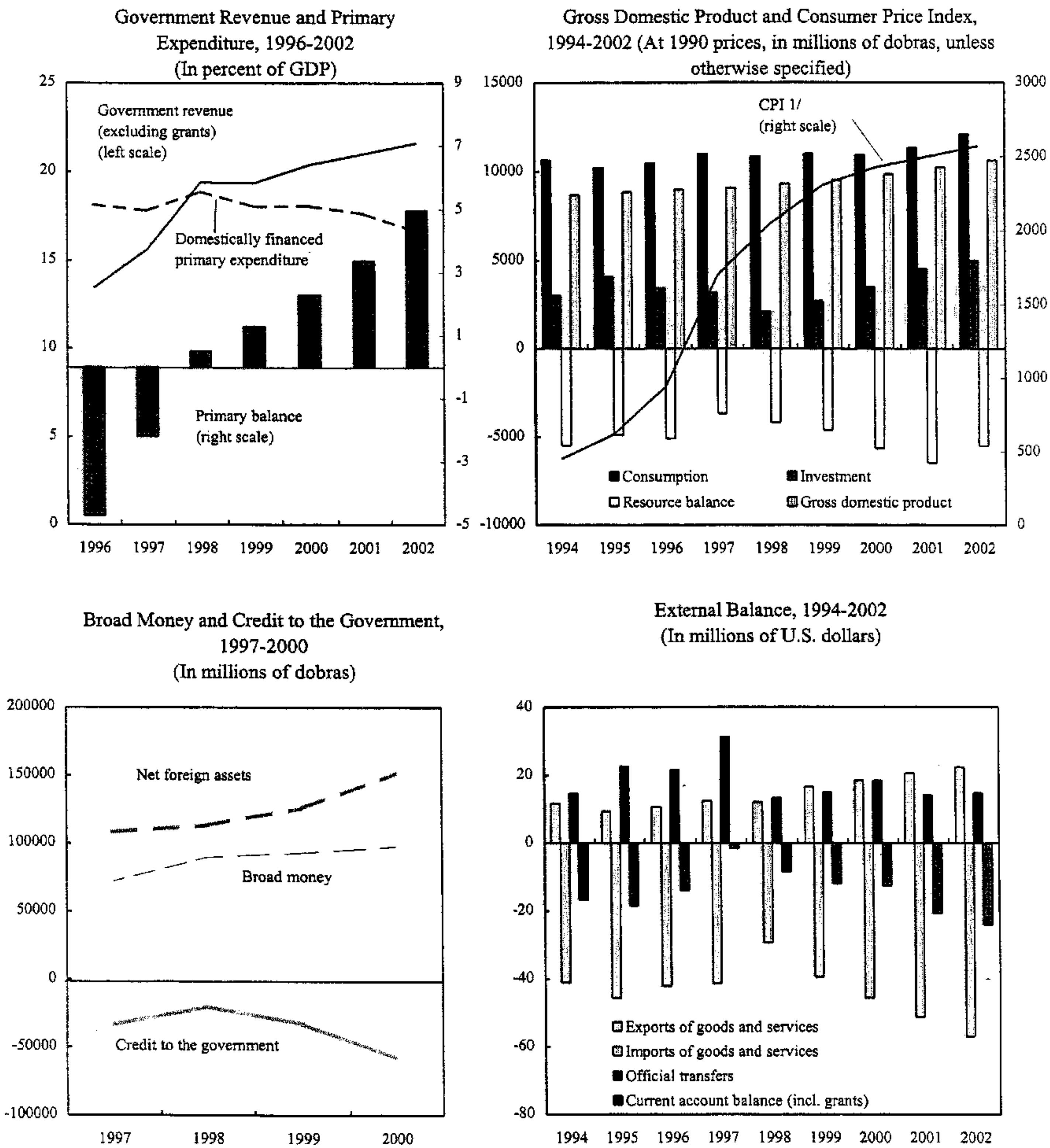


Average Exchange Rates, January 1996-September 1999
(Dobras per U.S. dollar, unless otherwise indicated)



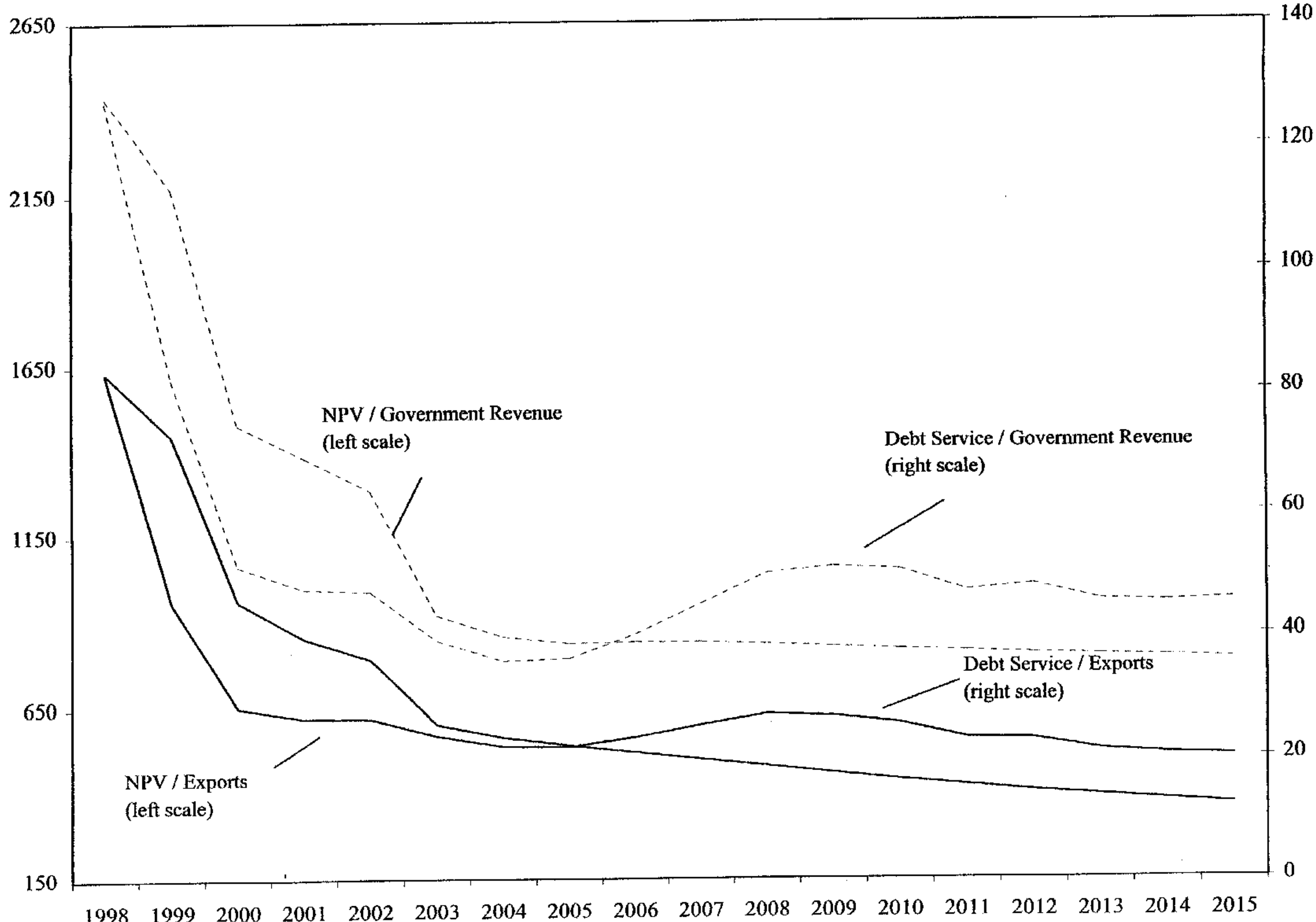
Sources: São Tomé and Príncipe authorities; IMF, World Economic Outlook database; and staff estimates.

Figure 2. São Tomé and Príncipe: Economic and Financial Indicators, 1994-2002



1/ Consumer price index, end-December, 1990=100.

Figure 3. São Tomé and Príncipe: External Debt Indicators, 1998-2015 1/



Sources: São Tomé and Príncipe authorities and staff projections.

1/ Assuming the full use of traditional debt relief mechanisms.

Table 1. São Tomé and Príncipe: Fund Position, 1999-2002

	Outstanding on Sep. 30, 1999	1999 Oct.-Dec.	2000 Jan.-Mar.	2000 Apr.-Jun.	2000 Jul.-Sep.	2000 Oct.-Dec.	2000 Year	2001	2002
				(In millions of SDRs)					
Transactions during the period (net)		0.000	0.951	0.000	0.951	0.000	1.902	1.902	1.902
Poverty Reduction and Growth Facility (net)		0.000	0.951	0.000	0.951	0.000	1.902	1.902	1.902
Disbursements		0.000	0.951	0.000	0.951	0.000	1.902	1.902	1.902
Repayments		0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Total Fund credit outstanding (end of period)	0.000	0.000	0.951	0.951	1.902	1.902	1.902	3.804	5.706
Poverty Reduction and Growth Facility	0.000	0.000	0.951	0.951	1.902	1.902	1.902	3.804	5.706
				(In percent of quota)					
Total Fund credit outstanding (end of period)	0.0	0.0	12.9	12.9	25.7	25.7	25.7	51.4	77.1
Enhanced Structural Adjustment Facility	0.0	0.0	12.9	12.9	25.7	25.7	25.7	51.4	77.1

Sources: IMF, Treasurer's Department; and staff projections.

Table 2. São Tomé and Príncipe: Schedule of Disbursements
Under the Proposed PRGF Arrangement

Amount (In millions of SDRs)	Availability Date	Conditions for Purchase 1/
0.951	April --, 2000	Executive Board approval
0.951	September 15, 2000	Observance of quantitative and structural performance criteria as of June 30, 2000, and completion of the first review under the program
0.951	March 15, 2001	Observance of quantitative and structural performance criteria as of December 31, 2000, and completion of the second review under the program
0.951	September 15, 2001	Observance of quantitative and structural performance criteria as of June 30, 2001, and completion of the third review under the program
0.951	March 15, 2002	Observance of quantitative and structural performance criteria as of December 31, 2001, and completion of the fourth review under the program
0.951	September 15, 2002	Observance of quantitative and structural performance criteria as of June 30, 2002, and completion of the fifth review under the program
0.951	March 15, 2003	Observance of quantitative and structural performance criteria as of December 31, 2002, and completion of the sixth review under the program

Source: International Monetary Fund, Treasurer's Department.

1/ Other than generally applicable conditions under the arrangement, including the performance clause on the exchange and trade system.

Table 3. São Tomé and Príncipe: Quantitative Benchmarks for the 1999 Staff-Monitored Program

(In millions of dobras, unless otherwise specified)

	1997	1998	1999									
	Actual	Actual	March		June		September			December		
			SMP	Actual	SMP	Actual	SMP		Est.	SMP		Proj.
							Original	Adj. 1/		Original	Adj. 1/	
1. Floor on primary balance of the central government's financial operations, excluding foreign-financed investments (cumulative from beginning of year) 1/ 2/	-4,377	1,945	43	249	3,123	2,150	5,827	-159	208	9,354	4,252	4,327
2. Floor on total central government revenue (cumulative from beginning of year) 1/	31,245	54,502	10,133	12,732	25,032	30,104	40,188	34,202	44,878	66,310	61,208	64,605
3. Ceiling on primary spending of the central government, excluding foreign-financed investments (cumulative from beginning of year) 2/	35,790	53,076	10,090	12,720	21,908	27,954	34,361	34,361	44,671	56,956	56,956	60,279
4. Ceiling on changes in net bank credit to the central government (cumulative from beginning of year) 1/ 3/	-34,874	6,270	8,302	8,882	-4,844	-3,797	-25,980	1,145	-8,907	-44,660	3,611	-12,796
5. Ceiling on central government's outstanding external payments arrears (in millions of U.S. dollars) 4/	5	6	6	0	6	0	6	6	0	6	6	0
6. Ceiling on contracting and guaranteeing new nonconcessional borrowing by the central government with a maturity of more than one year (cumulative from beginning of year; in millions of U.S. dollars) 5/	0	0	0	0	0	0	0	0	0	0	0	0
7. Ceiling on changes in the central government's outstanding stock of short-term external credit with a maturity of less than one year (cumulative from beginning of year)	0	0	0	0	0	0	0	0	0	0	0	0
8. Floor on changes in the net international reserves position of the central bank (cumulative from beginning of year) 1/ 6/	47,757	13,584	-8,669	-14,867	3,038	-2,072	27,062	-508	11,155	47,244	-1,027	15,249
Memorandum items:												
Exceptional financial assistance (cumulative from beginning of year)	29,970	0	0	0	0	0	21,584	0	0	43,169	0	0
Fishing royalties (cumulative from beginning of year)	3,471	5,204	0	0	0	0	5,986	445	445	5,986	884	884

1/ The ceiling or the floor has been adjusted downward (or upward) to accommodate the negative deviation between actual and projected disbursements of exceptional financial assistance and receipts of fishing royalties.

2/ Based on a definition of expenditure excluding all interest payments and investment financed by foreign loans and grants.

3/ Program targets for 1999 have been adjusted to reflect liquidation proceeds from the Caixa Nacional de Poupança e Crédito.

4/ Arrears to multilateral organizations. Nonaccumulation of new external payments arrears to multilateral organizations is a continuous performance criterion.

5/ With a grant element of less than 50 percent.

6/ Excluding deposits at the National Bank of Angola.

Table 4. São Tomé and Príncipe: Structural Benchmarks for the 1999 Staff-Monitored Program

	Measures	Timetable	Status
1.	Creation of administrative unit responsible for enforcing government policy in the oil sector.	End-March 1999	Implemented in June 1999
2.	Adoption of timetable for implementation of the administrative reform and civil service downsizing program.	End-April 1999	Adopted in June 1999
3.	Adoption of organizational and staffing plans for the first group of four ministries.	End-June 1999	Adopted in October 1999
4.	Adoption of new public enterprise privatization program.	End-June 1999	Adopted in October 1999
5.	Adoption of strategy for the privatization of large government agricultural estates and the rationalization of the land tenure system.	End-December 1999	Not observed
6.	Adoption of organizational and staffing plans for the second group of six ministries.	End-December 1999	Observed
7.	Preparation of action plan against poverty.	End-December 1999	Interim PRSP adopted in January 2000
8.	Submission of monthly monetary data within six weeks of the end of each month.	Continuous	Observed

Table 5. São Tomé and Príncipe: Selected Economic Indicators, 1996-2002

	1996	1997	1998	1999		2000	2001	2002
			Est.	SMP	Est.		Program	
			(In units indicated)					
Production								
Cocoa export volume (in thousands of metric tons)	3.2	2.8	3.8	3.5	3.3	3.8	4.0	4.1
Cocoa export unit value (in U.S. dollars per kilogram)	1.5	1.6	1.7	1.6	0.9	1.1	1.3	1.4
Gross domestic product (in millions of dobras)	98,900	200,000	281,000	334,109	334,109	369,533	408,654	441,896
At constant prices (percentage change)	1.5	1.0	2.5	2.5	2.5	3.0	4.0	4.1
Gross domestic product deflator (percentage change)	50.8	100.2	37.1	16.0	16.0	7.4	6.3	4.0
Consumer prices (percentage change; end of period)	51.7	81.1	20.8	10.0	12.6	5.0	3.0	3.0
Consumer prices (percentage change; average)	42.0	69.0	42.1	14.9	16.3	7.4	4.3	3.0
			(Annual percentage change, unless otherwise specified)					
External sector								
Exports, f.o.b.	-3.1	8.1	-11.2	10.1	-17.3	28.5	21.3	14.4
Imports, c.i.f.	-16.4	-3.2	-12.3	31.5	28.5	25.2	17.3	15.7
Exchange rate (in dobras per U.S. dollar; period average)	2,203.0	4,552.5	6,927.4	9,150.0	7,092.6	...	...	...
Exchange rate (in dobras per U.S. dollar; end of period)	2,833.0	6,969.7	6,885.0	9,214.6	7,300.2	...	...	...
Real effective exchange rate	1.4	-25.0	13.1	...	12.8	...	...	...
Terms of trade	8.6	11.4	14.8	2.7	-52.0	10.6	24.9	13.1
Money and credit (end of period)								
Net domestic assets 1/	28.2	-131.7	17.7	-50.2	-10.6	-22.8	...	...
Credit to government (net) 1/	59.1	-113.4	18.2	-54.8	-14.3	-27.2	...	...
Credit to the economy 1/	-28.2	-3.8	14.9	5.6	10.5	4.3	...	...
Broad money	82.2	94.5	24.5	19.5	3.6	5.0	...	...
Velocity (ratio of GDP to average broad money)	3.4	3.7	3.5	3.4	3.7	3.9	...	...
Central bank discount rate (in percent; end of period)	35.0	55.0	29.5	...	17.0	...	...	...
Commercial bank lending rate (in percent; end of period)	38.0 to 42.0	56.0 to 62.0	42.0 to 48.0	...	30.0 to 40.0	...	...	...
Commercial bank deposit rate (in percent; end of period)	30.0 to 36.0	37.5 to 46.0	30.0 to 35.0	...	18.0 to 24.0	...	...	...
			(In percent of GDP, unless otherwise specified)					
National accounts								
Consumption	113.7	116.5	107.0	110.8	108.5	104.9	97.0	97.7
Gross investment	56.2	49.1	35.8	52.5	40.0	49.3	59.3	61.2
Public investment	29.2	22.1	19.8	29.8	26.0	23.3	31.1	30.8
Private investment	27.0	27.0	16.0	22.7	14.0	26.0	28.2	30.5
Of which: oil sector	0.0	0.0	0.0	0.0	0.0	6.0	9.2	13.5
Gross domestic savings	-13.7	-16.5	-7.0	-10.8	-8.5	-4.9	3.0	2.3
Public savings	-14.3	-17.3	-7.7	-16.5	-11.9	-11.8	-2.5	-0.9
Private savings	0.5	0.9	0.7	5.7	3.3	7.0	5.5	3.3
Gross national savings	25.0	45.5	14.7	38.5	14.6	24.0	21.2	20.2
Government budget								
Total revenue and grants	37.0	43.4	29.1	42.2	43.9	46.5	46.2	46.8
Of which: grants	23.5	27.8	9.7	22.4	24.6	26.2	25.2	25.2
Total expenditure	69.1	70.1	59.6	67.9	69.8	68.1	64.5	62.5
Of which: noninterest current expenditure	17.2	16.6	16.3	15.6	15.8	15.6	14.9	13.9
Overall balance (commitment basis)	-32.2	-26.7	-30.5	-25.6	-25.8	-21.5	-18.2	-15.7
Primary balance (commitment basis) 2/	-4.7	-2.2	0.7	2.8	1.3	2.3	3.4	5.0
External sector								
Current account balance (excluding official transfers)	-79.3	-74.8	-53.9	-63.3	-57.2	-62.1	-64.0	-66.2
Current account balance (including official transfers)	-30.8	-3.6	-21.1	-14.0	-25.4	-25.2	-38.1	-41.0
Total external debt outstanding 3/	590.0	608.5	721.3	...	636.0	...	...	...
Net present value of total debt 3/	343.0	408.4	471.8	...	420.4	...	...	...
Net present value of total debt 3/ 4/	1,446.0	1,441.9	1,634.6	...	1,450.1	...	...	...
			(In millions of U.S. dollars, unless otherwise specified)					
External sector								
Export earnings	4.9	5.3	4.7	7.0	3.9	5.0	6.1	7.0
Of which: cocoa	4.8	4.6	4.6	5.4	2.9	4.0	5.0	5.8
Overall balance	-4.8	1.1	-6.3	2.6	-2.3	-0.8	-6.6	-9.0
Outstanding medium- and long-term debt	234.0	235.5	244.9	...	248.0	...	...	...
Of which: arrears	29.3	29.6	32.6	...	27.7	...	...	...
Gross foreign reserves (in months of following year's imports of goods and nonfactor services)	1.5	5.1	3.0	4.3	3.0	4.0	4.2	5.6
External debt service								
Before debt relief 4/	73.5	71.8	83.1	59.8	49.7	43.6	39.7	48.2
Actual debt service paid 4/	26.6	19.7	46.8	...	23.6	...	...	...

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ In percent of broad money at beginning of period.
2/ Excluding interest obligations, grants, and foreign-financed capital outlays.
3/ Beginning in 1998, includes arrears to Italy -- a loan that remains in dispute.
4/ In percent of exports of goods and services.

Table 6. São Tomé and Príncipe: Balance of Payments, 1996-2002

(In millions of U.S. dollars, unless otherwise specified)

	1996	1997	1998	1999		2000	2001	2002
			Est.	SMP	Est.	Program		
Trade balance	-14.9	-13.9	-12.1	-16.8	-17.7	-22.1	-25.7	-29.8
Exports, f.o.b.	4.9	5.3	4.7	7.0	3.9	5.0	6.1	7.0
Cocoa	4.8	4.6	4.6	5.4	2.9	4.0	5.0	5.8
Other	0.2	0.8	0.2	1.6	1.0	1.1	1.1	1.2
Imports, f.o.b.	-19.8	-19.2	-16.8	-23.8	-21.6	-27.1	-31.8	-36.8
Food	-4.7	-3.8	-4.3	-7.7	-4.8	-4.8	-4.9	-4.9
Investment goods	-5.9	-5.6	-8.2	-8.2	-10.8	-15.5	-20.4	-25.0
Of which: petroleum related	0.0	0.0	0.0	-2.0	0.0	-2.5	-4.2	-6.6
Petroleum products	-3.0	-3.8	-1.9	-2.1	-3.4	-4.1	-3.6	-3.6
Other	-6.2	-6.0	-2.5	-5.8	-2.6	-2.6	-2.8	-3.1
Services and income (net)	-21.2	-19.8	-10.3	-13.2	-9.8	-9.6	-9.6	-9.6
Exports of services	5.7	7.1	7.3	7.8	12.6	13.4	14.4	15.4
Travel and tourism	3.0	4.0	4.1	5.0	9.2	9.9	10.6	11.4
Other services	2.7	3.1	3.2	2.8	3.4	3.6	3.8	4.0
Imports of nonfactor services	-22.2	-22.1	-12.6	-16.2	-17.7	-18.4	-19.4	-20.2
Freight and insurance	-5.0	-5.1	-4.2	-5.9	-4.5	-6.0	-7.0	-8.1
Technical assistance	-9.5	-10.0	-2.8	-4.9	-7.4	-6.7	-6.4	-5.8
Other	-7.7	-7.0	-5.5	-5.4	-5.8	-5.8	-6.0	-6.3
Interest due	-4.7	-4.8	-5.0	-4.8	-4.7	-4.6	-4.5	-4.9
Private transfers (net)	0.5	0.8	0.5	0.6	0.6	0.6	0.4	0.6
Current account, excluding official transfers	-35.6	-32.9	-21.8	-29.4	-26.9	-31.0	-34.9	-38.8
Official transfers (net)	21.6	31.3	13.3	22.9	15.0	18.4	14.1	14.8
Public investment projects	9.9	12.0	3.9	8.9	9.3	11.0	12.0	13.0
Aid in kind	0.5	2.8	1.5	1.4	2.4	1.8	1.8	1.8
Stabilization System for Export Earnings grants	0.8	0.2	0.1	0.1	0.0	0.0	0.0	0.0
Other	10.3	16.3	7.8	12.5	3.4	5.7	0.3	0.0
Current account, including official transfers	-14.0	-1.6	-8.5	-6.5	-12.0	-12.6	-20.8	-24.1
Medium- and long-term capital (net)	11.8	2.7	5.5	9.2	9.6	11.8	14.2	15.1
Project loans	8.6	6.2	5.4	9.8	9.6	8.2	8.7	9.1
Nonproject loans	3.7	0.0	0.0	0.0	0.0	...	...	...
Direct foreign investment	2.4	0.4	4.2	3.3	3.0	6.8	9.0	12.0
Of which: petroleum related	0.0	0.0	0.0	2.0	0.0	3.0	5.0	7.9
Amortization	-2.9	-3.9	-4.1	-3.9	-3.1	-3.2	-3.6	-5.9
Short-term capital and errors and omissions	-2.6	0.0	-3.2	0.0	0.0	0.0	0.0	0.0
Overall balance	-4.8	1.1	-6.3	2.7	-2.3	-0.8	-6.6	-9.0
Financing	4.8	-1.1	6.2	-71.7	2.3	-60.7	-0.2	-1.5
Change in reserves (increase -)	0.1	-7.4	2.7	-6.6	-1.5	-5.8	-2.8	-4.1
Medium- and long-term arrears (net; decrease -)	5.0	6.5	4.4	-32.9	-3.5	-27.7	0.0	0.0
Short-term arrears (net; decrease -)	0.0	0.0	0.0	-31.8	0.0	-29.5	0.0	0.0
Poverty Reduction and Growth Facility (net)	-0.2	-0.2	-0.2	-0.1	-0.1	2.6	2.6	2.6
Other	0.0	0.0	-0.7	-0.3	-0.3	-0.3	0.0	0.0
Debt relief	0.0	0.0	0.0	0.0	7.8	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	69.1	0.0	61.5	6.8	10.5
To be covered by debt relief	0.0	0.0	0.0	69.1	0.0	59.1	1.6	3.5
Residual gap	0.0	0.0	0.0	0.0	0.0	2.4	5.2	7.0
Memorandum items:								
Exchange rate (in dobras per U.S. dollars, average)	2,203	4,553	6,927	...	7,093	...	...	...
GDP (in millions of dobras)	98,900	200,000	281,000	334,109	334,109	369,533	408,654	441,896
Debt-service ratio (before debt relief) 1/ 2/	73.5	71.8	83.1	59.8	49.7	43.6	39.7	48.2
Debt-service ratio (after debt relief) 3/	26.6	19.7	46.8	...	23.6	...	...	...
Debt service actually paid 1/ 3/	26.6	19.7	46.8	...	23.6	...	...	..
Current account excluding official transfers (in percent of GDP)	-79.3	-74.8	-53.9	-63.3	-57.2	-62.1	-64.0	-66.2
Current account including official transfers (in percent of GDP)	-30.8	-3.6	-21.1	-14.0	-25.4	-25.2	-38.1	-41.0
Gross reserves (in millions of US dollars)	5.0	12.4	9.7	16.3	11.2	17.0	19.9	24.0
Gross reserves (in months of following year's imports)	1.5	5.1	3.0	4.3	3.0	4.0	4.2	5.6

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ In percent of exports of goods and services

2/ Includes amortization to the IMF; excludes arrears.

3/ Includes obligations to the IMF and net changes in arrears.

Table 7. São Tomé and Príncipe: Financial Operations of the Central Government, 1997-2002

	1997	1998	1999 Jan.-Dec. SMP	1999 Jan.-Dec. Actual	2000 Jan.-Mar. Program	2000 Jan.-Jun. Program	2000 Jan.-Sep. Program	2000 Jan.-Dec. Program	2001 Program	2002 Program
					(In millions of dobras)					
Total revenue and grants	86,773	81,747	141,038	146,769	40,579	80,173	120,766	171,934	188,985	206,661
Total revenue	31,245	54,502	66,310	64,605	17,480	33,973	51,466	75,277	85,817	95,450
Tax revenue	21,236	36,635	47,443	54,055	12,922	27,929	43,028	60,420	68,756	78,109
Consumption taxes	4,186	9,280	14,292	14,644	3,800	7,500	12,750	17,424	19,794	22,487
Import taxes	4,701	10,114	13,146	18,259	4,911	8,996	14,500	20,676	23,488	26,683
Export taxes	1,874	2,956	3,022	1,754	0	0	0	0	0	0
Profit taxes	4,810	6,074	6,440	7,147	1,981	5,987	7,947	10,485	11,911	13,531
Personal income taxes	4,090	5,468	7,611	4,785	1,382	3,554	5,287	7,953	9,114	10,354
Other taxes	1,575	2,743	2,932	7,466	848	1,891	2,544	3,882	4,449	5,054
Nontax revenue	10,009	17,867	18,867	10,551	4,558	6,044	8,438	14,858	17,061	17,341
Of which: transfers from enterprises	2,058	4,085	6,564	4,844	884	1,921	2,870	5,112	5,654	6,253
fishing royalties	3,471	5,204	5,986	884	2,473	2,923	3,368	4,889	...	...
Grants	55,528	27,245	74,727	82,163	23,100	46,200	69,299	96,657	103,168	111,211
Of which: nonproject grants	2,044	0	10,900	14,662	6,500	8,533	10,816	12,936	13,130	13,195
Total expenditure and net lending	140,174	167,518	227,771	233,059	63,571	122,189	183,800	251,554	263,540	276,216
Current expenditure	55,675	80,709	87,738	90,747	24,015	43,927	65,112	92,856	96,920	98,013
Of which: noninterest current expenditure	33,151	45,899	52,060	52,914	12,530	24,861	37,110	57,778	60,951	61,530
Personnel costs	11,709	18,930	21,755	25,223	7,772	13,418	19,860	27,088	28,606	28,723
Goods and services	7,004	9,240	10,294	12,722	1,963	5,448	6,705	10,540	11,445	11,668
Interest on external debt due	22,356	33,667	34,535	36,691	11,198	18,494	27,145	33,935	34,826	35,339
Interest on internal debt due	168	1,143	1,143	1,143	286	572	857	1,143	1,143	1,143
Transfers	8,892	8,441	9,412	6,141	552	1,614	3,604	7,376	8,009	8,421
Other	4,950	8,438	9,899	7,619	2,024	3,971	6,512	11,774	11,785	11,522
Of which: defense	1,630	655	1,123	1,099	278	818	1,285	1,752	...	...
Redeployment fund	596	850	700	1,209	218	409	429	1,000	1,106	1,196
Capital expenditure	84,499	87,328	138,961	141,430	39,706	78,562	119,138	159,298	166,619	178,204
Financed by the treasury	2,471	7,177	4,896	7,365	3,400	6,250	7,200	9,000	11,043	11,941
Financed by extraordinary funds	0	15,557	0	0	0	0	0	0	0	0
Financed by external sources	82,028	64,594	134,065	134,065	36,306	72,312	111,938	150,298	155,577	166,263
Net lending 1/	0	-519	1,072	881	-150	-300	-450	-600	0	0
Overall fiscal balance (commitment basis, including grants)	-53,401	-85,771	-86,733	-86,290	-22,991	-42,016	-63,035	-79,620	-74,554	-69,555
Change in arrears (net; reduction -)	20,979	21,110	0	24,486	0	-72,939	-72,939	-72,939	0	0
External arrears (net; reduction -)	17,566	24,523	0	24,486	0	-72,939	-72,939	-72,939	0	0
Domestic arrears (net; reduction -)	3,413	-3,413	0	0	0	0	0	0	0	0
Overall fiscal balance (cash basis)	-32,423	-64,661	-86,733	-61,804	-22,991	-114,955	-135,973	-152,558	-74,554	-69,555
Financing	32,423	64,661	-410,429	61,804	19,548	-311,092	-309,005	-301,752	23,383	-9,620
External (net)	53,358	14,873	-380,158	53,108	11,237	-328,443	-317,438	-313,436	38,509	23,579
Disbursements (projects)	28,544	37,349	70,238	72,238	19,706	34,646	51,185	60,903	65,539	68,246
Special grant	29,970	0	43,169	0	0	0	0	0	0	0
Amortization (net)	-5,156	-22,476	-493,565	-72,820	-8,470	-363,088	-368,623	-374,339	-27,030	-44,667
Scheduled	-17,794	-27,432	-28,060	-24,774	-8,470	-14,415	-19,950	-25,666	-27,030	-44,667
Net change in arrears (reduction -)	12,638	4,956	-465,505	-48,046	0	-348,673	-348,673	-348,673	0	0
Debt relief 2/	0	0	0	53,690	0	0	0	0	0	0
Domestic (net)	-20,935	49,788	-30,270	8,696	8,311	17,350	8,433	11,684	-15,126	-33,199
Bank net credit	-34,874	6,270	-44,660	-12,796	8,311	2,704	-6,213	-25,276	-15,126	-33,199
Privatization proceeds	0	15,809	0	0	0	0	0	0	0	0
Oil concession rights proceeds	13,939	27,709	14,390	21,492	0	14,646	14,646	36,960	0	0
Financing gap 3/	0	0	497,162	0	3,444	426,047	444,979	454,310	51,171	79,175
To be covered by debt relief 3/	0	0	472,700	0	3,443	426,047	432,769	436,818	12,005	26,156
Residual gap	0	0	24,462	0	0	0	12,209	17,492	39,166	53,019
Memorandum items:										
Domestically financed primary expenditure	35,790	53,076	56,956	60,279	15,930	31,111	44,310	66,778	71,994	73,471
Primary balance (commitment basis)	-4,377	1,945	9,354	4,327	1,549	2,863	7,156	8,499	13,823	21,978
Quasi-fiscal balance of the central bank	-3,332	2,604	1,310	274	...	...	...	0	0	0
External debt-service cash payments	9,946	31,620	30,938	31,335	12,031	24,958	31,453	36,413	49,140	51,562
					(In percent of GDP, unless otherwise indicated)					
Memorandum items:										
Total revenue	15.6	19.4	19.8	19.3	...	...	...	20.4	21.0	21.6
Of which: tax revenue	10.6	13.0	14.2	16.2	...	...	...	16.4	16.8	17.7
Total expenditure and net lending	70.1	59.6	67.9	69.8	...	...	...	68.1	64.5	62.5
Of which: education	7.2	4.5	...	...	...	...	...	8.5	9.5	11.0
health	10.2	7.3	...	...	...	...	...	9.0	9.0	9.0
defense	0.9	1.7	...	0.9	...	...	...	...	...	...
Current expenditure	27.8	28.7	26.3	27.2	...	...	...	25.1	23.7	22.2
Of which: personnel costs	5.9	6.7	6.5	7.5	...	...	...	7.3	7.0	6.5
Capital expenditure	42.2	30.9	41.6	42.3	...	...	...	43.1	40.8	40.3
Domestically financed primary expenditure	17.9	18.7	17.0	18.0	...	...	...	18.1	17.6	16.6
Of which: current expenditure		16.3	15.6	15.8	...	...	...	15.6	14.9	13.9
Primary balance	-2.2	0.7	2.8	1.3	...	...	..	2.3	3.4	5.0
Quasi-fiscal balance of the central bank	-1.7	0.9	0.4	0.1	...	...	..	0.0	0.0	0.0
Overall balance (commitment basis, including grants)	-26.7	-30.5	-25.6	-25.8	...	...	...	-21.5	-18.2	-15.7
Overall balance (commitment basis, excluding grants)		-56.5	-48.3	-50.4	...	...	...	-47.7	-43.5	-40.9
Gross domestic product (in millions of dobras)		281,000	334,109	334,109	...	...	...	369,533	408,654	441,896

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ Includes net proceeds from the liquidation of the former Caixa Nacional de Poupança e Crédito and use of SDR allocation, reclassified at end-1997.

2/ Rescheduling of arrears on debt service to Arab Bank for Economic Development in Africa in February 1999.

3/ Assuming agreement on a Poverty Reduction and Growth Facility arrangement by early 2000, this financing gap could be partially covered by a Paris Club rescheduling, along with comparable treatment from non-Paris Club bilateral creditors.

Table 8. São Tomé and Príncipe: Monetary Survey, 1997-2000 1/

	1997	1998	1999 December SMP	1999 December Prelim.	2000 March Program	2000 June Program	2000 Sep. Program	2000 Dec. Program
	(In millions of dobras; end of period)							
Net foreign assets	108,186	113,062	175,311	125,803	117,433	123,252	132,374	151,635
Central bank	53,093	66,677	117,994	81,926	73,750	79,490	88,184	107,976
Commercial banks	55,092	46,385	57,317	43,877	43,683	43,762	44,190	43,660
Net domestic assets	-36,136	-23,347	-68,071	-32,892	-23,524	-28,119	-36,025	-54,076
Net domestic credit	-25,727	-3,089	-39,859	-6,558	2,745	-1,870	-9,796	-27,867
Net credit to government	-33,124	-19,999	-64,669	-32,795	-24,484	-30,091	-39,008	-58,071
Claims	29,461	35,266	36,338	36,170	43,504	43,600	53,380	53,536
Of which: use of SDR allocation	...	6,432	6,357	5,631	15,231	15,326	25,107	25,263
bank liquidation (net)	522	3	1,150	575	-558	-558	-558	-558
Deposits	-62,585	-55,264	-101,007	-68,965	-67,988	-73,690	-92,388	-111,607
Budgetary deposits	-835	-3,137	-22,248	-35,711	-34,523	-40,016	-58,503	-77,511
Counterpart funds	-20,600	-24,271	-24,281	-26,168	-26,334	-26,499	-26,665	-26,830
Foreign currency deposits 2/	-41,150	-27,857	-54,478	-7,086	-7,131	-7,176	-7,220	-7,265
Net claims on other public institutions	...	-1,200	...	-1,335	-1,335	-1,335	-1,335	-1,335
Credit to the economy	7,397	18,109	24,810	27,572	28,563	29,555	30,547	31,539
Other items (net)	-10,409	-20,258	-28,212	-26,334	-26,269	-26,249	-26,229	-26,209
Revaluation accounts	21,841	2,111	1,914	-3,147	-3,147	-3,147	-3,147	-3,147
Other	-32,250	-22,369	-30,126	-23,187	-23,122	-23,102	-23,082	-23,062
Broad money (M2)	72,050	89,714	107,240	92,911	93,909	95,132	96,349	97,559
Local currency	38,942	48,114	59,715	56,624	57,884	59,145	60,406	61,666
Currency outside banks	14,823	18,677	21,077	19,669	19,726	19,782	19,839	19,895
Demand deposits	23,929	26,436	33,483	33,371	34,414	35,457	36,500	37,543
Time deposits	191	3,001	5,155	3,583	3,745	3,906	4,067	4,228
Foreign currency deposits	33,108	41,601	47,525	36,287	36,025	35,987	35,944	35,893
	(In percent of beginning-of-period money stock, unless otherwise specified)							
Net foreign assets	226.2	6.8	65.1	14.2	-9.0	-2.7	7.1	27.8
Net domestic assets	-131.7	17.7	-46.9	-10.6	10.1	5.1	-3.4	-22.8
Net credit to government	-113.4	18.2	-49.8	-14.3	8.9	2.9	-6.7	-27.2
Counterpart funds	-29.5	-5.1	0.0	-2.1	-0.2	-0.4	-0.5	-0.7
Credit to the economy	-3.8	14.9	7.5	10.5	1.1	2.1	3.2	4.3
Credit to the economy (annual percentage change)	-14.5	144.8	37.0	52.3	3.6	7.2	10.8	14.4
Broad money (M2)	94.5	24.5	19.5	3.6	1.1	2.4	3.7	5.0
Local currency broad money	40.5	12.7	12.9	9.5	1.4	2.7	4.1	5.4
Memorandum items:								
M2/base money multiplier	1.6	1.9	2.1	1.7	2.0	2.0	2.0	2.0
Velocity (ratio of GDP to average broad money)	3.7	3.5	3.4	3.7	...	...	...	3.9
Foreign currency deposits (in percent of total deposits)	57.9	58.6	55.2	49.5	48.6	47.8	47.0	46.2

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ With reclassifications, including in December 1997 amalgamation of the savings and loan institution (CNPC) in liquidation with the central government, and identification of the social security administration as other public administration.

2/ Includes deposits constituted from proceeds of special grants, privatization of public enterprises, and oil concession rights.

Table 9. São Tomé and Príncipe: Summary Accounts of the Central Bank, 1997-2000 1/

(In millions of dobras; end of period)

	1997	1998	1999 December SMP	1999 December Prelim.	2000 March Program	2000 June Program	2000 Sep. Program	2000 Dec. Program
Net foreign assets	53,093	66,677	113,931	81,926	73,750	79,490	88,184	107,976
Gross official reserves	86,610	66,687	113,931	81,936	83,314	89,115	107,553	127,465
Liabilities	-33,517	-10	0	-10	-9,564	-9,624	-19,369	-19,489
Net domestic assets	-8,011	-18,306	-62,806	-35,006	-26,675	-32,262	-41,160	-60,202
Net domestic credit	-23,682	-18,993	-64,625	-32,873	-24,562	-30,169	-39,086	-58,149
Net credit to government	-23,732	-17,837	-64,669	-32,664	-24,353	-29,960	-38,878	-57,940
Claims	30,778	38,940	36,338	36,300	44,767	44,863	54,643	54,799
Of which: use of SDRs/Poverty Reduction and Growth Facility	...	6,432	6,357	5,631	15,231	15,326	25,107	25,263
bank liquidation (CNPC)	1,839	1,839	1,150	706	706	706	706	706
Deposits	-54,509	-56,778	-101,007	-68,965	-69,121	-74,823	-93,521	-112,740
Ordinary	-835	-3,137	-22,248	-34,578	-34,523	-40,016	-58,503	-77,511
Bank liquidation (CNPC)	-1,317	-1,513	0	-1,133	-1,133	-1,133	-1,133	-1,133
Counterpart funds	-11,208	-24,271	-24,281	-26,168	-26,334	-26,499	-26,665	-26,830
Loan related	-8,684	-8,708	-8,718	-8,709	-8,764	-8,819	-8,874	-8,929
Grant related	-2,524	-15,562	-15,562	-17,459	-17,570	-17,680	-17,791	-17,901
Foreign currency 2/	-41,150	-27,857	-54,478	-7,086	-7,131	-7,176	-7,220	-7,265
Net claims on other public institutions	...	-1,200	...	-1,335	-1,335	-1,335	-1,335	-1,335
Other claims	50	44	44	1,126	1,126	1,126	1,126	1,126
Other items (net)	15,671	688	1,819	-2,133	-2,113	-2,093	-2,073	-2,053
Revaluation accounts	21,841	2,111	2,506	-3,147	-3,147	-3,147	-3,147	-3,147
Other	-2,697	-5,221	-4,750	-2,149	-2,149	-2,149	-2,149	-2,149
Bilateral payment agreements	-3,473	3,797	4,063	3,162	3,182	3,202	3,222	3,242
Base money	45,083	48,372	51,125	46,920	47,074	47,228	47,024	47,773
Currency outside banks	14,823	18,677	21,077	19,669	19,726	19,782	19,839	19,895
Bank reserves	30,260	29,695	30,048	27,251	27,348	27,445	27,185	27,878
Memorandum item:								
Change in net official reserves (cumulative from beginning of year)	52,871	13,584	47,254	15,249	-8,176	-2,436	6,258	26,050

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ With reclassifications, including amalgamation of the bank in liquidation (CNPC) with the central government, and identification of the social security administration as other public admnistration.

2/ Includes foreign currency deposits constituted from proceeds of special grants, privatization of ENCO (oil importing company), and oil concession rights.

Table 10. São Tomé and Príncipe: Summary Accounts of Banking Institutions, 1997-2000 1/

(In millions of dobras; end of period)

	1997	1998	1999		2000			
			December		March	June	Sep.	Dec.
			SMP	Prelim.	Program			
Net foreign assets	55,092	46,385	57,317	43,877	43,683	43,762	44,190	43,660
Foreign assets	55,092	46,385	57,317	43,877	43,683	43,762	44,190	43,660
Foreign liabilities	0	0	0	0	0	0	0	0
Net domestic assets	2,135	24,652	28,846	29,410	30,500	31,588	32,320	34,004
Reserves	30,596	30,127	30,048	27,251	27,348	27,445	27,185	27,878
Cash holdings	1,535	2,249	2,569	1,002	1,500	1,200	1,500	2,200
Dobra deposits in the central bank	26,381	25,549	...	24,315	...	...	...	...
Foreign exchange deposits in the central bank	2,680	2,329	...	1,934	...	...	...	...
Net domestic credit	-2,045	17,742	24,765	26,315	27,307	28,299	29,290	30,282
Net credit to government	-9,392	-322	0	-131	-131	-131	-131	-131
Claims	0	0	0	0	0	0	0	0
Deposits	0	0	0	0	0	0	0	0
Counterpart funds 2/	-9,392	0	0	0	0	0	0	0
Deposits of bank in liquidation (CNPC)	0	-322	...	-131	-131	-131	-131	-131
Credit to the economy	7,348	18,065	24,765	26,446	27,437	28,429	29,421	30,413
Other items (net)	-26,416	-23,217	-25,967	-24,156	-24,156	-24,156	-24,156	-24,156
Deposits	57,227	71,037	86,163	73,288	74,183	75,350	76,510	77,664
Local currency	24,365	29,581	38,638	37,232	38,159	39,363	40,567	41,771
Demand deposits	23,929	26,436	33,483	33,371	34,414	35,457	36,500	37,543
Time deposits	191	3,001	5,155	3,583	3,745	3,906	4,067	4,228
Nonresidents' deposits	245	145	..	278	..	..	..	
Foreign currency	32,863	41,456	47,525	36,055	36,025	35,987	35,944	35,893
Demand deposits	30,421	32,431	37,530	27,685	27,601	27,511	27,414	27,311
Time deposits	366	326	355	359	361	364	366	368
Nonresidents' deposits	2,076	8,699	9,640	8,011	8,062	8,113	8,163	8,214
Memorandum item:								
Net position vis-à-vis the central bank	30,596	30,127	30,048	27,251	27,348	27,445	27,185	27,878

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.

1/ With reclassifications, including amalgamation of the bank in liquidation (CNPC) with the central government, and identification of the social security administration as other public administration.

2/ In March 1998, in order to satisfy reserve requirements, deposits of public institutions and counterpart funds were transferred to the central bank.

Table 11. São Tomé and Príncipe: Stock of Public External Debt, 1996-99

(In millions of U.S. dollars)

	1996		1997		1998		1999	
	Total	*Of which:* arrears	Total	*Of which:* arrears	Total	*Of which:* arrears	Total	*Of which:* arrears
Total outstanding debt 1/	265.8	61.1	267.3	61.4	292.6	80.3	295.6	75.2
Medium- and long-term debt 1/	234.0	29.3	235.5	29.6	244.9	32.6	248.0	27.7
Multilateral	162.2	5.7	158.2	5.2	167.4	7.1	170.3	0.0
IMF	0.6	0.0	0.3	0.0	0.1	0.0	0.0	0.0
IDA	59.5	0.0	57.4	0.0	61.9	0.0	65.4	0.0
African Development Fund	83.8	0.0	81.3	0.0	86.9	0.0	87.5	0.0
Arab Bank for Economic Development in Africa	8.5	5.7	8.6	5.0	8.4	7.1	8.2	0.0
Others	9.9	0.0	10.6	0.2	10.0	0.0	9.2	0.0
European Investment Bank	1.7	0.0	1.4	0.2	1.0	0.0	0.6	0.0
International Fund for Agricultural Development	6.1	0.0	6.2	0.0	6.7	0.0	6.4	0.0
Organization of Petroleum Exporting Countries	2.1	0.0	3.0	0.0	2.3	0.0	2.2	0.0
Official bilateral	71.7	23.5	77.4	24.4	77.5	25.6	77.7	27.7
Paris Club	62.2	18.7	62.2	21.4	60.0	20.5	60.4	22.5
Portugal	29.0	0.8	29.1	0.8	30.2	1.7	31.1	2.7
Germany	8.9	6.6	9.0	8.1	13.0	13.0	13.5	13.5
France	9.2	0.0	8.0	0.0	8.3	0.0	7.1	0.0
Spain	3.1	1.2	3.3	1.6	3.6	2.0	3.7	2.4
Russia	11.1	10.0	11.9	10.9	3.8	3.8	4.0	4.0
Belgium	1.0	0.0	0.9	0.0	1.2	0.0	1.0	0.0
Non-Paris Club	9.5	4.9	15.2	3.0	17.5	5.0	17.3	5.2
China	5.7	2.4	11.2	0.0	11.8	0	11.8	0.0
Others	3.8	2.5	4.0	3.0	5.6	5.0	5.5	5.2
Cape Verde	1.3	0.0	1.3	0.3	0.6	0.0	0.3	0.0
Algeria	1.3	1.3	1.4	1.4	1.3	1.3	1.3	1.3
Yugoslavia, Fed. Rep. of	1.2	1.2	1.3	1.3	3.8	3.8	3.9	3.9
Short-term debt 2/	31.8	31.8	31.8	31.8	47.7	47.7	47.5	47.5
Of which: Italy	...	...	...	...	19.3	19.3	18.0	18.0

Sources: São Tomé and Príncipe authorities; and staff estimates.

1/ Including the IMF.

2/ Starting in 1998, includes some US$19 million in dispute with Italy; all short-term debt is official bilateral (Angola, Italy, Air Portugal).

Table 12. São Tomé and Príncipe: Indicators of Fund Credit, 1996-2006

	1996	1997	1998	1999	Program 2000	Program 2001	Program 2002	Program 2003	2004	2005	2006
					(In units indicated)						
Total Fund credit outstanding (end of period)											
In millions of SDRs	0.40	0.24	0.08	0.00	1.90	3.80	5.71	6.66	6.66	6.56	6.09
In millions of U.S. dollars	0.58	0.32	0.11	0.00	2.61	5.22	7.88	9.27	9.35	9.21	8.54
In billions of dobras	1.63	2.26	0.78	0.00	19.54	39.27	59.56	70.42	71.46	75.74	75.54
In percent of quota	7.27	4.36	1.45	0.00	25.70	51.41	77.11	89.96	89.96	88.67	82.25
Debt service to the Fund											
In millions of SDRs	0.16	0.16	0.16	0.08	0.00	0.01	0.02	0.03	0.03	0.13	0.51
In millions of U.S. dollars	0.24	0.22	0.22	0.11	0.00	0.02	0.03	0.04	0.05	0.18	0.72
In billions of dobras	0.67	1.55	1.49	0.81	0.02	0.12	0.22	0.33	0.36	1.49	6.34
In percent of:											
Export of goods and services	2.2	1.8	1.8	0.7	0.0	0.1	0.1	0.2	0.2	0.6	2.4
Total debt service due	3.0	2.5	2.2	1.4	0.0	0.2	0.3	0.4	0.4	1.4	5.0
Government revenue	3.9	3.2	2.8	1.2	0.0	0.1	0.2	0.3	0.3	1.1	4.1
GDP	0.5	0.5	0.5	0.2	0.0	0.0	0.1	0.1	0.1	0.2	0.9
Quota	3.0	2.9	2.9	1.1	0.0	0.2	0.3	0.4	0.4	1.7	6.9
					(In millions of SDRs)						
Debt service to the Fund											
Charges	0.00	0.00	0.00	0.00	0.00	0.01	0.02	0.03	0.03	0.03	0.03
Repurchases/repayments	0.16	0.16	0.16	0.08	0.00	0.00	0.00	0.00	0.00	0.10	0.48

Sources: IMF, Treasurer's Department; and staff estimates and projections.

São Tomé and Príncipe--Three-Year Arrangement Under the Poverty Reduction and Growth Facility

1. Attached hereto is a letter ("the letter") dated March 24, 2000, with an annexed Memorandum of Economic and Financial Policy ("the Memorandum"), from the Minister of Planning, Finance and Cooperation of São Tomé and Príncipe requesting from the International Monetary Fund as Trustee of the Poverty Reduction and Growth Facility Trust ("the Trustee") a three-year arrangement under the Poverty Reduction and Growth Facility, and setting forth:

(a) the objectives and policies of the program that the authorities of São Tomé and Príncipe intend to pursue during the three-year period of the arrangement;

(b) the objectives, policies and measures that the authorities of São Tomé and Príncipe intend to pursue during the first year of the arrangement; and

(c) understandings of São Tomé and Príncipe with the Trustee regarding reviews that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of São Tomé and Príncipe will pursue for the second and third years of the arrangement.

2. To support these objectives and policies, the Trustee grants the requested three-year arrangement in accordance with the following provisions, and subject to the provisions applying to assistance under the Poverty Reduction and Growth Facility Trust.

1) (a) For a period of three years from April --, 2000, São Tomé and Príncipe will have the right to obtain loan disbursements from the Trustee in a total amount equivalent to SDR 6.657 million, subject to the availability of resources in the Poverty Reduction and Growth Facility Trust.

(b) Disbursements under this arrangement shall not exceed the equivalent of SDR 2.853 million until March 15, 2001 and the equivalent of SDR 4.755 million until March 15, 2002.

(c) During the first year of the arrangement:

(i) the first disbursement, in an amount equivalent to SDR 0.951 million, will be available on April --, 2000, at the request of São Tomé and Príncipe;

(ii) the second disbursement, in an amount equivalent to SDR 0.951 million, will be available on September 15, 2000, at the request of São Tomé and Príncipe and subject to paragraph 2 below; and

(iii) the third disbursement, in an amount equivalent to SDR 0.951 million, will be available on March 15, 2001, at the request of São Tomé and Príncipe and subject to paragraph 2 below.

(d) The right of São Tomé and Príncipe to request disbursements during the second and third years of this arrangement shall be subject to such phasing and conditions as shall be determined. The phasing of, and conditions for, disbursements during the second year of this arrangement shall be determined in the context of a review of São Tomé and Príncipe's program with the Trustee, the timing of which shall be established at the first review contemplated in paragraph 2(d) of this arrangement.

2) São Tomé and Príncipe will not request the second or third disbursement specified in paragraphs 1(c)(ii) and 1(c)(iii) above:

(a) If the Managing Director of the Trustee finds that, with respect to the second disbursement, the data as of June 30, 2000 and, with respect to the third disbursement, the data as of December 31, 2000, indicate that:

(i) the floor on the primary balance of the central government's financial operations, or

(ii) the ceiling on changes in net bank credit to the central government, or

(iii) the ceiling on changes in net domestic assets of the central bank, or

(iv) the floor on changes in the net international reserves position of the central bank, or

(v) the ceiling on the central government's non-reschedulable outstanding external payments arrears, or

(vi) the ceiling on contracting and guaranteeing by the central government of new concessional borrowing with a maturity of more than one year, or

(vii) the ceiling on change in the central government's outstanding stock of short-term external credit with a maturity of less than one year,

referred to in paragraph 34 of the Memorandum and specified in Table 1 of the Memorandum, was not observed; or

(b) If the Managing Director of the Trustee finds:

(i) with respect to the second disbursement, that São Tomé and Príncipe has not carried out its intentions with respect to the adoption of a privatization program of large agricultural estates and the adoption of a law simplifying real property and land ownership by June 30, 2000 as specified in paragraph 25 and Table 2 of the Memorandum, or

(ii) with respect to the third disbursement, that São Tomé and Príncipe has not carried out its intentions with respect to the adoption of a mechanism by which adjustments of water and electricity rates reflect production and distribution costs by September 30, 2000 as specified in paragraph 24 and Table 2 of the Memorandum; or

(c) If São Tomé and Príncipe has:

(i) imposed or intensified restrictions on payments and transfers for current international transactions, or

(ii) introduced or modified multiple currency practices, or

(iii) concluded bilateral payments agreements that are inconsistent with Article VIII, or

(iv) imposed or intensified import restrictions for balance of payments reasons, or

(v) incurred any new external payments arrears by the public sector; or

(d) Until the Trustee has determined, with regard to the second disbursement, that the first review of São Tomé and Príncipe's program scheduled for completion on or before September 14, 2000 and referred to in paragraph 4 of the Letter has been completed and, with regard to the third disbursement, that the second program review scheduled for completion on or before March 14, 2001 and referred to in paragraph 4 of the Letter has been completed.

3. When São Tomé and Príncipe is prevented from requesting disbursements under this arrangement because of this paragraph 2, such disbursements may be made available only after consultation has taken place between the Trustee and São Tomé and Príncipe and understandings have been reached regarding the circumstances in which São Tomé and Príncipe may request the disbursements.

3) In accordance with paragraph 4 of the Letter, São Tomé and Príncipe will provide the Trustee with such information as the Trustee requests in connection with the progress of São Tomé and Príncipe in implementing the policies and reaching the objectives of the program supported by this arrangement.

4) In accordance with paragraph 3 of the Letter, during the period of this arrangement São Tomé and Príncipe, shall consult with the Trustee on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director

Managing Director of the Trustee requests such a consultation. Moreover, after the period of this arrangement and while São Tomé and Príncipe has outstanding financial obligations to the Trustee arising from loan disbursements under this arrangement, São Tomé and Príncipe will consult with the Trustee from time to time, at the initiative of the Government or whenever the Managing Director of the Trustee requests consultation on São Tomé and Príncipe's economic and financial policies. These consultations may include correspondence and visits of officials of the Trustee to São Tomé and Príncipe or of representatives of São Tomé and Príncipe to the Trustee.

Attachment

March 24, 2000

Mr. Stanley Fischer
Acting Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C. 20431
U.S.A.

Dear Mr. Fischer:

1. Since early 1998, the São Tomé and Príncipe authorities have been implementing macroeconomic policies and structural adjustment measures as part of a staff-monitored program agreed with the International Monetary Fund. To consolidate the progress achieved, the government has adopted an economic reform program for 2000-02, the objectives of which are described in the interim poverty reduction strategy paper and the matrix of economic policy actions, prepared with the assistance of the staffs of the Fund and the World Bank and sent to you under separate cover.

2. The attached memorandum of economic and financial policies describes the government's objectives and economic policies for 2000-02, as well as the specific objectives and measures envisaged for the first year of the program, from January 1 to December 31, 2000. In support of these objectives and policies, the government requests a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF) in an amount equivalent to SDR 6.657 million (90 percent of quota). The government also plans to seek assistance, in due course, from the Fund, the World Bank, and the international financial community in the context of the enhanced Initiative for Heavily Indebted Poor Countries (HIPC Initiative).

3. The government believes that the policies set forth in the attached memorandum will enable it to attain the objectives of its program, but it is ready to take further measures that may prove necessary to this end. During the period of the proposed three-year PRGF arrangement, the authorities will consult with the Managing Director of the Fund on the adoption of any measures that may be appropriate, either at their own initiative or at the Managing Director's request. Moreover, following the period of implementation of the arrangement, and as long as São Tomé and Príncipe has outstanding financial obligations toward the Fund arising from loans disbursed under the arrangement, the government will consult with the Fund, from time to time, on São Tomé and Príncipe's economic and financial policies, at its own initiative or at the request of the Managing Director.

4. The government will communicate to the Fund any information the Fund may request to monitor the progress made in implementing the economic and financial policies and the measures required to achieve the program objectives. In addition, the authorities of São Tomé and Príncipe will conduct with the Fund two semiannual reviews of the program during the first year, to be completed by September 2000 and March 2001, respectively.

Sincerely yours,

/s/

Adelino Castelo David
Minister of Planning, Finance and Cooperation

Attachment: Memorandum of Economic and Financial Policies for 2000

São Tomé and Príncipe

Memorandum of Economic and Financial Policies for 2000

March 24, 2000

I. Introduction

1. Since early 1998, the government of São Tomé and Príncipe has implemented macroeconomic policies and structural adjustment measures, first under an economic policy framework and subsequently under a staff-monitored program that were agreed with Fund staff. The program aimed at eliminating the government's primary budget deficit, reducing inflation, and improving the prospects for medium-term economic growth. On the whole, the measures and reforms implemented enabled São Tomé and Príncipe to achieve its macroeconomic objectives, particularly as regards fiscal consolidation, containment of inflation, liberalization of the economy, and reduction of the spread between the official exchange rate and the parallel market rate of the dobra. Seven out of the eight quantitative benchmarks were met by end-September and end-December 1999 under the staff-monitored program, the exception being the ceiling on government primary expenditure. Moreover, all structural benchmarks were met through end-December, with the exception of the two related to the adoption of the strategy for the privatization of large government estates and to the preparation of an action plan against poverty. Over this two-year period, the government's efforts were also supported by technical and financial assistance from the World Bank and several other bilateral and multilateral donors and lenders.

2. Despite the progress made, the country's economic and financial situation remains very difficult. São Tomé and Príncipe's economy and external position are largely dependent on external assistance. The external public debt burden is particularly heavy, per capita income is very low, and structural rigidities continue to hamper economic growth and private sector development. Access to essential social services is limited, and poverty is widespread. In these circumstances, the government is determined to consolidate progress already made during 1998-99, intensify fiscal adjustment efforts, and accelerate structural reforms in the coming years, with a view to diversifying the economy, reducing domestic and external financial imbalances, achieving durable growth, and significantly reducing poverty.

3. Against this backdrop, the authorities have prepared a matrix of economic policy actions for 2000-02, with assistance from Fund and World Bank staffs, as well as an interim poverty reduction strategy paper that endorse the macroeconomic framework and matrix of policy actions. In support of the program for 2000-02, the government requests a three-year arrangement under the Fund's Poverty Reduction and Growth Facility (PRGF), as well as nonproject assistance from the World Bank, the African Development Bank (AfDB), and other multilateral and bilateral donors and lenders. The government also hopes that São

Tomé and Príncipe will, in due course, benefit from the enhanced Initiative for Heavily Indebted Poor Countries (HIPC Initiative).

4. This memorandum of economic and financial policies describes the objectives and economic policies set by the government for 2000-02, as well as the specific objectives and measures to be implemented in 2000. It also covers external sector developments and program monitoring.

II. MEDIUM-TERM PROGRAM AND OBJECTIVES FOR 2000

5. The government's medium-term program for 2000-02 will focus on four main priorities: (a) a prudent fiscal policy, designed to **broaden the tax base** and assign priority in expenditure allocation to social sectors and infrastructure maintenance; (b) an ambitious social program, with special emphasis on reducing poverty, and improving education and health services; (c) a tight monetary policy to reduce inflation and improve international reserves; and (d) accelerated structural reforms designed to promote private sector development and consolidate the bases for sustainable economic growth. Special emphasis will be placed on good governance.

6. As indicated in the interim poverty reduction strategy paper, the objectives of the adjustment strategy for 2000-02 are to establish a stable macroeconomic environment conducive to higher growth by (a) reducing inflation to 3 percent before 2001; and (b) limiting the external current account deficit (excluding official transfers) to 66 percent of GDP (or to less than 41 percent after official transfers) in 2002, against the backdrop of new investments in oil exploration. The government will endeavor to (a) intensify the campaign to reduce poverty; (b) promote job creation by the private sector; (c) develop human resources; and (d) enhance protection of the environment. The average annual growth rate of real GDP is expected to be 4 percent in 2001-02, making possible a 1.7 percent annual increase in per capita income. Excluding oil investments, São Tomé and Principe's balance of payments should continue to improve as a result of increased export diversification, notably in agriculture, fisheries, and tourism. Private investment is expected to grow from 14 percent of GDP in 1999 to 31 percent of GDP in 2002 as a result of the expected start-up of oil sector investments; gross national savings are expected to increase from 15 percent of GDP in 1999 to 20 percent of GDP in 2002.

7. With a view to attaining the objectives of its medium-term adjustment strategy, the government will focus its efforts on the pursuit of a prudent fiscal policy, so as to increase the primary fiscal surplus from 1.3 percent of GDP in 1999 to 5 percent of GDP in 2002, while increasing budgetary allocations to the education and health sectors. The government will also pursue a tight monetary policy designed to reduce inflation and strengthen the central bank's international reserves position, in the context of the market-based exchange rate system currently in place. It will also expand structural reforms, with a view to promoting private sector development, while improving the efficiency of the public sector.

8. As the economy has been significantly liberalized already, the government will create a legal and regulatory framework geared to the expansion of private investment and the encouragement of private capital investment from abroad, making the private sector the engine of economic growth. In addition, it will strive to improve the operations of the legal system and will continue to implement the public enterprise reform and privatization program.

9. The government is convinced that the achievement of sustainable economic growth will help reduce poverty. To increase life expectancy and improve quality of life, the government intends to step up the fight against major endemic illnesses, in particular malaria and AIDS, improve access to primary health care services, expand the vaccination of children, increase school attendance and literacy rates, and improve housing, especially for the most disadvantaged populations. Moreover, the government intends to reduce infant mortality and intensify efforts to inform, educate, and communicate in the areas of health and family planning by carrying on a campaign to increase the awareness of women, especially in rural areas.

10. Within the medium-term strategic framework, the primary macroeconomic objectives for the first year of the program are to (a) reduce the inflation rate to 5 percent in 2000; and (b) limit the external current account deficit (excluding official transfers) to 62 percent of GDP. Real GDP growth in 2000 is projected to reach 3 percent. In the area of government finance, the program aims to increase the primary fiscal surplus to 2.3 percent of GDP in 2000. In order to attain these objectives, a series of measures will be implemented in the course of the year in the fiscal, money, and exchange rate policy areas, the external sector, and the area of structural reform.

A. Macroeconomic Policies

Fiscal policy

11. The fiscal policy will aim at reducing the fiscal deficit (on a commitment basis, including grants) from 26 percent of GDP in 1999 to 22 percent of GDP in 2000, and at increasing the primary surplus (excluding foreign-financed investments) from 1.3 percent of GDP in 1999 to 2.3 percent of GDP in 2000. The draft budget law for 2000, which was submitted to the National Assembly on February 29, 2000, is in line with these program objectives. It includes a series of measures designed to rationalize the customs tariffs and domestic indirect taxation, broaden the tax base, and control expenditure. The central bank's draft budget, appended to the general government budget, also envisages a surplus of 0.6 percent of GDP, and the draft budget of the water and electricity distribution company (EMAE) calls for a balance in 2000. With the rescheduling of arrears to the Arab Bank for Economic Development in Africa (BADEA) in 1999, all payments arrears to multilateral organizations have been settled, as have all domestic payments arrears. The government will not accumulate any new external or domestic payment arrears during the program period.

12. As regards revenue (excluding grants), an increase of 16.5 percent in 2000 (to Db 75 billion, or 20.4 percent of GDP) is forecast. The improved revenue figure includes the impact of the new customs tariff adopted at end-December 1999, the elimination of export taxes, and the adjustment of excise taxes on petroleum products, alcoholic beverages, and tobacco starting in February 2000. The new customs tariff has reduced the number of import duty rates to three: 5 percent, 10 percent, and 20 percent. The zero rate has been eliminated, and the 5 percent rate has been applied to all imports previously subject to the zero rate; no other taxes will be levied by customs. By end-September 2000, a study will be undertaken on the rationalization of domestic indirect taxation, with a view to simplifying the general sales tax and applying it to domestic goods and services (such as hotels, restaurants, and maintenance and repair services). The government has also adjusted upward the rates of excise taxes—to 149 percent for petroleum products and 55 percent for alcoholic beverages and tobacco—with a view to ensuring the revenue neutrality of its tax reform effort regarding these products. Simulations based on 1997 revenue show that the introduction of the new rate, the elimination of export duties, and the adjustment of excise taxes could result in revenue losses of approximately Db 4 billion annually (about 1 percent of GDP).

13. To offset the tax reduction resulting from the implementation of the new customs tariff, the authorities will strengthen the taxation and customs administrations and intensify collection efforts in the course of 2000 through a variety of actions. First, by end-March 2000, they will draw up a list of all tax and duty exemptions. The authorities will subsequently eliminate all ad hoc tax and customs exemptions starting April 1, 2000, strictly monitor legal exemptions, and broaden the taxable base. Second, starting by end-March 2000, the government will introduce, with technical assistance from Portugal, a system to monitor and verify values declared at customs, including a periodic updating of their file of import unit values. Third, the authorities will strengthen the tax audit and control offices in both the finance directorate and the customs administration. Fourth, the authorities will implement an action plan to restructure and strengthen the customs service. Fifth, the authorities will make fully operational the SYDONIA software system for assessing the basis of customs duties and calculating the amount of duty due. Sixth, beginning in March 2000, full power will be given to the customs service and the Ministry of Finance to evaluate the tax bases at customs, assess and collect duties and taxes, and apply penalties where appropriate, through the adoption of an amendment (to Article 180 of the Law of 1944) designed to eliminate the requirement that government departments settle tax disputes through the court system. Seventh, the authorities will make sure that all tax and customs laws and regulations are enforced. Eighth, the authorities will monitor very strictly transfers by public enterprises and government agencies to the budget, in particular by the Food Aid Management Commission (GGA). Implementation of all these measures should enable the government to increase its revenues from 19.3 percent of GDP in 1999 to 20.4 percent of GDP in 2000.

14. Control over government expenditure, other than interest on the public debt, will be pursued primarily through restraint of the wage bill, which currently absorbs 7.5 percent of GDP. Accordingly, the government will implement a program of administrative reform and reduction in the number of civil servants in the first half of 2000. Taking account of the

inflation objective, the size of the civil service, and expected revenue collections, the government will postpone application of the December 1997 law on the civil service regulations and the special provisions governing employees (other than military personnel, security forces, and education and health services), which have proved difficult to implement and very costly. The government also repealed the decree on preliminary reforms and early retirements. It will implement the organizational and staffing plans for all government ministries, starting in March 2000. It will also prepare a report identifying redundant civil servants, and providing the assessment of the civil service downsizing resulting from the implementation of the organizational and staffing plans by end-April 2000, and create a single data processing system for managing the civil service and payroll by end-June 2000. The government will complete by December 2000 a study of the civil service wage scale, with a view to rationalizing the salary scale and introducing a compensation and promotion system based on performance evaluation. Severance pay to employees discharged from the civil service will be equal to the base salary as of December 1999, multiplied by the number of years of seniority in the civil service, as specified by law. An allocation of Db 1 billion has been included in the 2000 budget to cover severance pay for employees laid off under the civil service downsizing program.

15. To reduce imbalances in civil service salaries, and taking account of social pressures, the authorities decided to grant a selective salary increase averaging Db 80,000 per month, effective January 1, 2000, for 1,100 government employees who had not benefited from the December 1997 law on the civil service regulations and the special provisions governing civil servants. This adjustment will add up to a 7.4 percent increase in the wage bill, approximately the average projected inflation rate for 2000. Implementation of this wage policy will reduce the ratio of government payroll expenditure to GDP from 7.5 percent in 1999 to 7.3 percent in 2000.

16. Other current expenditure on goods and services should fall from 3.8 percent of GDP in 1999 to 2.9 percent of GDP in 2000, while giving priority to boosting nonwage expenditure for education, health, agriculture, and infrastructure maintenance. Transfer costs will increase from 1.8 percent of GDP in 1999 to 2 percent in 2000, with a view to better covering the needs for scholarships and hospital costs abroad, as well as contributions to multilateral organizations. The government will design its sectoral development strategies with technical assistance from the World Bank and the United Nations Development Program (UNDP). Having completed its work on the agricultural policy (October 1999), it will develop policies for tourism (June 2000), education (June 2000), health (September 2000), and infrastructure maintenance (September 2000). The government has also expanded its programming of public investments by extending the public investment program (PIP) planning horizon to cover a three-year period. Before end-September 2000, it will consult with the IMF and the World Bank regarding the budgetary allocation ceiling and makeup of the PIP for 2001-03, which will give priority to human resource development and infrastructure maintenance. Adoption of the 2001-03 PIP is a structural benchmark of the program for end-September 2000. As part of its general strategy, the government will organize quarterly meetings on the monitoring of public investments, with the participation of the main donors in São Tomé and Príncipe; the first of these meetings is scheduled to take

place before end-April 2000. These meetings will contribute to improving the selection of PIP projects and oversight of their implementation; the entire government investment program will be covered, including investment financed by special external grant, counterpart funds, and extraordinary deposits of the proceeds of oil exploration concessions. No project will be executed unless recorded in the budget and the PIP.

17. The government will raise the budgetary allocation for health and education, and devote adequate resources to poverty reduction, for which a strategy and action plan will be adopted in 2001. Total outlays for education, which were estimated at 14 percent of total primary expenditure in 1999 (7.9 percent of GDP), will be raised to 15.9 percent in 2000 (8.5 percent of GDP). In the health sector, expenditure will stabilize at 15 percent of primary expenditure (9 percent of GDP).

18. On the basis of its study of the finance directorate in March 1999, the government took steps to improve operations and prepare a staff training and technical assistance program. By end-June 2000, it will make operational the three autonomous administrations responsible, respectively, for domestic taxation, preparation and supervision of budget execution, and management of the treasury and public accounting. All government revenues (including proceeds from oil concessions), as well as external financing (including funds drawn on special grants) and central government deposits have been centralized at the treasury as of January 1, 2000.

Monetary and exchange rate policies

19. In 2000, the central bank will pursue a prudent monetary policy aimed at reducing inflation and increasing gross international reserves to US$17 million, equivalent to 4½ months of imports. Continued improvement in the fiscal situation should make it possible to reduce net bank lending to the government by 27 percent of the end-December 1999 money stock. Credit to the private sector is expected to increase by 4 percent of the end-December 1999 stock of money, reflecting the expected diversification of the economy and the improving rate of financial intermediation. On the whole, however, net domestic assets should decline by 23 percent of the end-December 1999 money stock, given the scheduled strong increase in the government's credit position with the banking system. In 2000, the money supply should increase by 5 percent, consistent with the inflation target.

20. Having already fully liberalized lending and borrowing rates, the monetary authorities will maintain the central bank's reference interest rate above the inflation rate recorded during the program period, while paying particular attention to reducing the spread between the reference rate and the borrowing rates applied by commercial banks. In this context, the government will implement structural measures aimed at easing proceedings regarding contract enforcement and loan settlements during the second half of 2000, such as a simplification of real property and land ownership, and reforms in the judiciary. The monetary authorities will also create a money market in July 2000, introducing central bank bills that banks and other economic agents will be able to acquire and sell at freely

negotiated interest rates. In 2001, the central bank will review the required reserve ratio, currently set at 22 percent, and adjust it in light of observed money market performance.

21. The central bank will continue strengthening its bank supervision activities, so as to ensure that banks continue to adhere to required prudential ratios, and the government will intensify its efforts to recover loans owed to the national savings and loan institution (CNPC), which is being liquidated. In this connection, debtors who are behind in their payments on loans advanced by the CNPC will be identified publicly, denied access to bank credit,[1] and subject to legal action. The central bank has also decided to strengthen its inspection department and, with the assistance of the IMF, will create a genuine internal audit unit to oversee its operations. Furthermore, the bank will have its accounts verified annually by external auditors.

22. In the exchange rate area, the authorities will ensure that their flexible, market-based exchange rate system will work effectively. Accordingly, the central bank will not attempt to influence the rate offered by commercial banks and will limit its intervention on the foreign exchange markets to achieving its international reserves target. The government is aware that fiscal discipline and compliance with the targets of net bank credit to the government are prerequisites for a successful monetary and exchange rate policy. Following this policy would help consolidate the gains made in 1998-99 and reduce the spread between the official rate and the parallel market rate below 1 percent.

23. The authorities adopted new foreign exchange legislation in August 1999 liberalizing São Tomé and Príncipe's current external transactions. Under the circumstances, the government will take all steps required to accept the obligations of Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement as soon as possible. In addition, the authorities will encourage the use of the dobra in transactions among major companies by asking public and semi-public enterprises, such as EMAE, the petroleum distribution company (ENCO), the telecommunications company (CST), the airport management agency (ENASA), and the harbor management agency (ENAPORT), to do all their billing in dobras, with the exception of export transactions with foreign airlines and maritime companies, by end-June 2000.

B. Structural Policies

24. In consultation with the World Bank, the government will review the structure of water and electricity production and distribution costs, with a view to introducing cost-cutting measures and adopting by end-September 2000 a new mechanism by which adjustments in water and electricity rates reflect changes in production and distribution costs. The government will also conduct an in-depth analysis of the telecommunications sector, with a view to opening it up to competition in due course. In the area of external

[1] Credits to debtors not current on their obligations to the CNPC will continue to be provisioned at 100 percent.

trade, following the elimination of nontariff barriers in 1999, the authorities have implemented a comprehensive reform of the customs tariff and eliminated export taxes under the 2000 budget (paragraph 12), with technical assistance from the World Bank and France. By end-June 2000, the government will also design an action plan, with technical assistance from the World Bank, to increase private sector business and investment incentives, with an emphasis on strengthening the legal, regulatory, and judicial systems.

25. With respect to public enterprises, the government will implement its new reform and privatization program in 2000. By end-June 2000, the government will adopt a financial restructuring plan for EMAE, introducing an appropriate accounting and budget system and strengthening revenue collection procedures, together with a medium-term investment strategy and program for the company. In the same time frame, the government will complete a study of the possible alternatives for the future of the company (privatization, awarding a concession arrangement for managing the utility to a private strategic partner, etc.). Lastly, the authorities will have the accounts of the public enterprises (EMAE, ENCO, ENAPORT, and ENASA) certified each year by external auditors. In the agricultural sector, the government has already turned all its large plantations over to private operators under long-term operating leases and redistributed about 40,000 hectares of arable land to 6,000 families engaged in small and medium-sized farming operations. With assistance from the World Bank, by end-June 2000, the government will adopt a privatization program of large agricultural estates, as well as a law simplifying real property and land ownership, thereby increasing incentives to produce and invest.

26. With respect to prospects for oil exploration, the government will continue to ensure transparency in the conduct of future operations and formalize procedures and operations of the administrative unit responsible for the preparation of its policy in the oil sector, with assistance from the World Bank and Norway. This unit, which is placed in the Office of the Prime Minister, will report on its activities periodically to the Economic Council (and its technical oversight committee), which will henceforth be responsible for coordinating government policy in the oil sector, including conducting negotiations with oil companies. In September 1999, the authorities began discussions with the U.S. company Environment Remediation Holdings Company (ERHC) to review progress made in implementing the memorandum of understanding signed between São Tomé and Príncipe and ERHC in May 1997, and to reassess the role of the U.S. company and the Société des Pétroles de São Tomé et Principe (STPETRO), a joint venture created in 1998 by the government (51 percent) and ERHC (49 percent). In 2000, the government will continue negotiations with ExxonMobil on a production-sharing contract. It will also prepare and submit to parliament a draft law governing petroleum exploration and production in São Tomé and Príncipe by end-June 2000, and adopt the implementing decrees and orders for the new legislation by end-December 2000. The government will consult the Fund and the World Bank with respect to negotiations for oil concession or production-sharing contracts and the drafting of oil legislation.

27. Achievement of sustainable growth in per capita income will help reduce poverty in São Tomé and Príncipe. Specifically, the distribution of arable land to small-scale farmers

and simplification of the regulations governing real property and ownership, together with the elimination of taxes on agricultural exports, should significantly improve the standard of living of rural populations. By contrast, salaried workers in cities will be hurt by the program's structural adjustment measures, including the reform of the civil service and the program for reforming public enterprises. With the help of donors and lenders, and in consultation with civil society, the government will by end-2001 prepare a poverty reduction strategy, to be implemented during the program period. The strategy should include precisely targeted measures designed to further boost school enrollment and literacy rates, improve primary health care, increase women's participation in development activities, slow urban drift, and bring demographic growth under control. The government has already expressed its intention to create or repair 60 classrooms per year for primary schools, especially in rural areas, and 30 classrooms per year for secondary schools. It will recruit and train 90 new teachers yearly and retrain 300 teachers in primary schools; it will also train 30 teachers in secondary schools. In December 2000, the government will establish a committee to oversee its poverty reduction plan, which will call for sufficient budget appropriations for the education and health sectors. In order to ensure effective follow-up of progress made in reaching the targets for social welfare and poverty reduction, a set of indicators will be developed with the help of the AfDB and the UNDP. The authorities will transmit annual figures for these indicators to the Fund and the World Bank.

28. The government is determined to maintain transparency and good governance throughout this crucial phase, in which the prospects for oil development are taking shape. It will combat and take strong action against any acts of fraud and corruption that come to its attention. In the case of the fraudulent transfers of foreign currency assets uncovered in 1994, the central bank has prepared a detailed report enabling it to establish responsibility and assess the amount of fraudulent transfers. The agents involved in the case have been removed from their positions, and legal action has been taken against them. In addition, the central bank has ordered an independent external audit of its correspondent accounts, the report of which will be completed and published by end-March 2000 as a prior action of the program. As for the attempted fraud in treasury bills uncovered by the authorities in February 1999, the government has dismissed the officials involved and taken legal action against them. It has recently prepared a report showing that the matter is under judicial review and awaiting trial. The first program review will include, inter alia, an assessment of the handling of these two cases of fraud.

29. Other new measures have also been adopted to strengthen good governance and transparency. For example, the requirement that the central bank and public enterprises have their accounts audited by independent, external auditors, together with the strengthening of internal auditing and inspection of departments of the central bank, will contribute significantly to greater transparency in the management of public affairs. Other measures designed to prevent and combat fraud and corruption more effectively include simplifying both customs tariffs and domestic indirect taxation, and eliminating ad hoc exemptions, along with strengthening the internal audit departments of the finance directorate and customs.

30. The government will intensify its efforts to improve the quality and timeliness of its statistical data and will supply to the IMF the necessary basic data for Article IV consultations, while strengthening program monitoring and control. With the technical and financial support of the AfDB, the authorities will conduct a households statistical survey, develop a social database in the National Institute of Statistics, and prepare a series of social welfare and poverty indicators to be monitored as part of its poverty reduction policy. In the area of monetary statistics, the authorities will accelerate the distribution of data and make sure that the monthly monetary statement is available six weeks after the end of the month concerned.

III. External Sector, Debt Sustainability, and Financing Requirement

31. In the external sector, the government will pursue its objective of reducing the balance of payments current account deficit by applying the macroeconomic and structural adjustment policies described in this memorandum without imposing restrictions on current transactions.

32. Overall, the balance of payments current account deficit (excluding official transfers) is projected at US$31 million in 2000, or 62 percent of GDP (compared with 54 percent in 1998 and 57 percent in 1999). Taking into account amortization of the external public debt (US$3.5 million), the amount of external payment arrears (US$57.2 million) and the target for improving the central bank's international reserves position (US$5.8 million), the gross external financing requirement will total US$97.5 million. This financing requirement will be partially covered by grants and concessional project loans (US$19.2 million), food aid (US$1.8 million), proceeds from oil exploration concessions (US$5 million), fishing royalties (US$0.7 million), and flows of private capital, including direct investments in the oil sector (US$6.8 million). In addition, the government intends to use the first-year disbursements for the arrangement it has requested under the PRGF (US$2.6 million) to cover partially this financing need, and to request a rescheduling of its external debt service from Paris Club creditors (US$59.1 million) on Naples terms, with a 67 percent reduction in the net present value of its debt, as soon as the Fund approves the arrangement requested under the PRGF. It will seek comparable treatment from other bilateral creditors. A financing gap of US$2.4 million will remain. São Tomé and Príncipe will seek concessional nonproject financing from the World Bank, AfDB, and other multilateral and bilateral donors to close the gap. In this regard, the government will organize a donors' meeting in São Tomé by end-June 2000 with assistance from the UNDP. It will provide financing assurances for the first year of the program on the occasion of the first review.

33. With a net present value of 14 times the exports of goods and services in 1999, São Tomé and Príncipe's external public debt is excessively large and will remain unsustainable for many years to come. This being the case, the government will continue to seek grants and loans only on a very concessional terms in order to cover its financing needs. In this connection, it will neither contract nor guarantee any new external nonconcessional borrowing (with a grant element of less than 50 percent) with a maturity exceeding one year.

Furthermore, the government will neither contract nor guarantee external borrowing with an initial maturity of less than one year. With a view to normalizing its relations with its major external creditors and donors, São Tomé and Príncipe settled all of its nonreschedulable external payment arrears in 1999, and will remain current on its nonreschedulable external debt-service obligations during the program period. A continuous performance criterion will apply to the nonaccumulation of new nonreschedulable external payments arrears.

IV. Program Monitoring

34. To monitor progress in the implementation of the program, the government has set quantitative performance criteria, benchmarks, and indicators for end-March, end-June, end-September, and end-December 2000 (Table 1), as well as structural performance criteria and benchmarks (Table 2). The government will also provide the Fund with statistical data and other information that Fund staff may deem necessary or may request for the purposes of monitoring the program. During the program period, the government will neither introduce new restrictions, nor expand existing restrictions, on payments and transfers in connection with current international transactions without the approval of the Fund. It will neither introduce multiple exchange rate practices, nor enter into any bilateral payments agreement incompatible with Article VIII of the Fund's Articles of Agreement. Lastly, the government will not introduce or expand restrictions on imports for balance of payments reasons.

35. The government will conduct two reviews of the program with the Fund in order to assess progress made during the first year, the first of these reviews by end-September 2000 and the second by end-March 2001.

36. The Economic Council, chaired by the Prime Minister and including the Minister of Planning, Finance and Cooperation, the Minister of Economy, the Minister of Infrastructures, Natural Resources, and Environment, and the Governor of the Central Bank, will coordinate the program. The council will continue to be supported by a technical committee responsible for monitoring program implementation. Each week, the technical committee will report on program implementation to the Economic Council, and the Minister of Planning, Finance and Cooperation will report to the Council of Ministers. The Economic Council and its technical committee will also oversee the preparation and implementation of the government's policy for the oil sector, including conducting negotiations with oil companies. In this connection, the head of the administrative unit for oil policy will participate, as needed, in the meetings of the technical committee responsible for program monitoring.

Attachments

Table 1. São Tomé and Príncipe: Quantitative Performance Criteria and Benchmarks for the 2000 Program

(In millions of dobras, unless otherwise specified)

	1998	1999	2000			
	Dec	Dec.	March	June	Sep.	Dec.
			Program			
I. Quantitative benchmarks and performance criteria 1/						
1. Floor on primary balance of the central government's financial operations, excluding foreign-financed investments (cumulative from beginning of year) 2/ 3/	1,945	4,327	1,549	2,863	7,156	8,499
2. Ceiling on changes in net bank credit to the central government (cumulative from beginning of year) 2/	6,270	-12,796	8,311	2,704	-6,213	-25,276
3. Ceiling on changes in net domestic assets of the central bank (cumulative from beginning of year) 2/	-10,295	-16,701	8,331	2,744	-6,153	-25,196
4. Floor on changes in the net international reserves position of the central bank (cumulative from beginning of year; in millions of U.S. dollars) 2/	2.0	2.1	-1.1	-0.3	0.8	3.5
5. Ceiling on central government's nonreschedulable outstanding external payments arrears (in millions of U.S. dollars) 4/	33	29	29	0	0	0
6. Ceiling on contracting and guaranteeing new nonconcessional borrowing by the central government with a maturity of more than one year (cumulative from beginning of year; in millions of U.S. dollars) 5/	0	0	0	0	0	0
7. Ceiling on change in the central government's outstanding stock of short-term external credit with a maturity of less than one year (cumulative from beginning of year)	0	0	0	0	0	0
II. Quantitative indicators						
1. Floor on total central government revenue (cumulative from beginning of year) 2/	54,502	64,605	17,480	33,973	51,466	75,277
2. Ceiling on primary spending of the central government, excluding foreign-financed investments (cumulative from beginning of year) 3/	53,076	60,279	15,930	31,111	44,310	66,778
Memorandum items:						
Exceptional financial assistance (cumulative from beginning of year)	0	0	0	0	0	0
Oil concession rights proceeds	27,709	21,492	0	14,646	14,646	36,960
Fishing royalties (cumulative from beginning of year)	5,204	884	2,473	2,923	3,368	4,889
Exchange rate (in dobras per U.S. dollar; period average)	6,927	7,093	...	...	...	...

1/ Performance criteria for end-June and end-December 2000.

2/ The ceiling or the floor will be adjusted downward (or upward) to accommodate the positive (or negative) deviation between actual and projected disbursement of exceptional financial assistance, oil concession rights proceeds, and receipts of fishing royalties. The adjustment for shortfalls is capped at Db 2,000 million for fishing royalties and at Db 20,000 million for oil concession rights proceeds.

3/ Based on a definition of expenditure excluding all interest payments and foreign-financed investment.

4/ Nonaccumulation of nonreschedulable new external payments arrears is a continuous performance criterion.

5/ With a grant element of less than 50 percent.

Table 2. São Tomé and Príncipe: Structural Performance Criteria and Benchmarks for the 2000 Program

Measures	Timetable
1. Preparation of a report identifying redundant civil servants and providing the assessment of the civil service downsizing resulting from the implementation of the organizational and staffing plans, as specified in paragraph 14.	End-April 2000
2. Adoption by the government of a privatization program of large agricultural estates and a law simplifying real property and land ownership, as described in paragraph 25. 1/	End-June 2000
3. Submission to parliament of a draft law governing petroleum exploration and production, as indicated in paragraph 26.	End-June 2000
4. Adoption of a three-year public investment program for 2001-03 in accordance with the program, as specified in paragraph 16.	End-September 2000
5. Adoption of a mechanism by which adjustments in water and electricity rates reflect changes in production and distribution costs, as indicated in paragraph 24. 1/	End-September 2000
6. Submission of monthly monetary data within six weeks of the end of each month, as indicated in paragraph 30.	Continuous

1/ Performance criteria.

São Tomé and Príncipe: Relations with the Fund
(As of February 29, 2000)

I. **Membership Status**: Joined 9/30/77; Article XIV

		SDR Million	% Quota
II.	**General Resources Account**:		
	Quota	7.40	100.0
	Fund holdings of currency	7.40	100.0

		SDR Million	% Allocation
III.	**SDR Department**:		
	Net cumulative allocation	0.62	100.0
	Holdings	0.00	0.0

IV. **Outstanding Purchases and Loans**: None

V. **Financial Arrangements**:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Structural Adjustment Facility	6/02/89	6/01/92	2.80	0.80

VI. **Projected Obligations to the Fund**: None

VII. **Exchange Rate Arrangement**:

Between July 22, 1987 and December 2, 1994, São Tomé and Príncipe's currency, the dobra, was pegged to a basket of currencies of the country's seven major trading partners. After August 1991, the exchange rate of the dobra was determined on the basis of a crawling peg, with the objective of progressively depreciating the dobra in real effective terms. Since December 1994, the official exchange rate has been market determined. The intervention currency for the dobra is the U.S. dollar. The official exchange rate of the dobra was Db 6,885 per U.S. dollar on December 31, 1998 Db 7,300 on December 31, 1999 and Db 7,350 per U.S. dollar on February 29, 2000.

VIII. **Article IV Consultations with the Fund**

The last Article IV consultation with São Tomé and Príncipe was concluded by the Executive Board on July 13, 1998. The decision adopted was as follow:

1. The Fund takes this decision relating to São Tomé and Príncipe's exchange measures subject to Article VIII, Section 2(a) and 3, and in concluding the 1998 Article XIV consultation with São Tomé and Príncipe, in the light of the 1998 Article IV consultation with São Tomé and Príncipe conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. As described in SM/98/148, São Tomé and Príncipe maintains restrictions on the making of payments and transfers for current international transactions in accordance with Article XIV, Section 2, except for the restriction on allocations of foreign exchange for imports of certain essential goods through the Chamber of Commerce that is subject to Fund approval under Article VIII, Section 2(a). São Tomé and Príncipe also maintains multiple currency practices arising from the existence of spreads of more than 2 percent between the official rate and the free market rates, which are subject to Fund approval under Article VIII, Sections 2(a) and 3. The Fund encourages the authorities to eliminate all remaining restrictions and multiple currency practices as soon as possible.

In the event, São Tomé and Príncipe reduced the spread between the official exchange rate and the free market rate to less than 1.5 percent from an average of 2.5 percent in 1997.

IX. **Technical Assistance** (since 1991)

From January to December 1991, a member of the Monetary and Exchange Affairs Department (MAE) panel was assigned to the national bank to assist with the implementation of the new system of accounts. In 1992, another MAE panel expert provided assistance in the area of banking operations. During 1993, two advisors were assigned to the Central Bank of São Tomé and Príncipe to assist in banking supervision and foreign exchange management. From July 1994 to November 1995, an expert in banking supervision was assigned to the central bank. Another expert was assigned as advisor to the central bank for the period July 1995 through December 1996. In March 1997, a diagnostic mission visited São Tomé and Príncipe in order to assess the need for future technical assistance. Starting in January 1998, an advisor has been assigned to the central bank. In March and in June 1999, a MAE mission visited São Tomé and Príncipe to help the central bank establish procedures for effective internal control and inspection, and in January 2000 another MAE mission helped strengthen bank supervision.

From January to June 1995, an expert from the Statistics Department (STA) was assigned to the central bank to help improve the presentation of the monetary accounts and provide assistance in the compilation of balance of payments statistics. During the period April 23-May 6, 1997, a money and banking statistics mission reviewed the procedures for gathering and compiling monetary statistics at the central bank and advised on the establishment of a system for regularly reporting data to the Fund.

A member of the Fiscal Affairs Department (FAD) panel was assigned to the Ministry of Economy and Finance from July 1991 to January 1994, to assist in the implementation of tax reforms.

X. Resident Representative

A Fund resident representative has been recently assigned to São Tomé and Príncipe. Mr. Norbert Toé, who also covers Gabon and resides in Libreville, took up his position in November 1999.

São Tomé and Príncipe: Relations with the World Bank Group

IDA operations

1. São Tomé and Príncipe joined the Bank and IDA in 1977, and became a borrower in 1985, when a line of credit of SDR 5.3 million (US$5.0 million equivalent) for an economic rehabilitation and modernization project was approved. The credit supported a series of institutional reforms and covered the foreign exchange cost of small investments in agriculture, transport, and energy.

2. In support of the government's structural adjustment program (1988-89) and reforms in the agricultural sector, IDA approved in 1987 a loan of SDR 6.1 million (US$7.9 million equivalent) for a cocoa rehabilitation project. In 1989, IDA approved a structural adjustment credit of SDR 3.1 million (US$4.0 million equivalent), together with SDR 2.3 million (US$3.0 million equivalent) from the Special African Facility and cofinancing of US$8.5 million from the African Development Fund.

3. A second structural adjustment credit was approved on June 26, 1990. This IDA credit was to provide SDR 7.5 million (US$9.8 million equivalent), with cofinancing of US$14.4 million from the African Development Fund and the government of Sweden, to maintain support for the government's structural adjustment program. A technical assistance component supported institutional reforms. The first tranche was disbursed in September 1991, and the second in November 1992. The third and final tranche was approved in January 1996 and disbursed.

4. To mitigate the effects of the adjustment program on the most vulnerable population groups, mainly the poor and the redundant civil servants, IDA approved in June 1989 a multisector loan of SDR 3.9 million (US$ 5.0 equivalent). The loan financed projects in infrastructure, health and education, environmental protection, and private sector activities. A second multisector loan of SDR 4.6 million (US$6.0 million equivalent) was approved in June 1991, focusing on water supply and road rehabilitation.

5. In 1991, IDA approved a loan of SDR 7.4 million (US$9.8 million equivalent) to further assist the agricultural development strategy. The main objectives of this project are (a) to support the distribution and leasing of about 20,000 hectares of land from public estates to smallholders and medium-sized private enterprises; (b) to assist financially the laborers leaving the estates; (c) to assist technically and financially the privatization of the cocoa estates; (d) to finance ongoing investments in the cocoa plantations; and (e) to strengthen agricultural sector administration and support services.

6. In order to improve social conditions, IDA approved in March 1992 a health and education loan of SDR 8.2 million (US$11.4 million equivalent), which finances a malaria control program and provides essential drugs, education supplies, and textbooks.

7. The FY 2000 Business Plan focuses on the government's capacity to identify and implement growth strategies, using more effectively the large amounts of aid the country already receives. The plan comprises the following elements:

- It updates the 1996 strategy note to get a comprehensive and strategic view of IDA grant programs to São Tomé and Principe. Through IDF grants, the plan assists the government in (a) reforming the energy sector; (b) formulating a strategy in the agricultural sector; (c) strengthening planning, budget implementation, and control; and (d) supporting the ongoing administrative reform.
- The plan strengthens public resource management through periodic public finance reviews.
- It strengthens supervision of the two ongoing projects (Agricultural Privatization and Smallholder's Development; Health and Education Project).
- An adjustment operation could be considered if, inter alia, macroeconomic progress in the first half of 2000 is satisfactory.

Statement of IDA Credits as of February 29, 2000
(In millions of U.S. dollars)

Credit Number	Fiscal Year	Purpose	IDA Commitment[1]	Undisbursed
1590	1985	Economic rehabilitation	5.0	0.0
A029	1987	Structural adjustment credit	3.0	0.0
1825	1987	Structural adjustment credit	4.0	0.0
1830	1987	Cocoa rehabilitation credit	7.9	0.0
2038	1989	Multisector credit	5.0	0.0
2165	1990	Second structural adjustment credit	9.8	0.0
2280	1991	Multisector II credit	6.0	0.0
2325	1991	Agricultural sector	9.8	0.7
2343	1992	Health and education	11.4	2.7
Total:			61.8	3.4
	Of which repaid:		0.8	

IFC operations

8. São Tomé and Príncipe is not a member of the IFC.

[1]Less cancellation

São Tomé and Príncipe: Statistical Issues

Introduction

1. The March 1998 edition of *International Financial Statistics (IFS)* introduced a page for São Tomé and Príncipe but substantial deficiencies remain in economic statistics. The authorities prepare data for Fund missions but publish only some statistics on a regular basis.

National accounts

2. Statistics on GDP/GNP are compiled on a yearly basis and provided at the time of the Article IV consultation. In 1995, the official series on GDP since 1990 was revised upward in order to include value added in the construction and financial sectors, and domestic consumption and investment were raised to take account of foreign-financed outlays. In July 1996, the World Bank and the French Ministry of Cooperation provided technical assistance in this area and recommended: (a) a simplification and revision of the methodology for surveying the formal sector; (b) the implementation of a survey on the informal sector and nongovernmental organizations (NGOs); and (c) improved communication with customs, so that more detailed and timely statistics on international trade can be obtained. The recent adoption of the following measures should also lead to improvement in GDP statistics: (a) a homogeneous accounting system has just been implemented by all enterprises; (b) the list of enterprises was updated; (c) parliament is to ratify shortly the institutionalization of identification numbers, which should facilitate data collection; and (d) the consumer price index (CPI) methodology was revised. In April 1998, the National Institute of Statistics published revised GDP statistics for 1995-97, based on enterprise surveys carried out during 1995 and 1996 with technical and financial assistance from the United Nations Development Program (UNDP).

Consumer prices

3. The CPI is calculated monthly and reported to the Fund, with a lag of one to two months. In 1995, the UNDP assisted the authorities in conducting a new household survey, which has been used as a basis for the compilation of the official CPI starting in 1997. The data submitted in the last two years are more regular and provide a statistical base, which constitutes a major improvement over the past.

Government finance statistics

4. Fiscal data are compiled on a monthly basis, with a lag of one to two months. The quality of data on expenditure and revenue has improved significantly. Moreover, since 1996, each category of expenditure is recorded separately by ministry. However, a number of problems remain:

- Expenditures on projects financed and directly managed by donors (e.g., medical personnel directly paid overseas) are not adequately monitored by the Directorate of Finance.

- Discrepancies remain between debt-service payments as recorded by the treasury and by the central bank's debt-management office.

Monetary statistics

5. A money and banking statistics mission that visited São Tomé and Príncipe in 1997 found that the authorities had made considerable progress in improving the money and banking statistics in accordance with STA's recommendations. The *IFS* page includes sections on exchange rates and interest rates, international liquidity, monetary accounts for the monetary authorities and the deposit money banks, and the monetary survey. Data on net foreign assets of the monetary system are still not considered reliable because of a number of factors, including problems in revaluing the central bank's foreign assets and liabilities.

External sector

6. **Exchange rates.** The authorities record data on five exchange rates: the official, the *bureau de change*, the international commercial bank (BISTP), the Banco Comercial do Equador (BCE), and the parallel rates. These rates are reported to the Fund with a lag of one to two months. The rates are recorded on a daily basis in order to compute the official rate as a weighted average of the market rates for the previous day.

7. **Exports and imports**. Monthly data on the main exports and imports are reported to the Fund irregularly, and occasionally include unit prices and volumes of exports. Progress in data reporting was realized in 1995-97 with the introduction of a computerized customs system (SYDONIA). However, data produced with the new system—which records, according to a standardized code, the value of imports or exports, as well as the taxes paid for each transaction—still contain large reporting errors.

8. **Balance of payments**. In 1995, the central bank began compiling balance of payments statistics and started setting up surveys to collect information on services and current and capital transfers. However, transmission of balance of payments data has proved to be irregular; no data have been received since December 1997. A number of other important problems pertaining to the quality of data remain, including uncertainty about the composition of project grants as recorded by the central bank. The reporting of external debt and private transfers also appears to be weak.

São Tomé and Príncipe: Core Statistical Indicators

(As of February 29, 2000)

	Exchange Rates	Interna-tional Reserves	Central Bank Balance Sheet	Reserve/ Base money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Govern-ment Balance	GDP/ GNP	External Debt/ Debt Service
Date of Latest Observation	Jan. 2000	Jan. 2000	Jan. 2000	Jan. 2000	Dec. 1999	Nov. 1999	Jan. 2000	Sept. 1999	Sept. 1999	Dec. 1999	Dec. 1997	Dec. 1999
Date Received	Feb. 2000	Feb. 2000	Feb. 2000	Feb. 2000	Feb. 2000	Nov. 1999	Feb. 2000	Nov. 1999	Nov. 1999	Jan. 2000	May 1998	Feb. 2000
Frequency of Data 1/	D	M	M	M	M	V	M	M	A	A	A	Q
Frequency of Reporting 1/	V	M	M	M	M	V	M	V	V	M	V	V
Source of Update 2/	A	A	A	A	A	A	A	A	A	A	A	A
Mode of Reporting 3/	C/T/E/V	C/E/V	C/E/V	C/E/V	C/E/V	C/T/E/V	C/V	C/V	V	C/E/V	V	V
Confidentiality 4/	C	C	C	C	C	C	C	C	C	C	C	C
Frequency of Publication 1/	M	M	M	M	M	Q	M	Q	A	A	A	Q

1/ D=daily ; M=monthly ; Q=quaterly ; A=annually ; V=irregularly
2/ A=direct reporting by the authorities
3/ C=cable or fax simile ; T=telephone ; E=email ; M=mail ; V=staff visits
4/ C=publicly released information

São Tomé and Príncipe: Basic Data

Area, population, and GDP per capita	
Area (square kilometers)	1,001
Population (1998)	
Total	137,707
Annual growth rate (in percent)	2.5
GDP per capita (in U.S. dollars; 1998)	295

	1992	1993	1994	1995	1996	1997	1998 Est.
				(In units indicated)			
Production and prices							
GDP at market prices (in millions of dobras)	14,565	20,469	36,295	64,613	98,900	200,000	281,000
Cocoa production (in metric tons)	3,688	4,305	3,392	3,845	3,500	3,138	3,928
Cocoa exports (in metric tons)	4,363	3,725	3,716	3,362	3,170	2,840	3,800
Consumer price index (annual average; 1996=100)	31.8	41.8	53.0	72.7	100.0	168.2	253.1
				(In millions of dobras)			
Government fiscal operations							
Revenue and grants	4,264	7,102	11,186	25,777	36,547	86,773	81,747
Current expenditure	4,408	6,673	11,285	15,480	26,796	55,675	80,709
Of which : interest obligations	1,601	2,347	3,982	7,782	9,867	22,524	34,810
Capital expenditure	5,942	7,309	15,502	34,563	41,591	84,499	87,328
Net lending	0	0	0	-72	0	0	-519
Overall fiscal balance (commitment basis)	-6,086	-6,881	-15,601	-24,195	-31,839	-53,401	-85,771
Net change in arrears (decrease -)	352	2,062	3,955	5,433	4,899	20,979	21,110
Overall fiscal balance (cash basis)	-5,733	-4,819	-11,646	-18,763	-26,941	-32,423	-64,661
Financing	5,733	4,819	11,646	18,763	26,941	32,423	64,661
Net foreign financing	3,722	4,267	8,016	18,616	15,972	53,358	14,873
Net domestic financing	2,011	552	3,630	146	10,968	-20,935	49,788
Monetary survey (end of period) 1/							
Net foreign assets	-4,999	-8,898	5,575	12,867	23,453	108,185	113,062
Net domestic assets	9,470	14,840	9,164	10,094	15,763	-36,134	-23,348
Net domestic credit	10,559	11,808	12,274	11,418	17,699	-25,725	-3,089
Claims on the government (net)	5,081	5,633	6,755	7,829	18,562	-12,523	4,272
Counterpart funds (nonbudgetary)	-4,736	-5,527	-9,067	-10,942	-9,666	-20,600	-24,271
Credit to the economy	10,213	11,702	14,587	14,531	8,803	7,398	18,109
Of which: public enterprises	8,455	8,307	...	...	...	...	-1,200
Other items (net)	-1,088	3,032	-3,110	-1,324	-1,936	-10,409	-20,259
Money and quasi money	4,472	5,942	14,739	22,961	39,216	72,051	89,714
				(In millions of U.S. dollars)			
Balance of payments							
Exports, f.o.b.	5.3	5.2	5.9	5.1	4.9	5.3	4.7
Of which: cocoa	4.2	4.2	5.0	4.7	4.8	4.6	4.6
Imports, f.o.b.	-22.5	-25.6	-24.3	-23.4	-19.8	-19.2	-16.8
Trade balance	-17.2	-20.4	-18.5	-18.3	-14.9	-13.9	-12.1
Services and income (net)	-18.0	-16.9	-16.3	-23.3	-21.2	-19.8	-10.3
Transfers (net)	12.0	13.0	18.1	23.3	22.1	32.1	13.8
Current account deficit, excluding transfers	-34.1	-35.9	-31.3	-41.1	-36.1	-33.7	-22.3
Current account deficit, including transfers	-23.2	-24.4	-16.6	-17.8	-14.0	-1.6	-8.5
Medium- and long-term capital (net)	13.1	8.8	7.0	10.8	11.8	2.7	5.5
Short-term capital and errors and omissions	-1.0	0.2	1.9	0.2	-2.6	0.0	-3.2
Overall balance	-11.1	-15.3	-7.7	-7.4	-4.8	1.1	-6.3
Financing	11.1	15.3	7.7	7.4	4.8	-1.1	6.3
Change in net foreign assets (increase -)	2.0	4.7	-2.1	-0.4	0.1	-7.4	2.7
Change in arrears (reduction -)	6.1	9.2	-2.0	-21.9	5.0	6.5	3.7
Structural Adjustment Facility (net)	0.0	0.0	-0.1	-0.2	-0.2	-0.2	-0.2
Debt relief	3.1	1.4	11.9	29.9	0.0	0.0	0.0

São Tomé and Príncipe: Basic Data (concluded)

	1992	1993	1994	1995	1996	1997	1998 Est.
	(In millions of U.S. dollars, unless otherwise specified)						
Gross foreign reserves							
End of period	10.7	6.0	4.8	5.1	5.0	12.4	9.7
In months of following year's imports, c.i.f.	3.0	1.8	1.3	1.5	1.5	5.1	2.9
External public debt							
Medium- and long-term debt (disbursed and outstanding)	162.5	181.4	198.1	226.8	234.0	235.5	244.9
Debt-service ratio before debt relief (as percent of exports of goods and services)	116.5	124.7	101.1	110.3	73.5	71.7	77.65
Effective exchange rate indices (trade weighted; end of period; 1992=100)							
Nominal	100.0	87.3	40.2	24.3	16.4	6.9	6.7
Real	100.0	96.9	56.2	39.9	42.4	31.8	35.9
Social indicators							
Life expectancy at birth (in years; 1995)	64						
Population (1998)	137,707						
Rural	59,981						
Urban	77,727						
Women	69,680						
Men	68,028						
Crude birth rate (per thousand, 1997)	33.8						
Crude death rate (per thousand, 1997)	8.5						
Infant mortality rate (under 1, per thousand; 1998)	64.0						
Infant mortality rate (under 5, per thousand; 1998)	123.0						
Population per physician (1995)	3,272						
Gross primary school enrollement ratio (in percent of school-age-population; 1998)	71.8						
Literacy rate for ages 15 and above (in percent; 1998)	78.0						

Sources: World Bank; and São Tomé and Príncipe authorities.

1/ Owing to corrections and improvements to the accounts of the central bank, there is a break in the series starting in 1995.

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IMF Concludes Article IV Consultation with São Tomé and Príncipe

On April 28, the Executive Board concluded the Article IV consultation with São Tomé and Príncipe.[1]

Background

Following a decade of very large macroeconomic imbalances and declining real per capita income, São Tomé and Príncipe achieved a good measure of macroeconomic stability and significantly liberalized the economy in 1998-99, under a staff-monitored program. The government's strategy was based on strong fiscal consolidation efforts, a tight monetary policy in the context of a flexible, market-based exchange rate regime, and vigorous structural reforms aimed at liberalizing the economy and streamlining the public sector. As a result, the primary budget balance turned around from deficit to surplus, inflation lowered, the exchange rate stabilized, and real GDP growth picked up. However, São Tomé and Príncipe's economic performance remains fragile, the debt burden is particularly heavy and unsustainable, and poverty is widespread.

In 1999, São Tomé and Príncipe faced a substantial weakening of its external position, reflecting a sizable deterioration in the terms of trade, a decline in cocoa production and exports, and higher investment-related imports. However, progress in economic liberalization began to alleviate structural rigidities, and the impact of the decline in cocoa production on economic activity was more than offset by a rapid expansion in trade, construction, and tourism, following increased foreign direct investment in hotel facilities. As a result, real GDP growth averaged an estimated 2.5 percent in 1998-99, compared with 1.2 percent in 1996-97. The implementation of tight financial policies contributed to a substantial reduction in inflation, with the 12-month rate of consumer price inflation falling to 13 percent in December 1999 from more than 80 percent at end-1997. The external current account deficit (including official transfers) widened from 4 percent of GDP in 1997 to 25 percent of GDP in 1999, but a strengthening of

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

the capital account through increased projects loans and direct foreign investment allowed gross international reserves of the central bank to stabilize at the equivalent of three months of imports.

In the fiscal area, the primary budget balance (excluding foreign-financed investments) turned around from a deficit of 2.2 percent of GDP in 1997 to a surplus of 1.3 percent of GDP in 1999, as higher tax revenue collection more than offset spending overruns. Monetary policy remained tight, as the central bank maintained the reserve requirement ratio at 22 percent and its discount rate 4 percentage points above inflation. On the structural front, the government liquidated a savings and loan institution, partially privatized the national petroleum products distribution company, and significantly liberalized trade and prices. Regarding governance issues, the authorities dealt decisively with a treasury bond fraud attempt uncovered in 1999 and hired a reputable firm to conduct an independent external audit of the central bank's foreign assets accounts as at end-1998.

The PRGF-supported program for 2000-02 aims at reducing the rate of inflation to 3 percent in 2001-02 and at containing the external current account deficit (including official transfers), which is projected to widen to 41 percent of GDP by 2002 because of increasing oil exploration investment. Real GDP growth is projected to rise to 4 percent by 2002, allowing per capita income to rise by 1.7 percent a year and helping to reduce poverty. In the fiscal area, the primary budget surplus (excluding foreign-financed public investment) would rise from 1.3 percent of GDP in 1999 to 5 percent of GDP in 2002 through tax administration measures aimed at raising revenue and containing domestically financed primary expenditures, while giving priority to health and education services. Fiscal consolidation should allow the treasury to increase its deposits at the central bank. Monetary policy will aim at reducing inflation and strengthening the international reserves position of the central bank in the context of a flexible exchange rate system. Key structural measures include (a) the implementation of a civil service reform and retrenchment program; (b) the implementation of a new public enterprise reform and privatization program; (c) the enhancement of transparency, accountability, and good governance, including in the central bank, the budget, and oil exploration operations; and (d) the preparation of a comprehensive poverty reduction strategy.

The authorities are committed to reducing poverty, improving the living conditions of the most vulnerable groups of the population, and strengthening the effectiveness of education and health services. They have adopted an interim poverty reduction strategy paper (PRSP) and launched a participatory process with civil society, with a view to finalizing a full PRSP by end-December 2001.

Executive Board Assessment

Executive Directors commended the São Tomé and Príncipe authorities for their satisfactory performance under the government policy framework in 1998 and the staff-monitored program in 1999. Directors observed that the strengthening in the fiscal position, the substantial lowering of inflation, and the narrowing in the spread between the official exchange rate and the parallel market rate of the currency were the result of sound macroeconomic policies, which had been implemented despite a sizable deterioration in the terms of trade during 1999. They also noted that the government had liberalized the price, trade, and exchange regimes, adopted a civil service reform program, and started the implementation of a public enterprise divestiture program.

However, Directors stressed that, while real GDP had increased, São Tomé and Príncipe's economic situation remains fragile—with its debt burden relative to exports being the heaviest in the world—and vulnerable to terms of trade fluctuations and the availability of foreign assistance. In the circumstances, they underscored the importance of consolidating the gains achieved in macroeconomic adjustment, accelerating the implementation of structural reforms, and developing a comprehensive strategy to diversify the economy and reduce poverty.

Directors emphasized the need to strengthen public finances further, and urged the authorities to adhere strictly to the fiscal policy stance agreed for 2000 and preserve the integrity of the budget by including all public investments in the budget and the public investment program. In this regard, they indicated that it is essential to strengthen control over expenditure commitments and contain nonpriority primary spending, including the wage bill, while providing adequately for education and health. It is also important to strengthen implementation capacity in the public sector. In addition, given the ambitiousness of the program, prioritization of policies is important to encourage improvement in social indicators. The consensus achieved among the authorities, labor unions, and the three main political parties on a cautious budget and wage policy for 2000, and on a comprehensive civil service reform agenda, has helped improve national ownership and ensure greater commitment to the successful implementation of the program.

Directors commended the authorities for the strong revenue collection performance in 1998-99, and for the elimination of all exports taxes and the adoption of a comprehensive customs tariff reform in early 2000. Noting the revenue shortfall expected from these trade liberalization efforts, they stressed the need to continue efforts to broaden the tax base and improve revenue collection.

Directors endorsed the tight monetary policy stance for 2000 and stressed the need to introduce open-market operations in July 2000 as intended. The large reduction in the spread between the official exchange rate and the parallel market rate was welcomed, and the central bank was encouraged to continue its efforts to unify the markets in the context of a flexible exchange rate regime.

Directors underscored the importance of carrying out the envisaged structural measures, including the full implementation of the civil service reform program, public enterprise reform and privatization, an overhaul of business legislation and regulation, and a strengthening of the judiciary in the area of contract enforcement. They also emphasized the need to enhance good governance, accountability, and transparency in public finances, central bank operations, and particularly oil operations.

Directors encouraged the authorities to strengthen the country's human and institutional capacity in economic management, with donor assistance, including in the areas of civil service reform, the privatization program, oil policy, and statistics and program monitoring. They also stressed the importance for the authorities and concerned donors to conduct the necessary household surveys and poverty assessments and develop an adequate series of social and poverty indicators in a timely manner, in order to prepare and implement a full-fledged poverty reduction strategy by end-2001, as intended, following a participatory process involving civil society.

Directors urged the authorities to regularize all domestic and external payments arrears and remain current on external debt-service obligations. They also encouraged the authorities to improve the quality and timeliness of external debt data and pursue prudent external debt management and borrowing policies in order to avoid a further increase in the external debt burden. Directors noted that São Tomé and Príncipe will continue to need financial assistance from the international community to help cover its financing needs during the period of the Fund-supported program. In view of the heavy and unsustainable debt burden, they stressed the importance of fully implementing the authorities' reform program in order to establish the required track record for debt relief under the enhanced HIPC Initiative.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. As part of a pilot project, the staff report (use the free Adobe Acrobat Reader to view this pdf file) for the 1999 Article IV consultation with São Tomé and Príncipe is also available.

São Tomé and Príncipe: Selected Economic Indicators, 1996-1999

	1996	1997	1998 Est.	1999 Est.
		(In units indicated)		
Gross domestic product (in millions of U.S. dollars)	44.9	43.9	40.6	47.1
At constant prices (percentage change)	1.5	1.0	2.5	2.5
Gross domestic product deflator (percentage change)	50.8	100.2	37.1	16.0
Consumer prices (percentage change; end of period)	51.7	81.1	20.8	12.6
Consumer prices (percentage change; average)	42.0	69.0	42.1	16.3
	(Annual percentage change, unless otherwise specified)			
External sector				
Exports, f.o.b.	-3.1	8.1	-11.2	-17.3
Imports, c.i.f.	-16.4	-3.2	-12.3	28.5
Exchange rate (in dobras per U.S. dollar; period average)	2,203.0	4,552.5	6,927.4	7,092.6
Exchange rate (in dobras per U.S. dollar; end of period)	2,833.0	6,969.7	6,885.0	7,300.2
Real effective exchange rate	1.4	-25.0	13.1	12.8
Terms of trade	8.6	11.4	14.8	-52.0
Money and credit (end of period)				
Net domestic assets 1/	28.2	-131.7	17.7	-10.6
Credit to government (net) 1/	59.1	-113.4	18.2	-14.3
Credit to the economy 1/	-28.2	-3.8	14.9	10.5
Broad money	82.2	94.5	24.5	3.6
Velocity (ratio of GDP to average broad money)	3.4	3.7	3.5	3.7
Central bank discount rate (in percent; end of period)	35.0	55.0	29.5	17.0
	(In percent of GDP, unless otherwise specified			
National accounts				
Consumption	113.7	116.5	107.0	108.5
Gross investment	56.2	49.1	35.8	40.0
Public investment	29.2	22.1	19.8	26.0
Private investment	27.0	27.0	16.0	14.0
Gross domestic savings	-13.7	-16.5	-7.0	-8.5
Gross national savings	25.0	45.5	14.7	14.6
Government budget				
Total revenue and grants	37.0	43.4	29.1	43.9
Of which: grants	23.5	27.8	9.7	24.6
Total expenditure	69.1	70.1	59.6	69.8
Of which: noninterest current expenditure	17.2	16.6	16.3	15.8
Overall balance (commitment basis)	-32.2	-26.7	-30.5	-25.8
Primary balance (commitment basis) 2/	-4.7	-2.2	0.7	1.3
External sector				
Current account balance (excluding official transfers)	-79.3	-74.8	-53.9	-57.2
Current account balance (including official transfers)	-30.8	-3.6	-21.1	-25.4
Total external debt outstanding	590.0	608.5	721.3	636.0
Net present value of total debt	343.0	408.4	471.8	420.4
Net present value of total debt 3/	1,446.0	1,441.9	1,634.6	1,450.1

Sources: São Tomé and Príncipe authorities; and IMF staff estimates and projections.

1/ In percent of broad money at beginning of period.

2/ Excluding interest obligations, grants, and foreign-financed capital outlays.

3/ In percent of exports of goods and services.