March 2008
IMF Country Report No. 08/95

Democratic Republic of São Tomé and Príncipe: Fifth Review Under the Three-Year Arrangement under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion—Staff Report; Press Release on the Executive Board Discussion; and Statement by the Executive Director for the Democratic Republic of São Tomé and Príncipe

In the context of the fifth review under the three-year arrangement under the Poverty Reduction and Growth Facility, and request for a waiver of a performance criterion, the following documents have been released and are included in this package:

- The staff report for the Fifth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion, prepared by a staff team of the IMF, following discussions that ended on October 12, 2007 with the officials of the Democratic Republic of São Tomé and Príncipe on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on December 4, 2007. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A press release of summarizing the views of the Executive Board as expressed during its December 21, 2007 discussion of the staff report that completed the review and request.

- A statement by the Executive Director for the Democratic Republic of São Tomé and Príncipe

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of the Democratic Republic of São Tomé and Príncipe
Memorandum of Economic and Financial Policies by the authorities of the Democratic Republic of São Tomé and Príncipe
Technical Memorandum of Understanding*
*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

Fifth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion

Prepared by the African Department
(In consultation with other departments)

Approved by J. A. P. Clément and Scott Brown

December 4, 2007

Program Review

- This report recommends completion of the fifth review under the PRGF arrangement based on São Tomé and Príncipe's performance and on understandings reached on policy implementation for the remainder of 2007 and 2008.

- All quantitative performance criteria for end-June 2007 were met. Staff supports the authorities' request for waiver of nonobservance of the June 2007 structural performance criterion, based on their remedial actions.

- The authorities have submitted the second annual PRSP progress report for IDA and IMF staff assessment.

Participants

- The mission (October 1-12, 2007) comprised Mr. Wang (head), Mr. Ronci, Ms. Farhan, and Ms. Takebe (All AFR). The staff team worked closely with a parallel World Bank mission. Mr. Shanghavi (AFR) helped to prepare the staff report.

- The mission met with Mr. A. Carvalho, former Governor of the Central Bank and now Minister of Planning and Finance (since late November 2007), Mrs. M. Tebús Torres, former Deputy Prime Minister and Minister of Planning and Finance, and other senior officials. They also met with the Speaker and other members of the National Assembly, representatives of the private sector, trade unions, the donor community, and the media.

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ABBREVIATIONS AND ACRONYMS

AML/CFT	Anti-Money-Laundering/Counter Financial Terrorism
BCSTP	Central Bank of São Tomé and Príncipe
DPO	Development Policy Operation of the World Bank
EEZ	Exclusive Economic Zone
EITI	Extractive Industries Transparency Initiative
EMAE	Water and electricity state enterprise
ENASA	Airport state enterprise
GDP	Gross domestic product
HIPC	Heavily indebted poor countries
IDA	International Development Association (of the World Bank
IFC	International Financial Corporation (of the World Bank Gr
JDA	Joint Development Agency (with Nigeria)
MEFP	Memorandum of Economic and Financial Policies
MDRI	Multilateral Debt Relief Initiative
NA	National Assembly
NIR	Net international reserves
MCC	Millennium Challenge Corporation
LOI	Letter of intent
INE	National Institute of Statistics
ORML	Oil Revenue Management Law
PRSP	Poverty Reduction Strategy Paper
SAFE	Public financial management system
eSAFE	Integrated computerized SAFE
SAFINHO	Pilot system for eSAFE
TMU	Technical Memorandum of Understanding

EXECUTIVE SUMMARY

Economic activity remains robust in 2007. Annual inflation declined through mid-2007 to 14 percent, from its peak of 26 percent in August 2006, and the real effective exchange rate depreciated. All quantitative performance criteria for end-June 2007 were met. In September 2007, the authorities raised domestic prices of petroleum products, electricity, and water, after international oil prices increased. Progress on structural reforms was mixed.

The authorities are committed to achieving the objectives of the 2007 program. Difficult negotiations with trade unions led to a general wage increase from July 2007 that is larger than the program envisaged. To achieve the targeted reduction in the domestic primary deficit, the authorities decided in October 2007 to cut nonwage spending for the remainder of the year.

The 2008 program aims to further reduce the domestic primary fiscal deficit and inflation. The authorities agreed to slow the pace of the wage increase to keep the share of nonwage priority expenditure sustainable and to rely primarily on fiscal restraint and a proactive monetary policy to contain pressures on domestic prices. Their structural reform agenda will focus mainly on removing impediments to private investment**.**

Risks to program implementation include heavy pressure for higher wages, weak implementation capacity, and uncertain oil prospects. Finding commercially viable oil reserves continues to be a long and uncertain process.

Staff recommends completion of the fifth review based on the country's performance and policy commitments. Staff supports the authorities' request for a waiver for the nonobservance of the end-June performance criterion related to prudential regulations, based on the authorities' remedial actions.

I. BACKGROUND

1. **São Tomé and Príncipe has a very narrow production and export base**. The once-dominant cocoa sector has declined in the last three decades. Tourism is relatively small and brings in little net foreign exchange receipts because it relies heavily on imported goods and services. The large external current account deficit has been financed by official transfers, private inflows, and in recent years oil signature bonuses. Exploratory drilling so far has not yet confirmed the existence of commercially extractable oil reserves.

2. **São Tomé and Príncipe reached the completion point under the enhanced HIPC Initiative in March 2007**. By September 2007, creditors representing over 80 percent of the country's external debt at the completion point had agreed to deliver HIPC relief, enabling the Fund to disburse its share of topping up assistance.[1]

II. PERFORMANCE UNDER THE ARRANGEMENT

3. **Economic activity continues to be robust in 2007, driven by foreign investment in tourism-related construction and services**. Real GDP is projected to grow at 6 percent, somewhat slower than in 2006, reflecting lower public expenditure and imports financed by oil bonuses (Figure 1 and Table 1).

4. **Inflation declined to 14 percent (year-on-year) by the end of June 2007**. The deceleration in the first half of 2007 reflected the authorities' efforts to reduce fiscal imbalances in the 2007 budget, and to curb liquidity growth. The dobra depreciated in real effective terms during the period, partially offsetting last year's real appreciation. In early September 2007, the government raised domestic prices of petroleum products by 14-25 percent, and electricity and water by 40-60 percent, as international oil prices increased.

5. **All quantitative performance criteria for end-June 2007 were met**. Domestic revenue fell short of the program target for the first half of the year, mainly because import duties and nontax revenue were lower than expected. The government met the performance criterion on the domestic primary deficit mainly by compressing capital expenditure. In addition, the wage bill was less than projected because a general wage increase of 18 percent did not take place at the beginning of the year as expected. The end-June structural performance criterion related to the issuance of prudential regulations was not met. However, all four required regulations were issued by mid-November 2007 (Appendix I, Attachment I, Table I.2).

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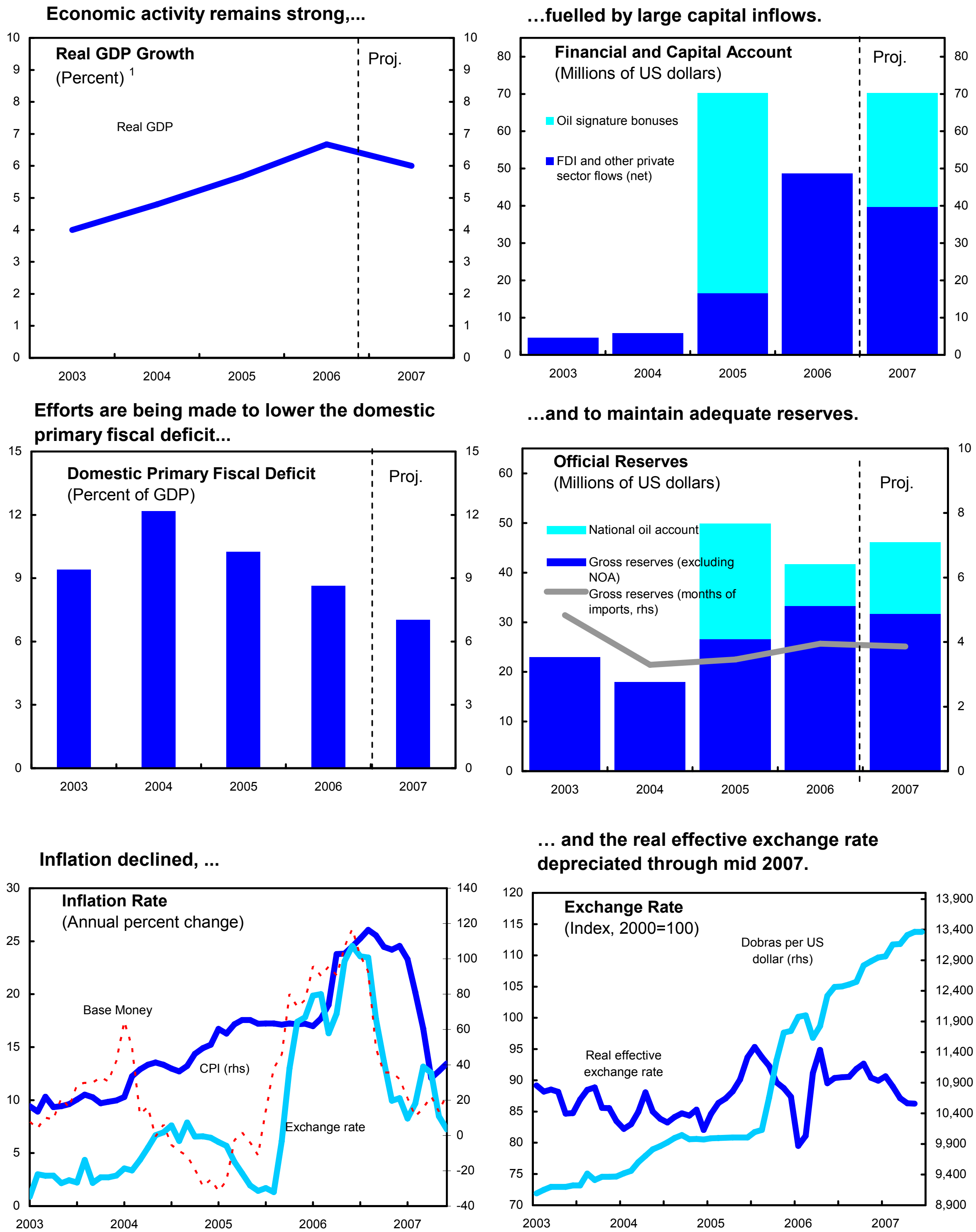
[1] See Press release 07/306.

Figure 1. Recent Macroeconomic Developments, 2003–07



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

[1] There is a break in the GDP data series between 2003 and 2004.

6. **Fiscal developments since July 2007 have complicated program implementation**. Protracted negotiations with trade unions led to a 35 percent general wage increase effective from July 2007. More overtime payments were also made to teachers and health workers. The wage bill is thus projected at 9.1 percent of GDP for the year, rather than 8.2 percent under the program (Table 2). Moreover, domestic revenue for the year is expected to be lower than programmed by about 1 percent of GDP, in part due to an unexpected shortfall in the oil-related grant. Higher public expenditure in the third quarter and the petroleum price increase put pressure on inflation and exchange rate depreciation.

7. **The central bank (BCSTP) strengthened its efforts to control liquidity growth**. It continued to sterilize the budgetary use of oil bonuses and HIPC savings through foreign exchange sales. As a result, the 12-month base money growth declined from over 110 percent in mid-2006 to about 20 percent in mid-2007 (Table 3). Since then, the dobra component of base money grew by about 20 percent, excluding base money changes due to a surge in foreign currency bank reserves at the BCSTP. The velocity of money remained broadly unchanged.

8. **Progress on structural reforms has been mixed** (MEFP Table I.2). The authorities have been preparing monthly budget execution reports using the pilot budget preparation and execution program (SAFINHO). Agreement was reached with the U.S. Millennium Challenge Corporation (MCC) on a threshold program for technical assistance to strengthen revenue administration. However, final approval by the National Assembly (NA) of the corporate income tax law, along with the remainder of the tax reform package, awaits the submission of a revised draft of the personal income tax law. Regulations to implement the anti-money laundering law have not been issued because the NA has not yet given the law its final approval. The Oil Resource Management Law (ORML) Handbook is under a government review before its publication. Finally, some progress has been made by EMAE, the utility company, in installing the prepaid electricity meter systems, which reached about 1,000 meters in September 2007.

III. Policies for the Remainder of 2007

9. **The authorities remain committed to reducing the domestic primary deficit to 7 percent of GDP**. The recent adjustments of fuel and utility prices are expected to enable ENCO, the fuel importer, to clear its tax arrears of about 0.9 percent of GDP. The government also intends to reduce nonwage spending by about 1-2 percent of GDP from budgeted amounts, while protecting HIPC-related social spending. Expenditure commitments will be strictly controlled to prevent any build up of payment arrears (MEFP paras. 9, 10). To protect the poorest segments of the population, electricity and water tariffs have been linked to the level of consumption since October 2007.

Financing of the Domestic Primary Deficit
(Percent of GDP)

	2006	2007		2008
	Est.	Country Report 07/267	Rev. Prog.	Proj.
Domestic revenue [1]	**20.1**	**17.8**	**17.2**	**17.4**
Domestic primary spending	**28.7**	**24.8**	**24.2**	**22.2**
Of which: Wages	8.8	8.2	9.1	8.8
Transfers to JDA	2.5	2.2	2.1	0.6
Other [2]	17.5	14.4	13.0	12.8
Domestic primary balance	**-8.6**	**-7.0**	**-7.0**	**-4.8**
Financing	**8.6**	**7.0**	**7.0**	**4.8**
Use of oil bonuses	10.6	5.4	5.7	1.9
IDA [3]	0.0	0.0	0.0	2.5
Other, net [4]	-2.0	1.6	1.3	0.4

Sources: São Tomé and Príncipe authorities; and IMF staff estimates and projections.
[1] Excludes receipts of oil signature bonuses.
[2] Includes goods and services, non-essential current spending, domestically financed capital expenditure, and HIPC-related spending.
[3] World Bank Development Policy Operation grants.
[4] Includes debt relief of about US $1.5 million.

10. **The BCSTP will maintain a tight monetary policy to counter the pressures from higher energy costs** (MEFP para. 12). Since weak financial intermediation is limiting the effectiveness of monetary policy instruments, the authorities have to rely primarily on fiscal restraint and foreign exchange sales to contain pressures on domestic prices. Recognizing the tradeoff between NIR accumulation and sales of foreign exchange to mop up excess liquidity, they agreed that a proactive monetary policy needs to be supported by continued fiscal adjustment in order to bring annual inflation as close as possible to the original program target of 13-15 percent by the end of 2007.

11. **The authorities intend to accelerate public financial management reform**. They have prepared the 2008 budget consistent with the PRGF-supported program. With support from the World Bank, they also plan to upgrade SAFINHO, aiming to put in place a strengthened budget execution and monitoring system by March 2008. The government intends to adopt by the end of this year a petroleum sector strategy and the relevant laws consistent with the ORML and the Extractive Industries Transparency Initiative (EITI) to launch licensing for the Exclusive Economic Zone (EEZ) in 2008 (MEFP paras. 11, 13).

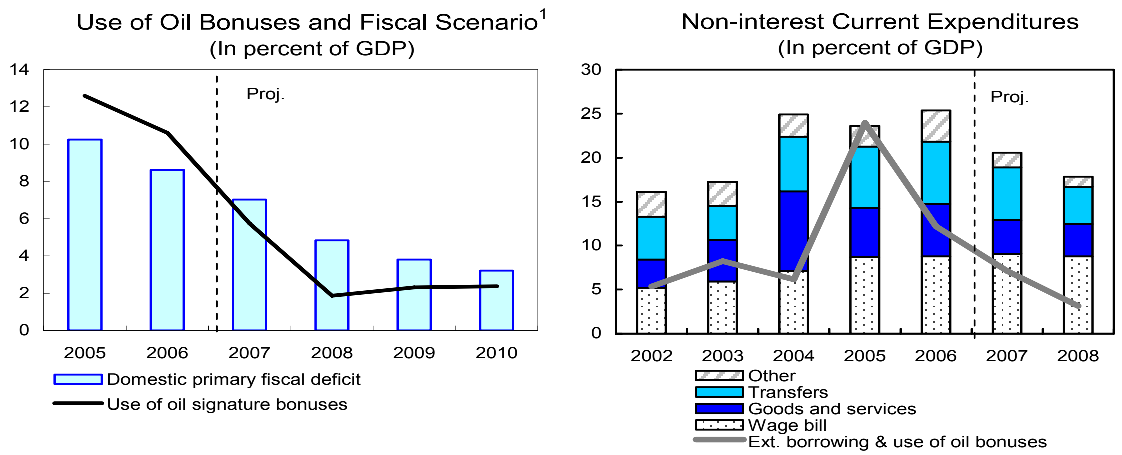
IV. The 2008 Program

12. **Economic policies in 2008 aim to consolidate macroeconomic stabilization gains and promote private-sector-led growth**. The authorities face two major challenges in 2008 and beyond: (i) maintaining fiscal sustainability with an uncertain oil outlook; and (ii) developing the country's production and export base to reduce poverty and aid dependence.

13. **The authorities and staff shared the view that the country's fiscal and external financing strategies need to adjust to the uncertain oil revenue prospects**. While in recent years oil bonuses have filled in budget financing gaps, the remaining balance in the National Oil Account (NOA) is low, the prospects of additional oil bonuses in 2008 are uncertain, and finding commercially viable oil reserves is a long and uncertain process. Besides mobilizing more foreign grant aid, continued fiscal adjustment is not only prudent but also necessary to safeguard macroeconomic stability and long-term growth prospects.

A. Fiscal Policy

14. **The draft 2008 budget aims to reduce the domestic primary deficit to 4.8 percent of GDP**. The domestic primary deficit is expected to be fully financed by a grant of 2.5 percent of GDP from the IDA Development Policy Operation (DPO), the use of existing oil bonuses equivalent to 1.9 percent of GDP, and other net external financing including debt relief.



Sources: São Tomé and Príncipe's authorities, and IMF staff estimates and projections.
1/ Baseline scenario assumptions: Oil production and exports start in 2014 and oil bonuses for block 5-6 are received in 2008.

15. **On the revenue side, the authorities intend to implement the direct tax reform package after its approval by the National Assembly**. The package includes a revised corporate tax law that reduces the rate from 45 to 25 percent, a new personal income tax law with a progressive tax structure, and a new urban property tax code (MEFP para. 17). Although these reforms are expected to be revenue-neutral in 2008, timely implementation would help reduce distortions and increase revenue buoyancy over time. With MCC support, the authorities also plan to strengthen tax and customs administration, including by stepping up efforts to audit tax returns and increase tax arrears' collection.

16. **Fiscal consolidation under the 2008 budget would come mainly from the expenditure side** (MEFP paras. 17, 18). The main elements of the expenditure program are:

- *Containing personnel costs*. After a sharp increase in 2007, the wage bill would increase by about 3 percent in real terms but fall relative to GDP from 9.1 percent in 2007 to

8.8 percent in 2008 (Box 1). As part of the DPO-supported program, the government plans to undertake a public wage reform, based on a comprehensive wage study, as a first step toward a civil service reform strategy. Key elements of the wage reform would include a revised salary structure and the integration of fringe benefits into the wage bill.

- *Curtailing nonwage nonessential current spending*. The adjustment of up to 2 percent of GDP would be mostly in discretionary expenditures (administrative expenses, fringe benefits, and other goods and services), returning these spending categories to their levels relative to GDP before the inflows of large oil bonuses.

- *Increasing domestically financed capital expenditure and pro-poor spending*. Allocations for maintenance, investment, and propoor programs are expected to increase, in line with the priorities identified by the PRSP.

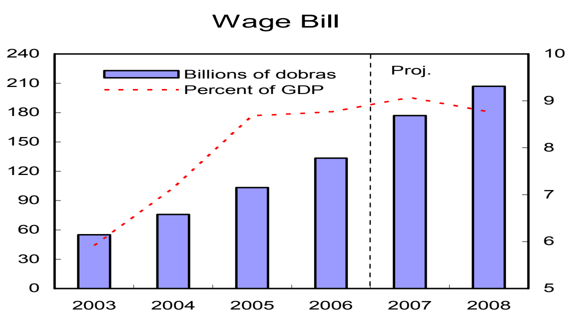
- *Strengthening budgetary execution and monitoring*. Efforts will be made to train staff and further develop SAFINHO.

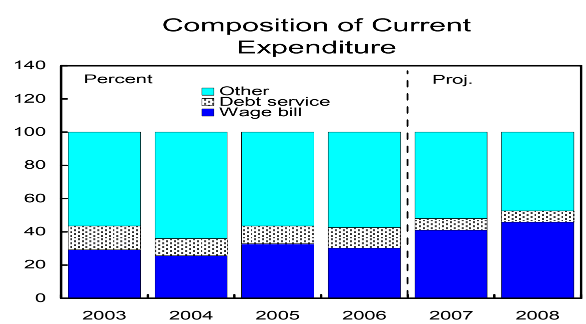
Box 1. The Wage Bill, Composition of Public Expenditure, and Fiscal Sustainability

The government wage bill has increased rapidly in recent years, financed in part by large inflows of oil bonuses. The increase reflected an expansion in the public payroll, a significant increase in real wages, and substantial overtime compensation and benefit payments.

Consequently, budgetary personnel costs accounted for an increasing share of public expenditure. If fringe benefits currently recorded under other current expenditures were included, the share would be even higher.

Maintaining fiscal sustainability is a serious challenge. In addition to civil service reform, the private sector needs to develop to provide alternative employment opportunities and to provide the basis for increasing domestic revenue.





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

B. Monetary and Exchange Rate Policies

17. **The monetary program aims to reduce annual inflation to 9-12 percent by the end of 2008, with base money as the anchor in the context of a flexible exchange rate regime** (MEFP para. 20). The BCSTP will continue to improve liquidity forecasts and proactively use monetary instruments, primarily foreign exchange sales, to ensure that 12-month base money growth, especially the dobra component, is on a declining trend. The authorities shared the view that their monetary policy needs to be supported by fiscal restraint, which is essential for containing aggregate demand (MEFP para. 21).

18. **The BCSTP is committed to deepening foreign exchange market reform**. In 2008, it would consider revising the mechanism for setting the daily central bank exchange rate to further narrow the spread between the central bank and commercial bank exchange rates. The investment code that has been submitted to the NA contains provisions that aim to remove the exchange restriction on transfers abroad of dividends. The BCSTP emphasized, however, that a dynamic export sector is needed to increase both foreign exchange supply and the participation of commercial banks in the market (MEFP para. 22).

C. Structural Reforms

19. **The authorities attached high priority to structural reforms that would help develop the supply side of the economy**. They considered that at the root of their persistent internal and external financial imbalances is the lack of development of the country's productive and export sectors (Box 2). Therefore, their reform agenda will focus on removing regulatory impediments, developing the financial sector, and upgrading the country' infrastructure.

20. **To attract private investment, the authorities intend to press ahead with regulatory reform**. They plan to adopt laws to sharply reduce the cost and duration of starting a business, modernize the country's commercial codes, and implement the new investment code and the revised labor code after NA approval (MEFP paras. 24, 25, 26).

21. **On financial sector reform, the BCSTP would further strengthen banking supervision, especially its enforcement capability**. Key measures include improving accounting standards and bank financial disclosures and putting in place an anti-money laundering regime (MEFP para. 27).

22. **With support from donors the authorities aim to start reforming the key sectors, including utility, transportation, and agriculture**. They plan to focus initially on addressing the financial weaknesses of EMAE, ENASA (the airport authority), and other state-owned entities, with a view to corporatizing and commercializing them over the medium term.

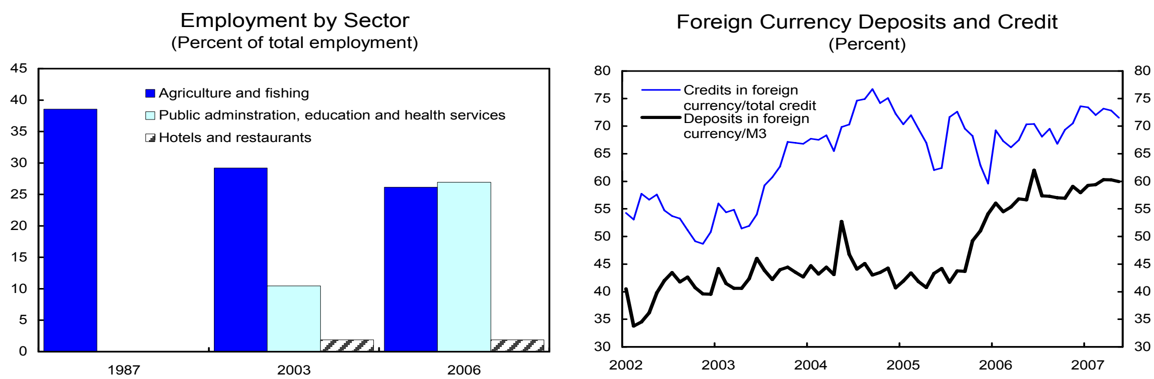
D. Debt Management

23. **The authorities are conscious of the need to maintain debt sustainability after HIPC and MDRI debt relief**. They are committed to refraining from new external borrowing, especially on non-concessional terms. Having recently secured debt relief from the EU, they plan to seek full delivery of HIPC debt relief, aiming to conclude agreements with Angola and Portugal, the two largest remaining creditors (MEFP para. 29).

Box 2. Impediments to Private Sector Development and Supply Constraints

A shrinking traditional sector. As output, exports, and employment have been declining in the cocoa sector, the government has become the largest employer in the economy in recent years.

Impediments to the development of new productive sectors. These include: (i) high cost of investing and doing business, as assessed by the IFC's *2008 Doing Business Report*; (ii) weak financial intermediation and difficulty in accessing financing, with high euro-rization; and (iii) poor infrastructure. These difficulties are compounded by the small size of the market.



Source: São Tomé and Príncipe authorities.

V. Program Monitoring and Risks

24. **The quantitative performance criteria related to the sixth review of the program for end-December 2007 remain unchanged** (Table 7). Indicative targets for end-March and end–June 2008 are proposed. The PRGF arrangement will expire on July 31, 2008. To simplify the use of adjustors in monitoring the 2008 program, indicative targets on NIR, NDA, and net credit to the government will include only unblocked oil funds (MEFP paras. 31, 32).

25. **Risks to the program arise primarily from social tensions and demand for higher wages, weak capacity in policy implementation, and unfavorable oil prospects**. The authorities' policy commitments should help contain these risks.

VI. Staff Appraisal

26. **São Tomé and Príncipe's performance under the PRGF-supported program has been encouraging**. Economic activity remains robust, inflation had fallen significantly by mid-year, the domestic primary deficit was contained, and central bank net international reserves exceeded the June 2007 program target. The authorities are to be commended for raising the domestic prices of petroleum products and utilities to reduce implicit subsidies. However, the larger than envisaged general wage increase in July 2007 has raised a difficult issue regarding fiscal sustainability.

27. **To consolidate the stabilization gains and safeguard fiscal sustainability, the government will need to significantly improve public financial management and address head-on the increasing wage bill to make room for public investment and poverty-reducing expenditure**. These are particularly important in view of the uncertain outlook for oil revenue. Timely implementation of the direct taxation reforms after approval by the National Assembly will help broaden the tax base to sustain public expenditure.

28. **Improving the investment climate through regulatory reform and upgrading infrastructure are vital for attracting private investment**. The authorities should press ahead with reforms to reduce the cost of investing and doing business and work with their development partners to upgrade infrastructure and the key economic sectors, including utility, transportation, and agriculture.

29. Staff recommends completion of the fifth review based on the country's performance and policy commitments. It supports the authorities' request for a waiver for the nonobservance of the end-June 2007 structural performance criterion related to the issuance of four prudential regulations, all of which were issued by November 2007.

Table 1. São Tomé and Príncipe: Selected Economic Indicators, 2005–2010 [1]

	2005	2006	2007		2008	2009	2010
	Actual	Est.	Country Report No. 07/267	Rev. Prog.	Projections		
	(Annual percentage changes, unless otherwise specified)						
National income and prices							
GDP at constant prices	5.7	6.7	6.0	6.0	6.0	6.0	6.5
Consumer prices							
End of period	17.2	24.6	13.5	19.6	9.5	7.0	6.0
Period average	16.3	23.1	16.6	19.9	14.1	8.2	6.5
External trade							
Exports, f.o.b. [2]	22.6	14.0	18.9	12.2	7.2	4.3	3.1
Imports, c.i.f.	15.7	65.9	0.9	-4.1	15.8	4.2	8.7
Exchange rate (dobras per US$; end of period) [3]	11,748	12,945	…	…	…	…	…
Real effective exchange rate (depreciation = -)	6.5	2.9	…	…	…	…	…
Money and credit (end of period)							
Base money	76.6	32.0	21.0	21.2	17.4	17.9	17.4
Broad money (M3)	45.9	39.3	25.0	25.2	21.0	20.2	18.6
Velocity (GDP to average broad money)	3.3	3.0	3.0	3.0	3.0	2.9	2.8
Central bank reference interest rate (percent)	18.2	28.0	…	…	…	…	…
Bank lending rate	30.0	31.0	…	…	…	…	…
Bank deposit rate	10.6	12.0	…	…	…	…	…
	(Percent of GDP, unless otherwise specified)						
Government finance							
Total revenue, grants, and oil signature bonuses [4]	81.9	37.5	164.5	164.7	48.8	30.6	30.0
Of which : tax revenue	15.1	17.5	15.8	15.2	15.6	15.7	15.8
nontax revenue	2.3	3.7	3.2	2.8	2.3	2.1	1.9
grants	17.2	16.2	125.4	125.6	14.4	12.8	12.3
oil signature bonuses	47.3	0.0	20.2	21.2	16.5	0.0	0.0
Total expenditure and net lending	44.5	51.5	39.6	39.3	37.1	35.6	34.8
Of which: personnel costs	8.7	8.8	8.2	9.1	8.8	8.6	8.4
nonwage noninterest current expenditure	14.9	16.6	11.8	11.5	9.1	8.1	7.7
capital and HIPC-related social expenditures	18.0	22.5	18.0	17.2	17.9	17.8	17.7
Domestic primary balance [5]	-10.3	-8.6	-7.0	-7.0	-4.8	-3.8	-3.2
Overall balance (commitment basis)	37.5	-14.0	124.9	125.4	11.7	-5.0	-4.8
External sector							
Current account balance [2]							
Including official transfers	-13.6	-45.7	-41.3	-35.8	-36.6	-33.4	-34.4
Excluding official transfers	-43.9	-72.9	-55.9	-57.5	-59.1	-53.6	-53.4
NPV of external debt	172.9	162.7	16.3	16.0	16.3	15.8	15.2
External debt service (percent of exports) [2 6]							
Before HIPC and MDRI debt relief	75.6	65.8	37.3	59.7	48.9	48.5	47.4
After HIPC and MDRI debt relief	62.1	33.8	4.7	7.5	6.7	6.2	5.8
Export of goods and services (US$ millions) [2]	15.9	17.2	24.5	15.3	20.1	21.5	22.8
Gross foreign reserves [7]							
Months of imports of goods and nonfactor services	4	4	4	4	4	4	4
Millions of U.S. dollar	26.6	33.3	31.7	31.7	28.9	34.6	37.1
National Oil Account (US$ millions)	23.5	8.6	14.3	16.2	40.0	38.0	35.4
Memorandum Item:							
GDP							
Billions of dobras	1,189	1,522	1,954	1,952	2,361	2,739	3,135
Millions of U.S. dollars	114	123	142	145	158	173	190

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

[1] Based on 2001 census and survey-based GDP series unless otherwise specified.

[2] Due to the revision of balance of payment data, the data of Country Report No. 07/267 and revised program are not comparable.

[3] Central bank buying rate.

[4] Includes HIPC and MDRI debt relief and oil signature bonuses.

[5] Excluding oil revenue, grants, interest earned, and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays.

[6] Percent of exports of goods and nonfactor services. The difference between debt service before and after HIPC relief is larger than debt service saving in cash terms because this table is on an accrual basis.

[7] Gross reserves exclude the National Oil Account and guarantee deposits placed at the BCSTP by financial institutions waiting for operating licenses.

Table 2. São Tomé and Príncipe: Financial Operations of the Central Government, 2005–2008

	2005	2006	2007				2008
		Est.	Jan.-Jun.		Jan.-Dec.		Proj.
			Country Report No. 07/267	Actual	Country Report No. 07/267	Rev. Prog.	
	(billion dobra)						
Total revenue and grants	**974**	**570**	**2873**	**538**	**3216**	**3214**	**1151**
Total revenue	207	324	155	137	372	351	422
Tax revenue	180	267	125	123	309	296	368
Nontax revenue	27	57	30	14	63	55	55
Grants	204	247	2324	19	2450	2450	339
Project grants	152	197	111	1	222	222	266
Nonproject grants	17	2	0	0	15	15	60
HIPC Initiative-related grants [1]	35	47	2213	18	2213	2213	13
Oil signature bonuses	562	0	394	382	394	413	390
Total expenditure	**528**	**783**	**364**	**252**	**774**	**766**	**875**
Current expenditure [2]	314	441	220	223	423	432	452
Of which: personnel costs	103	133	80	69	161	177	207
interest on external debt due	32	52	14	8	31	30	31
goods and services	66	91	34	42	81	74	87
transfers	83	108	65	84	91	117	100
Of which: JDA	33	38	43	41	43	41	15
other	28	54	26	18	59	33	27
Capital expenditure	186	307	123	16	294	277	353
Financed by the Treasury	21	51	22	7	45	29	45
Financed by external sources	165	256	100	8	249	248	308
HIPC Initiative-related social expenditure	28	35	21	14	58	58	71
Domestic primary balance [3]	**-122**	**-131**	**-97**	**-97**	**-137**	**-137**	**-114**
Overall fiscal balance (commitment basis)	**445**	**-213**	**2509**	**286**	**2442**	**2448**	**276**
Net change in arrears (reduction = -)	-134	21	0	7	0	0	0
External arrears [4]	-52	21	0	0	0	0	0
Domestic arrears	-82	0	0	7	0	0	0
Overall fiscal balance (cash basis)	**311**	**-192**	**2509**	**293**	**2442**	**2448**	**276**
Financing	**-311**	**192**	**-2509**	**-293**	**-2442**	**-2448**	**-276**
Net external	-37	31	-2383	-194	-2360	-2350	69
Disbursements (projects)	14	99	13	7	27	26	29
Program financing (loans)	0	24	10	13	20	27	30
Net short-term loans	0	0	-207	-200	-207	-202	0
Scheduled amortization [1]	-93	-92	-2224	-15	-2224	-2224	-13
Change in arrears (principal) [5]	-102	0	0	0	-140	-140	0
Bilateral rescheduling [6]	144	0	24	0	164	164	24
Net domestic	-274	162	-126	-99	-82	-98	-346
Net bank credit to the government	-277	162	-126	-99	-82	-98	-346
Banking system credit (excluding National Oil Account) [7]	-14	-23	-32	0	5	5	0
National Oil Account	-263	184	-94	-99	-87	-104	-345
Nonbank financing (including earmarked funds and residual)	3	0	0	0	0	0	0
Financing gap	0	0	0	-1	0	0	0
Memorandum items:							
Overall balance (commitment basis, incl. grants, excl. oil bonuses)	-117	-213	2115	-96	2048	2035	-114
Domestic primary spending	320	437	252	220	485	443	487
MDRI debt relief (flow in US$ million)	0	0	...	...	1.1	1.1	1.2
National Oil Account (US$ million, excl. transfers to budget)	23.5	8.5	14.2	8.6	14.2	16.2	13.2

continued

Table 2. São Tomé and Príncipe--Financial Operations of the Central Government, 2005–2010 (concluded)

	2005	2006	2007		2008	2009	2010
		Est.	Country Report No. 07/267	Rev. Prog.	Projections		
			(Percent of GDP) [1]				
Total revenue and grants	**81.9**	**37.5**	**164.8**	**164.7**	**48.8**	**30.6**	**30.0**
Total revenue	17.4	21.3	19.0	18.0	17.9	17.8	17.7
Tax revenue	15.1	17.5	15.8	15.2	15.6	15.7	15.8
Nontax revenue	2.3	3.7	3.2	2.8	2.3	2.1	1.9
Grants	17.2	16.2	125.6	125.6	14.4	12.8	12.3
Project grants	12.8	12.9	11.4	11.4	11.3	11.2	11.2
Nonproject grants	1.5	0.2	0.8	0.8	2.5	1.2	0.6
HIPC Initiative-related grants [2]	3.0	3.1	113.4	113.4	0.6	0.5	0.5
Oil signature bonuses	47.3	0.0	20.2	21.2	16.5	0.0	0.0
Total expenditure	**44.5**	**51.5**	**39.7**	**39.3**	**37.1**	**35.6**	**34.8**
Current expenditure [3]	26.5	29.0	21.7	22.1	19.1	17.8	17.2
Of which: personnel costs	8.7	8.8	8.2	9.1	8.8	8.6	8.4
interest on external debt due	2.7	3.4	1.6	1.6	1.3	1.2	1.1
goods and services	5.6	6.0	4.2	3.8	3.7	3.3	3.0
transfers	7.0	7.1	4.7	6.0	4.2	3.8	3.7
Of which: JDA	2.8	2.5	2.2	2.1	0.6	0.6	0.5
other	2.4	3.5	3.0	1.7	1.2	1.0	0.9
Capital expenditure	15.7	20.2	15.0	14.2	14.9	14.8	14.7
Financed by the Treasury	1.7	3.3	2.3	1.5	1.9	1.9	1.9
Financed by external sources	13.9	16.9	12.7	12.7	13.0	12.8	12.8
HIPC Initiative-related social expenditure	2.3	2.3	3.0	3.0	3.0	3.0	3.0
Domestic primary balance [4]	**-10.3**	**-8.6**	**-7.0**	**-7.0**	**-4.8**	**-3.8**	**-3.2**
Overall fiscal balance (commitment basis)	**37.5**	**-14.0**	**125.1**	**125.4**	**11.7**	**-5.0**	**-4.8**
Net change in arrears (reduction = -)	-11.3	1.4	0.0	0.0	0.0	0.0	0.0
External arrears [5]	-4.4	1.4	0.0	0.0	0.0	0.0	0.0
Domestic arrears	-6.9	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**26.2**	**-12.6**	**125.1**	**125.4**	**11.7**	**-5.0**	**-4.8**
Financing	**-26.2**	**12.6**	**-125.1**	**-125.4**	**-11.7**	**5.0**	**4.8**
Net external	-3.1	2.0	-120.9	-120.4	2.9	2.7	2.4
Disbursements (projects)	1.1	6.5	1.4	1.3	1.2	1.1	1.0
Program financing (loans)	0.0	1.6	1.0	1.4	1.3	1.2	1.1
Net short-term loans	0.0	0.0	-10.6	-10.4	0.0	0.0	0.0
Scheduled amortization [2]	-7.8	-6.0	-114.0	-114.0	-0.6	-0.5	-0.5
Change in arrears (principal) [6]	-8.6	0.0	-7.2	-7.2	0.0	0.0	0.0
Bilateral rescheduling [7]	12.2	0.0	8.4	8.4	1.0	0.9	0.9
Net domestic	-23.1	10.6	-4.2	-5.0	-14.6	2.3	2.4
Net bank credit to the government	-23.3	10.6	-4.2	-5.0	-14.6	2.3	2.4
Banking system credit (excluding National Oil Account) [8]	-1.2	-1.5	0.3	0.3	0.0	0.0	0.0
National Oil Account	-22.1	12.1	-4.5	-5.3	-14.6	2.3	2.4
Nonbank financing (including earmarked funds and residual)	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:							
Overall balance (commitment basis, incl. grants, excl. oil bonuses)	-9.8	-14.0	104.9	104.3	-4.8	-5.0	-4.8
Domestic primary spending	26.9	28.7	24.9	22.7	20.6	19.7	19.2
MDRI debt relief (flow in US$ million)	0	0	1.1	1.1	1.2	1.2	1.3
National Oil Account (US$ million, excl. transfers to budget)	23.5	8.5	14.2	16.2	13.2	8.2	3.2

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

[1] Based on 2001 census and survey-based GDP series.

[2] For 2007, includes IDA and AfDB MDRI debt relief as a stock of debt reduction.

[3] For 2007, includes the repayment of three $5 million loans disbursed by Nigeria in 2002–04 upon receipt of oil signature bonuses for Blocks 2–4 in the Joint Development Zone.

[4] Excluding oil revenue, grants, interest earned, scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays.

[5] For 2006, refers to a temporary accumulation of technical arrears with bilateral creditors, pending reconciliation of debt records.

[6] For 2005, reflects impact of Paris Club rescheduling in the last quarter of 2005.

[7] For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.

[8] Net of valuation changes. For 2007, includes IMF MDRI debt relief as a stock of debt reduction.

Table 3. São Tomé and Príncipe: Summary Accounts of the Central Bank, 2006–08

	2006	2007					2008			
	Dec.	Jun.		Sep.		Dec.	Mar.	Jun.	Sep.	Dec.
	Actual	Prog	Actual	Prog.	Actual	Prog.	Projections			
	(Billions of dobras, end of period)									
Net foreign assets	**619.5**	**650.9**	**731.5**	**699.3**	**809.2**	**708.6**	**660.9**	**652.9**	**1,004.0**	**1,011.0**
Net international reserves	528.7	593.5	624.7	640.9	708.8	656.4	658.6	660.3	1,011.5	1,018.5
Gross reserves [1, 2]	557.2	622.9	678.8	670.9	746.2	688.0	690.7	693.0	1,044.8	1,052.5
Of which: National Oil Account (NOA)	111.1	189.8	192.6	220.2	230.9	232.4	237.0	196.8	596.0	606.8
Of which: guarantee deposits	15.5	0.0	16.0	0.0	23.8	0.0	0.0	0.0	0.0	0.0
Short-term liabilities [1]	-28.5	-29.4	-54.1	-29.9	-37.4	-31.6	-32.2	-32.8	-33.3	-33.9
Other foreign assets	143.3	96.3	148.6	98.0	153.2	103.5	54.5	55.5	56.4	57.4
Other liabilities [3]	-52.4	-39.0	-41.9	-39.7	-52.7	-51.2	-52.2	-62.8	-63.9	-65.0
Net domestic assets	**-341.5**	**-348.1**	**-413.3**	**-373.9**	**-402.9**	**-371.7**	**-310.5**	**-303.3**	**-631.8**	**-615.3**
Net domestic credit	-121.3	-143.6	-177.8	-192.1	-157.6	-198.7	-133.0	-37.4	-523.9	-581.7
Net credit to government	-108.3	-150.2	-189.7	-200.7	-169.2	-208.3	-141.6	-45.4	-529.9	-586.3
Claims [3]	105.6	92.5	96.0	93.5	122.6	105.7	106.9	117.8	119.1	120.4
Of which : use of SDRs/PRGF Facility	64.5	51.4	54.4	52.4	65.8	64.6	65.8	76.7	78.0	79.3
Deposits [2]	-213.9	-242.7	-285.7	-294.2	-291.8	-314.0	-248.5	-163.2	-649.0	-706.8
Ordinary	-33.9	-40.0	-42.1	-18.7	-23.9	-21.5	-14.8	-14.8	-14.8	-67.8
Of which : HIPC Initiative resources	-12.2	-18.2	-20.3	-15.0	-1.0	-6.7	0.0	0.0	0.0	0.0
Counterpart funds	-22.6	-22.6	-22.6	-22.6	-8.2	-22.6	-22.6	-22.6	-22.6	-22.6
Foreign currency [2]	-157.4	-180.1	-220.9	-252.8	-259.8	-269.9	-211.1	-125.8	-611.6	-616.4
Of which: NOA [2]	-111.1	-189.8	-192.6	-220.2	-230.9	-232.4	-237.0	-196.8	-596.0	-606.8
Rediscount to commercial banks	2.5	1.4	2.4	1.8	2.3	2.0	1.8	1.7	1.2	1.0
Other claims	9.5	5.2	9.6	6.8	9.4	7.6	6.8	6.3	4.7	3.7
Central Bank certificates of deposit	-25.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other items (net)	-220.2	-204.5	-235.5	-181.7	-245.3	-173.0	-177.5	-265.9	-107.9	-33.6
Base money	**278.0**	**302.8**	**318.2**	**325.4**	**406.3**	**337.0**	**350.3**	**349.6**	**372.2**	**395.7**
Currency issued	102.7	105.6	88.7	112.5	96.8	124.5	135.2	122.0	128.7	146.2
Bank reserves	175.3	197.1	229.5	212.9	309.5	212.5	215.2	227.6	243.5	249.5
Of which : domestic currency	64.9	68.7	102.8	95.9	140.6	78.6	80.1	79.4	109.7	92.3
foreign currency	110.4	128.4	126.7	117.0	168.9	133.9	135.1	148.2	133.8	157.2
Memorandum items:										
Gross international reserves (US$ millions) [1, 2]	43.0	46.6	50.8	49.3	54.8	47.9	47.2	46.5	68.9	68.3
Excluding NOA and guarantee deposits	33.3	32.4	35.2	33.1	36.1	31.7	31.0	33.3	29.6	28.9
Net international reserves (US$ millions) [2]	40.8	44.4	46.7	47.1	52.1	45.7	45.0	44.3	66.7	66.1
National Oil Account (US$ millions) [2]	8.6	14.2	14.4	16.2	17.0	16.2	16.2	13.2	39.3	39.4
Net international reserves (US$ millions; excl. NOA)	32.3	30.2	32.3	30.9	35.1	29.5	28.8	31.1	27.4	26.7
Commercial banks reserves in foreign currency	8.5	9.6	9.5	8.6	12.4	9.3	9.2	10.0	8.8	10.2
Net international reserves (US$ millions)										
Excluding NOA and banks reserves in foreign curre	23.7	20.6	22.9	22.3	22.7	20.2	19.6	21.2	18.6	16.5
Base money (annual percent change)	32.0	16.8	22.8	19.1	48.7	21.2	13.1	9.9	-8.4	17.4
Currency Issued (annual percent change)	26.6	16.8	-1.9	19.1	2.5	21.2	68.5	37.5	33.0	17.4

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

[1] Includes guarantee deposits by prospective financial institutions waiting for operating licenses.

[2] Oil signature bonuses for Blocks 5 and 6 in JDZ, totalling US$26.1 million, originally assumed for 2007, are now projected for 2008.

[3] Includes prospective disbursements under PRGF arrangement and MDRI assistance from the IMF as debt reduction totalling SDR1.6 million, assumed in the first quarter of 2007.

Table 4. São Tomé and Príncipe: Monetary Survey, 2006–08

	2006	2007				2008			
	Dec.	Jun.		Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
	Actual	Prog.	Actual	Prog.		Projections			
	(Billions of dobras; end of period)								
Net foreign assets [1]	**860.0**	**899.3**	**941.8**	**952.3**	**975.8**	**932.7**	**929.8**	**1,285.8**	**1,297.6**
Central bank [1]	619.5	650.9	731.5	699.3	708.6	660.9	652.9	1,004.0	1,011.0
Commercial banks	240.4	248.4	210.2	253.0	267.1	271.8	276.8	281.8	286.7
Net domestic assets [1]	**-257.5**	**-247.9**	**-239.3**	**-240.6**	**-221.4**	**-129.4**	**-155.0**	**-447.3**	**-385.2**
Net domestic credit [1]	238.2	222.1	227.1	204.7	214.0	311.6	374.9	-73.3	-84.2
Net credit to government [1]	-115.3	-154.0	-197.7	-205.7	-213.3	-146.6	-50.1	-533.4	-589.8
Of which: valuation changes	-22.4	-5.4	-6.0	-10.2	-21.9	-4.4	-7.2	-23.4	-30.9
Claims	105.6	92.5	96.0	93.5	105.7	106.9	117.8	119.1	120.4
Deposits	-220.9	-246.6	-293.6	-299.1	-319.0	-253.5	-167.8	-652.5	-710.2
Budgetary deposits	-40.9	-43.8	-50.1	-23.7	-26.5	-19.8	-19.4	-18.2	-71.2
Counterpart funds	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6
Foreign currency deposits	-157.4	-180.1	-220.9	-252.8	-269.9	-211.1	-125.8	-611.6	-616.4
Of which: National Oil Account	-111.1	-189.8	-192.6	-220.2	-232.4	-237.0	-196.8	-596.0	-606.8
Credit to the economy [2]	353.5	376.1	424.8	410.3	427.3	458.2	425.0	460.1	505.6
Of which: credit in foreign currency	260.2	255.4	310.1	278.6	290.1	313.3	290.6	314.6	345.7
Other items (net) [2]	-495.7	-469.9	-466.4	-445.2	-435.4	-441.0	-530.0	-374.0	-301.0
Broad money (M3)	**602.5**	**651.4**	**702.5**	**711.8**	**754.4**	**803.3**	**774.7**	**838.5**	**912.4**
Local currency	253.3	280.6	256.9	306.6	325.0	345.4	333.1	360.5	392.3
Money	225.5	253.6	226.8	277.1	293.7	311.7	300.6	325.4	354.1
Currency outside banks	92.3	94.6	78.4	103.4	109.6	117.2	113.0	122.4	133.1
Demand deposits	133.2	159.0	148.4	173.7	184.1	194.5	187.6	203.0	220.9
Time deposits	27.8	27.1	30.1	29.6	31.3	33.7	32.5	35.2	38.3
Foreign currency deposits	349.2	370.8	445.5	405.1	429.4	457.9	441.6	478.0	520.1
	(Change in percent of beginning-of-period money stock, unless otherwise specified)								
Net foreign assets	8.1	6.5	27.0	15.3	19.2	-5.7	-6.1	41.1	42.7
Net domestic assets	31.2	1.6	35.4	2.8	6.0	12.2	8.8	-29.9	-21.7
Of which: net credit to government	32.2	-6.4	13.1	-15.0	-16.3	8.8	21.6	-42.4	-49.9
credit to the economy	26.4	3.7	42.8	9.4	12.2	4.1	-0.3	4.3	10.4
Broad money (M3)	39.3	8.1	62.4	18.1	25.2	6.5	2.7	11.2	21.0
Memorandum items:									
Velocity (ratio of GDP to average broad mone	3.0	...	...	...	3.0	...	...	...	3.0
Money multiplier (M3/M0)	2.2	2.2	2.2	2.2	2.2	2.3	2.2	2.3	2.3
Base money (12-month growth rate)	32.0	16.8	22.8	19.1	21.2	24.2	15.5	14.4	17.4
Credit to the economy (12-month growth rate)	47.6	28.8	45.5	31.6	20.9	21.2	13.0	12.1	18.3
M3 (12-month growth rate)	39.3	9.3	17.8	20.8	25.2	23.1	18.9	17.8	21.0

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

[1] Includes MDRI assistance from the Fund as debt reduction totalling SDR1.6 million, assumed for 2007.

[2] The changes in net credit to the economy and other items net after mid-2008 reflects increased government deposits in the financial system due to oil signature bonuses expected in the second half of 2008.

[3] Based on 2001 census and survey-based GDP series.

Table 5. São Tomé and Príncipe: Balance of Payments, 2005–10

	2005	2006	2007	2008	2009	2010
		Est.	Projections			
			(Millions of U.S. dollars)			
Trade balance	**-34.8**	**-61.3**	**-57.5**	**-67.3**	**-70.1**	**-76.8**
Exports, f.o.b.	6.8	7.7	8.7	9.3	9.7	10.0
Of which : cocoa	3.0	2.5	3.0	2.9	2.9	2.8
re-export	3.4	3.9	4.2	4.5	4.7	4.9
Imports, f.o.b.	-41.6	-69.0	-66.1	-76.6	-79.8	-86.7
Of which : food	-14.8	-17.0	-20.0	-20.4	-21.7	-23.7
petroleum products	-9.8	-15.0	-15.2	-18.1	-18.4	-19.1
Services and income (net)	-16.5	-30.0	-27.3	-28.0	-24.9	-26.9
Exports of nonfactor services	9.2	9.5	6.7	10.8	11.8	12.8
Of which : travel and tourism [1]	7.3	6.7	4.8	8.8	9.6	10.6
Imports of nonfactor services	-23.7	-37.5	-34.9	-38.5	-37.6	-40.7
Factor services (net)	-2.0	-2.0	0.9	-0.3	0.9	0.9
Interest due	-3.2	-3.8	-2.1	-2.1	-2.0	-2.0
National Oil Account (NOA) interest earnings	0.2	0.9	2.0	0.7	2.0	1.9
Private transfers (net)	1.5	1.6	1.7	1.9	2.1	2.4
Official transfers (net)	34.4	33.5	31.4	35.6	35.1	36.1
Of which : project grants	26.5	27.9	28.4	29.8	31.4	33.3
HIPC Initiative-related grants	3.2	3.8	0.0	0.0	0.0	0.0
Current account balance						
Including official transfers	-15.4	-56.2	-51.7	-57.9	-57.8	-65.3
Excluding official transfers	-49.9	-89.7	-83.2	-93.5	-92.9	-101.4
Capital and financial account balance	**46.3**	**41.3**	**55.1**	**76.7**	**59.9**	**63.5**
Capital transfer [2]	0.0	0.0	162.7	0.0	0.0	0.0
Financial account	46.3	41.3	-107.6	76.7	59.9	63.5
Public sector (net)	29.7	-7.3	-147.2	27.5	2.0	2.0
Project loans	1.3	4.4	1.9	1.9	1.9	1.9
Program loans	0.0	0.0	1.5	2.0	2.0	2.0
Oil signature bonuses	49.2	0.0	28.6	26.1	0.0	0.0
Amortization	-8.9	-7.4	-176.4	-0.9	-0.9	-0.9
Other investment	-11.9	-4.3	-2.9	-1.6	-1.0	-1.0
Of which : Nigerian and Angolan advances (net)	0.0	2.0	0.0	0.0	0.0	0.0
transfers to JDA	-11.4	-3.1	-3.1	-1.0	-1.0	-1.0
Private sector (net)	16.5	48.7	39.6	49.2	57.9	61.5
Direct foreign investment [3]	6.2	29.8	21.0	32.5	36.0	40.0
Commercial banks	-8.5	0.8	0.0	0.0	0.0	0.0
Short-term private capital	18.8	18.1	18.7	16.7	21.9	21.5
Errors and omissions	**1.5**	**3.9**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**32.4**	**-10.9**	**3.3**	**18.8**	**2.0**	**-1.7**
Financing	-32.4	10.9	-3.3	-18.8	-2.0	1.7
Change in official reserves, excl. NOA (increase= -)	-8.6	-6.6	2.7	2.8	-5.7	-2.5
Use of Fund resources (net)	0.5	1.2	-0.2	0.6	0.0	0.0
Purchases	0.6	1.2	1.9	0.6	0.0	0.0
Repurchases (incl. MDRI repayment)	-0.1	0.0	-2.1	0.0	0.0	0.0
National Oil Account (increase = -)	-23.3	14.7	-7.6	-23.8	2.0	2.6
Change in arrears (net; decrease = -) [4]	-14.6	1.7	-10.2	0.0	0.0	0.0
Debt relief [1]	13.5	0.0	11.9	1.6	1.6	1.6
Memorandum items:			(Unit specified)			
Current account balance (percent of GDP) [5]						
Before official transfers	-43.9	-72.9	-57.5	-59.1	-53.6	-53.4
After official transfers	-13.6	-45.7	-35.8	-36.6	-33.4	-34.4
Debt service ratio (percent of exports) [6]						
Before HIPC and MDRI relief	75.6	65.8	59.7	48.9	48.5	47.4
After HIPC and MDRI relief	62.1	33.8	7.5	6.7	6.2	5.8
Gross reserves [7]						
Millions of U.S. dollars	26.6	33.3	31.7	28.9	34.6	37.1
Months of imports of goods and nonfactor services	4	4	4	4	4	4

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

[1] Following the closure of the national airline, tourism receipts fell in 2006 and 2007. The airline was privatized in 2007.
[2] Include HIPC and MDRI debt relief delivered at the completion point in 2007.
[3] From 2006, FDI increases due to oil drilling by foreign companies as well as FDI in the hotel sector.
[4] For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.
[5] Based on 2001 census and survey-based GDP series.
[6] Percent of exports of goods and nonfactor services. The difference between debt service before and after HIPC relief is larger than debt service saving in cash terms because this table is on an accrual basis.
[7] Gross reserves exclude the National Oil Account and guarantee deposits placed at the central bank by financial institutions pending operating licenses; imports exclude oil sector-related imports of capital goods and services.

Table 6. São Tomé and Príncipe: External Financing Requirements and Sources, 2005–08

(Millions of U.S. dollars)

	2005	2006 Est.	2007 Prog.	2008 Proj.
Gross financing requirements	**-94.0**	**-106.4**	**-271.9**	**-93.2**
Current account, excluding official transfers	-49.9	-89.7	-83.2	-93.5
Exports, f.o.b.	6.8	7.7	8.7	9.3
Imports, f.o.b.	-41.6	-69.0	-66.1	-76.6
Services and income (net)	-16.5	-30.0	-27.3	-28.0
Private transfers	1.5	1.6	1.7	1.9
Financial account	-20.9	-11.8	-181.3	-2.5
Scheduled amortization [1]	-8.9	-7.4	-176.4	-0.9
IMF repayments [2]	-0.1	0.0	-2.1	0.0
Other public sector investment (net)	-11.9	-4.3	-2.9	-1.6
Change in external reserves (increase = -)	-8.6	-6.6	2.7	2.8
Change in arrears (net)	-14.6	1.7	-10.2	0.0
Available funding	**94.0**	**106.4**	**271.9**	**93.2**
National Oil Fund (net)	25.9	14.7	21.0	2.3
Oil signature bonuses	49.2	0.0	28.6	26.1
Saving (accumulation of oil reserve fund = -)	-23.3	14.7	-7.6	-23.8
Expected disbursements	35.7	37.9	197.5	39.5
Multilateral HIPC interim assistance	3.2	3.8	0.0	0.0
Capital transfers [1, 2]	0.0	0.0	162.7	0.0
Grants [3]	31.3	29.7	31.4	35.6
Concessional loans	1.3	4.4	3.4	3.9
Project loans	1.3	4.4	1.9	1.9
Program loans	0.0	0.0	1.5	2.0
Private sector (net)	18.0	52.6	39.6	49.2
IMF [4]	0.6	1.2	1.9	0.6
Financing gap	13.7	0.0	11.9	1.6
HIPC debt relief (bilateral creditors) [2]	0.2	0.0	1.7	1.6
Reschedualable arrears (bilateral creditors) [5]	13.5	0.0	10.2	0.0
Residual financing gap	0.0	0.0	0.0	0.0

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

[1] Includes HIPC and MDRI debt relief delivered at the completion point in 2007.

[2] Includes MDRI assistance from the IMF as a stock of debt reduction.

[3] Includes aid in kind received from Nigeria.

[4] Includes projected PRGF disbursements.

[5] In 2005, includes the new Paris Club rescheduling agreement. For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors of current maturities and stock of arrears.

Table 7. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2007 and 2008
(Billions of dobras, unless otherwise specified)

	2006		2007					2008	
	Sep. 30		Jun. 30	Jun. 30	Jun 30	Sep. 30	Dec. 31	March 31	Jun. 30
	Base	Base	Perf. Criteria	Perf. Criteria	Actual	Ind.Target	Perf. Criteria	Ind.Target	Ind.Target
	(stocks)	(stocks, excl. NOA)	Country Report No. 07/267	Country Report 07/102 (with adjustors)		Country Report No. 07/267	Country Report No. 07/267		
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	...	...	-97.0	-97.0	-97.0	-116.3	-137.3	-22.6	-80.1
2. Ceiling on changes in net bank financing of the government (cumulative from end–September 2006; billions of dobras at program exchange rate) [1,2,3,4]	-126.8	-20.8	-32.4	162.3	-60.7	-73.9	-33.8	103.2	151.9
3. Ceiling on changes in net domestic assets of the central bank (cumulative from end–September 2006; billions of dobras at program exchange rate) [1,2,3,4]	-289.8	-183.8	-19.6	175.1	-86.5	-7.8	26.3	156.4	133.3
4. Floor on changes in the net international reserves of the central bank (cumulative from end–September 2006; US$ millions) [4,5,6]	41.8	33.4	1.9	-14.1	4.9	2.5	1.0	-4.9	-2.8
5. Ceiling on central government's outstanding external payment arrears (stock, US$ millions) [7]	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0
6. Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (cumulative flows from January 2005, € millions) [8,9]	...	...	1.6	1.6	0.0	1.6	1.6	1.6	1.6
7. Ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP (stock, US$ millions) [10]	...	...	1.0	1.0	0.0	1.0	1.0	1.0	1.0
Memorandum items:									
Base money (ceiling; billions of dobras)	273.2	...	302.5	...	318.2	406.3	337.0	350.3	349.6
Currency Issued (ceiling; billions of dobras)	94.4	...	105.0	...	88.7	96.8	124.5	135.2	122.0
Oil signature bonuses including accrued interest on NOA (US$ millions, cumulative from beginning of year)	0.5	...	28.8	...	16.0	28.9	29.0	0.0	0.0
Transfer from NOA to the budget (US$ millions, cumulative from beginning of year)	...	...	8.0	...	8.0	8.0	8.0	0.0	3.0
Net external debt service payments (cumulative from beginning of the year, billions of dobras at program exchange rate) [11]	-35.4	...	-211.0	...	-213.2	-216.6	-220.0	-3.1	-6.3
Official external program support (cumulative from beginning of the year, billions of dobras at program exchange rate) [12]	7.8	...	0.0	...	0.0	31.4	41.8	0.0	50.0

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

[1] For 2007, the ceiling will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service; and by deviations in the opposite direction in external program support and oil bonuses, including accrued interest on the National Oil Account (NOA). The downward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[2] For 2008, the ceiling will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service; and by deviations in the opposite direction in external program support and transfers from NOA to the budget exceeding US$3 million. The downward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[3] The ceiling will be adjusted downward by the amount of accumulated domestic arrears. For end-June 2007, ceilings were adjusted for domestic areas totaling Dobras 6.5 billion.

[4] The National Oil Account (NOA) at the Central Bank is included in 2007 and excluded in 2008.

[5] For 2007, the floor on net international reserves will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service (including repayments to Nigeria), and by deviations in the same direction for oil bonuses, including accrued interest on NOA. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[6] For 2008, the floor on net international reserves will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service (including repayments to Nigeria), and by deviations in the same direction for transfers from NOA to the budget exceeding US$3 million. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[7] This is a continuous performance criterion.

[8] This performance criterion applies not only to debt as defined in point No. 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24, 2000), but also to commitments contracted or guaranteed for which value has not been received.

[9] With a grant element of less than 50 percent.

[10] Debt is defined as in point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24), 2000. Excludes US$15 million in loans from Nigeria during 2002–04, which are to be repaid from signature bonuses in 2007.

[11] Includes US$15 million repayment to Nigeria in 2007.

[12] Official external program support, as defined in the TMU, valued at the program exchange rate of 12,549 dobras per U.S. dollar (valued at projected average exchange rate of 13,935 dobras per U.S. dollar in fiscal table).

Table 8. São Tomé and Príncipe: Millennium Development Goals

	1990	1994	1997	2000	2003	2004
Goal 1. Eradicate extreme poverty and hunger						
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day.						
1. Population below US$1 a day (percent)	..	..	..	..	..	..
2. Poverty gap ratio at US$1 a day (percent)	..	..	..	..	..	..
3. Share of income or consumption held by poorest 20 percent (percent)	..	..	..	..	..	..
Target 2: Halve, between 1990 and 2015, the proportion of people suffering hunger.						
4. Prevalence of child malnutrition (percent of children under 5)	..	..	..	12.9	..	..
5. Population below minimum level of dietary energy consumption (percent)	..	..	..	..	..	..
Goal 2. Achieve universal primary education						
Target 3: Ensure that, by 2015, children will be able to complete a full course of primary schooling.						
6. Net primary enrolment ratio (percent of relevant age group)	..	..	85.5	97.1	..	..
7. Percentage of cohort reaching grade 5	..	..	..	61.5	..	..
8. Youth literacy rate (percent age 15–24)	..	..	..	..	..	..
Goal 3. Promote gender equality and empower women						
Target 4: Eliminate gender disparity in primary and secondary education, preferably by 2005, and to all levels of education by 2015.						
9. Ratio of girls to boys in primary and secondary education (percent)	..	..	..	92.1	..	..
10. Ratio of young literate females to males (percent ages 15–24)	..	..	..	..	..	..
11. Share of women employed in the nonagricultural sector (percent)	..	..	..	..	..	..
12. Proportion of seats held by women in the national parliament (percent)	12.0	..	7.0	9.0	9.0	9.0
Goal 4. Reduce child mortality						
Target 5: Reduce by two-thirds, between 1990 and 2015, the under-5 mortality rate.						
13. Under-5 mortality rate (per 1,000)	118.0	118.0	..	118.0	118.0	118.0
14. Infant mortality rate (per 1,000 live births)	75.0	75.0	..	75.0	75.0	75.0
15. Immunization against measles (percent of children under 12 months)	71.0	65.0	60.0	69.0	87.0	87.0
Goal 5. Improve maternal health						
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.						
16. Maternal mortality ratio (modelled estimate, per 100,000 live births)	..	..	..	..	..	..
17. Proportion of births attended by skilled health personnel	..	..	..	58.5	..	79.8
Goal 6. Combat HIV/AIDS, malaria, and other diseases						
Target 7: Halt by 2015, and begin to reverse, the spread of HIV/AIDS.						
18. HIV prevalence among females (percent ages 15–24)	..	..	..	..	..	1.3
19. Contraceptive prevalence rate (percent of women ages 15–49)	..	..	..	29.0	..	..
20. Number of children orphaned by HIV/AIDS	..	..	..	..	..	..
Target 8: Halt by 2015, and begin to reverse, the incidence of malaria and other major diseases.						
21. Prevalence of death associated with malaria	..	..	..	..	..	..
22. Share of population in malaria risk areas using effective prevention and treatment	..	..	..	80.0	..	..
23. Incidence of tuberculosis (per 100,000 people)	136.1	126.6	120.0	113.7	107.8	107.8
24. Tuberculosis cases detected under DOTS (percent)	..	..	..	..	..	..

Continued

Table 8. São Tomé and Príncipe: Millennium Development Goals (concluded)

	1990	1994	1997	2000	2003	2004
Goal 7. Ensure environmental sustainability						
Target 9: Integrate the principles of sustainable development into policies and programs. Reverse the loss of environmental resources.						
25. Forest area (percent of total land area)	28.1	..	..	28.1	..	..
26. Nationally protected areas (percent of total land area)	..	..	..	..	..	..
27. GDP per unit of energy use (PPP $ per kg oil equivalent)	..	..	..	..	..	..
28. CO2 emissions (metric tons per capita)	0.6	0.6	0.6	0.6	..	..
29. Proportion of population using solid fuels	..	..	..	..	..	..
Target 10: Halve, by 2015, the proportion of people without access to safe drinking water.						
30. Access to improved water source (percent of population)	..	..	..	..	79.0	..
Target 11: Achieve by 2020 significant improvement for at least 100 million slum dwellers.[1]						
31. Access to improved sanitation (percent of population)	..	..	..	..	24.0	..
32. Access to secure tenure (percent of population)	..	..	..	..	..	..
Goal 8. Develop a Global Partnership for Development						
Target 16: Develop and implement strategies for productive work for youth.						
45. Unemployment rate of population ages 15–24 (total)						
Female	..	..	..	..	..	..
Male	..	..	..	..	..	..
Target 17: Provide access to affordable essential drugs						
46. Proportion of population with access to affordable essential drugs.	..	..	..	..	..	..
Target 18: Make available new technologies, especially information and communications.						
47. Fixed line and mobile telephones (per 1,000 people)	19.2	19.8	31.2	31.0	77.6	77.6
48. Personal computers (per 1,000 people)	..	..	..	..	..	..

Sources: World Development Indicators database.

[1] Targets 33–44 are excluded because they cannot be measured on a country-specific basis. They are related to official development assistance, market access, and the HIPC Initiative.

Table 9. São Tomé and Príncipe: Schedule of Disbursements Under the PRGF Arrangement, 2005–08

SDR Millions	Percent of Quota	Date Available	Disbursement Conditions
0.423	5.7	Aug. 2005	Board approval of arrangement
0.423	5.7	Mar. 2006	Observance of PCs for end-September 2005 and completion of the first review
0.423	5.7	Aug. 2006	Observance of PCs for end-December 2005 and completion of the second review
0.423	5.7	Jan. 2007	Observance of PCs for end-June 2006 and completion of the third review
0.423	5.7	Jun. 2007	Observance of PCs for end-December 2006 and completion of the fourth review
0.423	5.7	Dec. 2007	Observance of PCs for end-June 2007 and completion of the fifth review
0.422	5.7	Jun. 2008	Observance of PCs for end-December 2007 and completion of the sixth review

Source: IMF.

Table 10. São Tomé and Príncipe: Indicators of Fund Credit, 2007–10

(Millions of SDRs, unless otherwise indicated)

	2007	2008	2009	2010
	Projections			
Fund credit outstanding [1]				
Millions of SDRs	2.91	3.34	3.25	2.96
Millions of U.S. dollars	4.32	4.98	4.85	4.42
Percent of quota	39.32	45.14	43.92	40.00
IMF obligations				
Total charges and interest	0.06	0.08	0.08	0.07
Existing drawings	0.03	0.04	0.04	0.03
Prospective drawings	0.03	0.04	0.04	0.04
Total repayment/repurchases	0.00	0.00	0.09	0.29
Existing drawings	0.00	0.00	0.09	0.29
Prospective drawings	0.00	0.00	0.00	0.00
Fund credit as a percent of				
Export of goods and nonfactor services	28.22	24.79	22.58	19.35
Gross official reserves	13.62	17.23	14.01	11.91
Memorandum items:				
Export of goods and nonfactor services (US$ millions)	15.3	20.1	21.5	22.8
Gross official reserves (US$ millions)	31.7	28.9	34.6	37.1

Sources: IMF staff estimates and projections.

[1] Includes prospective PRGF disbursements, totalling SDR1.268 million.

APPENDIX I—LETTER OF INTENT

São Tomé, December 1, 2007

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

Dear Mr. Strauss-Kahn:

1. The attached Memorandum of Economic and Financial Policies (MEFP) sets out the objectives and policies that the government of São Tomé and Príncipe intends to pursue for the remainder of 2007 and in 2008. They are consistent with the government's Poverty Reduction Strategy (PRS) and the objectives of the three-year arrangement under the IMF's Poverty Reduction and Growth Facility (PRGF). Our economic adjustment and reform efforts are being supported by the international community, notably through debt relief under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI).

2. The government of São Tomé and Príncipe has made further progress in macroeconomic stabilization and structural reforms in 2007. Economic growth has remained robust. Inflation fell below 15 percent by mid-2007, reflecting our efforts to reduce domestic fiscal imbalances in the 2007 budget and to bring down liquidity growth. As a result, all quantitative performance criteria for end-June 2007 under the PRGF-supported program were met. In September 2007 we raised the domestic prices for petroleum products, electricity, and water, following increases in international oil prices. We have also moved to strengthen public financial management.

3. Looking ahead, we intend to strengthen policy implementation, particularly in fiscal and structural areas, to achieve the objectives of the 2007 program. Our policies for 2008 aim to consolidate financial stability, ensure sound management of oil-related and debt relief resources, and lay the groundwork for sustained private sector-led growth. Our program envisages a further reduction of the domestic primary fiscal deficit relative to GDP, combined with a prudent use of oil bonuses, a strengthening of monetary and exchange rate policies to lower inflation, and an acceleration of structural reforms. These are key conditions for sustained growth, which in turn is key for poverty reduction.

4. In support of our objectives and policies, the government hereby requests the completion of the fifth review and the disbursement of the sixth loan under the PRGF arrangement in an amount equivalent to SDR 0.423 million (5.7 percent of quota). The government requests a waiver for the nonobservance of the end-June 2007 structural

performance criterion on issuing prudential regulations, which was due to technical difficulties we encountered in preparing the regulations. Three out of the four regulations were issued in August 2007. With IMF technical assistance, we have completed the preparatory work and issued the remaining regulation on limits on bank net open foreign currency positions by mid-November 2007.

5. The government will provide the IMF with such information as the IMF may request regarding progress in implementing economic and financial policies and achieving the objectives of the program.

6. The sixth review related to the seventh and final disbursement under the PRGF arrangement, based on end-December 2007 performance criteria, is expected in May 2008.

7. The government believes that the policies and measures set forth in the MEFP are adequate to achieve the objectives of the 2007-08 program supported by the PRGF arrangement, but will take further measures to that end if deemed necessary. During the implementation of the arrangement, the government will consult with the Managing Director of the IMF on the adoption of any measures that may be appropriate, at the initiative of the government or whenever the Managing Director requests such a consultation.

8. The government intends to make the contents of this Letter of Intent and those of the attached MEFP and Technical Memorandum of Understanding (TMU), as well as the IMF staff report on the fifth PRGF review, available to the public and authorizes the IMF to arrange for them to be posted on the IMF website, subsequent to Executive Board completion of the fifth review.

Yours truly,

/s/

Mr. Arlindo Afonso de Carvalho
Minister of Planning and Finance

/s/

Mrs. Edite Diogo Afonso Soares
Acting Governor of the Central Bank of São Tomé and Príncipe

Attachments: Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

APPENDIX I. ATTACHMENT I—MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

October 20, 2007

I. INTRODUCTION

1. This Memorandum of Economic and Financial Policies (MEFP) supplements that of May 2007 and our Letter of Intent dated May 6, 2007. It describes (i) performance under the PRGF arrangement through September 2007, (ii) macroeconomic policies for the remainder of 2007, and (iii) the government's economic program for 2008. The policies set forth in this Memorandum should help achieve the medium-term objectives set out in our PRSP, including efficient use of debt relief resources provided under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI). Our government is committed to creating the conditions for sustained economic growth, which is essential for reducing poverty.

II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

2. **Economic activity has remained robust in 2007, with real GDP growth projected at 6 percent**. Tourism-related construction, commerce, and services sectors continued to be the main drivers of output growth, boosted by foreign direct investment. Exports increased in the first half of the year on the back of rising world market prices for cocoa.

3. **Inflation declined to 14 percent (year-on-year) at the end of June 2007, from its peak of 26 percent in August 2006**. This deceleration reflected our efforts to reduce domestic fiscal imbalances under the 2007 budget and a tight monetary policy to contain liquidity growth. These policies led to a slower depreciation of the dobra, by 3 percent against the U.S. dollar in the first six months of 2007. In early September 2007 the government raised domestic prices of gasoline, diesel, and kerosene by 25, 14, and 23 percent respectively, following increases in international oil prices. At about the same time, to improve cost recovery by EMAE, the state-owned utility company, electricity and water tariffs were increased by 40 to 60 percent.

4. **Despite lower than projected domestic revenue, the domestic primary fiscal deficit met the performance criterion for end-June 2007** (Table I.1). Domestic revenue fell short of the program target for the first half of the year, owing mainly to lower than projected import duties and nontax revenue (e.g., fishing royalties), although income tax collection improved. Implementation of revenue reform measures experienced delays. The corporate income tax code was approved by the National Assembly (NA) in general terms. Its final approval, together with the remainder of the tax reform package (including an urban property tax code) submitted to the NA in January 2007, is pending the resubmission of a revised draft of the personal income tax code. The NA recently rejected the proposed

amendment to the excise duties. Under these circumstances, the government kept budgetary outlays in check by compressing domestically financed capital expenditure and HIPC-related social expenditure. In addition, a general wage increase of 18 percent did not take place as envisaged at the beginning of the year. Instead, demanding negotiations with trade unions eventually led to a 35 percent wage increase for all budgetary entities effective July 2007. As part of the wage increase negotiated with the trade unions, more overtime payments were made to teachers and health workers, further increasing the wage bill.

5. **The Central Bank of São Tomé and Príncipe (BCSTP) strengthened efforts to control liquidity growth**. It has continued to offset the monetary impact of budgetary use of oil bonuses and HIPC and MDRI savings through timely foreign exchange sales. As a result, base money growth (12-month change) declined from over 110 percent in mid-2006 to about 20 percent in the second quarter of 2007. By containing its net credit to the government, the BCSTP maintained net international reserves (NIR) above the program's performance criteria and met all other quantitative performance criteria for end-June 2007.

6. **The exchange rate of the dobra remains market-determined**. The BCSTP has continued to adjust its exchange rate to market conditions daily by calculating it as the sum of 40 percent of the previous day's selling rate quoted by commercial banks and 60 percent of its own previous day's selling rate. The spread between the reference exchange rate of the central bank and commercial bank exchange rates has declined to 0.8 percent in September 2007, compared to 1.6 percent in September 2006, following the resumption of foreign exchange auctions in December 2006.

7. **Progress on structural reforms has been mixed**. The end-June structural performance criterion was not met due to technical difficulties: of the four planned prudential regulations, three were issued with some delays in August 2007. With IMF technical assistance, the remaining regulation, related to limits on bank net open foreign currency positions, is expected to be issued by the end of November 2007 (Table I.2). The Ministry of Planning and Finance has been producing monthly budget execution reports using the pilot budget preparation and execution program (SAFINHO), which complies with the structural benchmark of June 2007. We have also made progress in gaining external support for our fiscal structural reforms. The U.S. Millennium Challenge Corporation (MCC) has approved a threshold program that will provide technical assistance for strengthening revenue administration. Although the legislation on anti-money-laundering and the financing of terrorism is still pending final approval by the NA, the BCSTP has set up the Central Risk Unit and started implementing the "know-your-clients" rules for banks. EMAE has made some progress in installing the prepaid electricity meter systems, reaching about 1,000 meters by September 2007. However, the *Oil Revenue Management Law (ORML) Handbook* is not yet posted on the government's website and the investment code has not yet received NA approval.

III. ECONOMIC POLICIES FOR THE REST OF 2007

8. **The authorities remain committed to achieving the objectives of the 2007 program**. The large upward adjustments of fuel and utility prices toward the end of the third quarter were necessary to eliminate the implicit subsidies arising from differences between international and domestic prices of energy. But the rise of administered prices also made attaining the program's original inflation target difficult. We intend to maintain strong fiscal restraint and a tight monetary policy to counter the pressures from higher energy costs, thereby bringing annual inflation as close as possible to the original program target of 13–15 percent by the end of 2007. To protect the poorest segments of the population, utility tariffs will be modified in October 2007 based on the level of consumption.

9. **To ensure that the domestic primary fiscal deficit is reduced to 7 percent of GDP, the government will step up efforts to mobilize revenue**. We will focus on (i) working closely with the NA to expedite passage of the new direct taxation laws (personal income tax, corporate income tax, and urban property tax), aiming for implementation in 2008; (ii) auditing the tax arrears of large tax payers as of September 2007; (iii) strengthening the collection of tax arrears by applying the tax administration and procedural codes, including by collecting indirect tax arrears from ENCO, the fuel importer, which stood at Db 17 billion at the end of September 2007. The recent adjustments of fuel prices and utility tariffs should facilitate payment of inter-enterprise obligations and tax arrears; and (iv) intensifying efforts to recover nontax revenue, including royalties and transfers from foreign entities.

10. **We are determined to keep domestic primary spending within the tight budget constraints**. Specifically:

- To the extent that the wage bill exceeds the amount indicated in the 2007 budget (Db 161 billion) due to the general wage increase and higher additional remuneration to teachers and health workers (in part to mitigate the adverse impact of the fuel and utility price increases), nonwage nonessential expenditures (excluding debt service payments and foreign-financed scholarships) will be cut so that domestic primary spending will remain within the resource envelope—domestic tax and nontax revenues plus the use of oil bonuses as authorized by the NA in accordance with the ORML.

- Nonwage nonessential spending will be further restrained to offset any revenue losses owing to delays in increasing the excise taxes on services and on imported alcoholic beverages and tobacco.

- The Ministry of Planning and Finance will strictly control expenditure commitments to prevent any buildup of domestic and external payment arrears.

- The use of HIPC and MDRI resources will be closely monitored to ensure that progress is made in implementing propoor programs.

- We will collaborate with donors to speed up implementation of foreign-funded investment projects.

11. **Making further progress in reforming public financial management is critical for implementing fiscal policy**. The government is preparing the 2008 budget in line with the new organic budget law (SAFE) for submission to the NA by the end of October 2007. The manual of public accounting procedures consistent with SAFE will be issued in November 2007. Upgrading SAFINHO is essential for strengthening budget execution and monitoring. With support from the World Bank and the MCC project, the Ministry of Planning and Finance will initiate procurement of IT equipment and issue a decree to establish the IT office by December 2007, with a view to putting them in place by March 2008. Developing the IT system will require further technical assistance.

12. **The BCSTP will continue to mop up excess liquidity through timely sterilization of budgetary use of oil bonuses and HIPC savings, consistent with the program's net international reserves (NIR) target and in close cooperation with fiscal policy**. Because base money serves as the anchor for the program, efforts need to be made to ensure that the 12-month change of base money, mainly the domestic currency component, continues on a declining path, in line with the program's indicative target. Owing to weak financial intermediation and extensive use of foreign currencies in the economy, the effectiveness of monetary policy in affecting aggregate demand is limited. If meeting the program's NIR target is at risk, the government will have to support monetary tightening by curtailing public expenditure, which has a major impact on domestic demand and inflation.

13. **We will make every effort to speed up structural reforms**. Key measures to be implemented by December 2007 include (i) accelerating the process of putting in place the legal and regulatory framework for anti-money-laundering; (ii) adopting a Petroleum Sector Strategy, consistent with the ORML and the Extractive Industries Transparency Initiative (EITI), for developing the Exclusive Exploration Zone (EEZ); (iii) adopting the legal framework for the EEZ, including the Production-Sharing Contract Model, the Framework Law on Oil-related activities, the Taxation Law, and the Environmental and Health and Safety at Work Standards; and (iv) finalizing and submitting to the NA legislation to sharply reduce the cost of investing and doing business in São Tomé and Príncipe.

IV. Economic Policies And Reforms for 2008

14. **Our macroeconomic policies in 2008 aim to consolidate financial stability and lay the basis for sustained private-sector-led growth**. The main objectives are to (i) maintain real GDP growth at 6 percent; (ii) reduce inflation to 9–12 percent; and (iii) safeguard international reserves equivalent to about 4 months of imports. Structural

reforms, notably in the areas of public financial management, public wage reform, and the investment climate, are critically important for addressing our economy's supply constraints, restoring fiscal sustainability over the medium term, and mobilizing support from the World Bank and other multilateral and bilateral development partners.

A. Fiscal Policy

15. **The government aims to further reduce the domestic primary deficit to 4.8 percent of GDP in 2008 (compared with 7 percent in 2007)**. Fiscal consolidation in the 2008 budget would come mainly from the expenditure side, because the revenue impact of the envisaged direct tax reforms, which aim to reduce distortions, would be largely neutral in 2008. The domestic primary deficit is expected to be financed by assistance from the World Bank under its Development Policy Operation (DPO) facility and a draw-down of up to US$3 million from the National Oil Account (NOA). There should be no recourse to domestic banking system credits (excluding the NOA).

16. **Prudent use of the remaining oil bonuses is essential for maintaining macroeconomic stability in the next several years**. This is because the remaining balance in NOA is already low, the prospects for additional oil signature bonuses in 2008 are highly uncertain, and finding commercially viable oil reserves is a long and uncertain process. If oil bonuses for Blocks 5-6 are delayed indefinitely, the use of oil resources may need to be further constrained. Strictly limiting the annual draw-down of the NOA within the requirements of the ORML would help extend the period of fiscal adjustment, avoiding a sharp compression of public expenditure.

17. **The main elements of the fiscal program for 2008 are**:

- **Implementing the new direct taxation laws, pending NA approval**. The package of legislation includes a reduction in the corporate income tax rate from 45 to 25 percent, a move to a progressive income tax from the current flat rate of 13.5 percent, and application of a new urban property tax code. Timely implementation after NA approval would help broaden the tax base, reduce distortions, and increase revenue buoyancy over the medium term.

- **Strengthening tax and customs administration**. The tax authorities will step up efforts to audit tax returns, keep track of large tax payers, and increase arrears collection, particularly from large tax payers. With progress made in recovering indirect taxes from ENCO in the fourth quarter of 2007, efforts will be made to reduce outstanding income tax arrears, which were estimated at Db 104 billion at the end of September 2007.

- **Containing budgetary personnel costs**. The wage bill is expected to increase by 16.9 percent to Db 207.0 billion, resulting in a decline in the wage bill-to-GDP ratio to 8.8 percent (from 9.1 percent projected for 2007). The government will closely monitor all the components and strictly limit the payments of bonuses and benefits. As part of the program to be supported by the World Bank under the DPO, the government plans to integrate fringe benefits into the wage bill and adopt a revised salary structure, based on a comprehensive wage study, with improved incentives for public servants, as a first step in its civil service reform strategy. These reforms are critically important for restoring fiscal sustainability and enhancing the growth orientation of the budget.

- **Adjusting nonwage current spending**. Transfers to the Joint Development Authority (JDA) will need to be reassessed, taking into account budget constraints, oil revenue prospects, and the execution of the JDA budget. Discretionary expenditures on goods, services, and other items will have to be restrained to correspond with available resources. Payments for utilities (electricity and water) will closely follow consumption while we continue to avoid arrears.

- **Increasing propoor spending**. We plan to achieve this goal through systematic application of the execution mechanisms contained in the new Organic Budget Law. While aligning allocations with the PRSP priorities set out in the Priority Actions Plan for 2006–08, we will strictly monitor the use of HIPC and MDRI resources.

- **Improving the execution of public investment projects**. Increasing infrastructure investment, especially in transportation and the electricity sector, will help address supply bottlenecks and enhance growth potential. We will work closely with our external development partners to accelerate implementation of foreign-funded projects, while ensuring adequate resources for domestically funded investment projects.

18. **The government will strengthen the monitoring and execution of the 2008 budget, including the use of debt relief resources, by further upgrading SAFINHO and training users**. With assistance from multilateral and bilateral donors, efforts will be made to develop SAFINHO into a fully fledged eSAFE system incorporating all public accounts, including patrimony and debt.

19. **The proposed 2008 program is fully financed**. The fiscal plan assumes budget support from the World Bank under the DPO and project financing and technical assistance from the EU, Portugal, Taiwan Province of China, the MCC of the U.S.A., and other donors. We will redouble our efforts to mobilize and absorb aid inflows for development. The government is committed to adjusting the medium-term fiscal and financing strategies, including the use of NOA resources if oil production and exports are seriously delayed beyond the previous projection of 2014.

B. Monetary and Exchange Rate Policies

20. **The monetary program for 2008 aims to reduce annual inflation to 9–12 percent by the end of 2008**. Although base money is an indicative target, it serves as the anchor for the program, playing a central role in restoring price stability. We will therefore make every effort to ensure that the 12-month base money growth continues a declining trend, to 17 percent by the end of 2008. To achieve this, the BCSTP will proactively use monetary instruments, primarily foreign exchange sales, consistent with the NIR target, to mop up liquidity.

21. **We recognize that close cooperation between the Treasury and the BCSTP is essential for improving the latter's liquidity forecast and ensuring timely action to offset the monetary impact of budgetary use of oil bonuses and HIPC and MDRI savings**. Regular information-sharing among the Ministry of Finance and BCSTP officials will include the budget's cash outlays (in both domestic and foreign currency), which will help inform the BCSTP's foreign exchange market operations. Because public expenditure is a major component of aggregate demand and affects domestic prices and the exchange rate, if meeting the program's NIR target is at risk, the government will support monetary tightening by curtailing domestic primary expenditures.

22. **The BCSTP is committed to deepening foreign exchange market reform and, on this basis, accepting the obligations under Article VIII, Sections 2(a), 3, and 4, of the IMF's Articles of Agreement**. The exchange restriction on transfers abroad of dividends will be eliminated when the new investment code is enacted by the National Assembly. To remove the remaining multiple currency practices, the BCSTP will consider revising the mechanism for setting the daily official exchange rate, based on a careful review of domestic market conditions. The revised mechanism would ensure that the spread between the official and commercial bank exchange rates will not exceed 2 percent. The BCSTP will continue implementing the current policies of holding regular foreign exchange auctions and progressively expanding the auction market to ensure a fuller and faster market determination of the exchange rate. Reforming the foreign exchange market will require promotion of a dynamic export sector to increase foreign exchange earnings of the country and a larger participation of commercial banks in the market to meet demand for foreign exchange, including for fuel imports, thereby reducing supply-demand imbalances in the market.

23. **The BCSTP will continue with its communication strategy of informing the market on its monetary and exchange policies.** In addition to the BCSTP Governor's regular meetings with the banking community and the media, summary data on monetary and macroeconomic aggregates will continue to be posted weekly on the central bank website. The BCSTP will also post yearly audited financial statements. Its budget execution and profit and loss accounts on a cash basis will be reported at least quarterly, as part of the program's monetary data.

C. Structural Reforms in 2008

24. **We intend to make concrete progress in improving the investment climate**. Early adoption of the draft legislation to reduce red tape and other regulatory impediments to start a business, drafted in consultation with the private sector, would help sharply lower the cost of investing and doing business in São Tomé and Príncipe and attract private investment. Progress in improving the "doing business indicators" of the International Financial Corporation, particularly "cost of starting a business" and "days to start a business." would facilitate our efforts to mobilize donor financing for investment projects. We will press ahead with the legislative process, aiming for NA approval of the legislation by mid-2008.

25. **Implementing the new investment code and the revised labor code, after NA approval, is important for long-term growth**. The investment code would provide equal treatment to foreign and domestic investors. Revision of the labor code would aim to more clearly define hiring and firing rules, remove ambiguities in contractual employment arrangements, and increase labor market flexibility by eliminating regulatory impediments.

26. **We will further develop the institutional framework for transparent management of current and prospective oil resources**. With World Bank support, the Oversight Committee for auditing and supervising petroleum receipts and expenditures is now operational. The Minister of Natural Resources and Environment issued an order in August 2007 verifying São Tomé and Príncipe's formal adherence to the Extractive Industries Transparency Initiative (EITI). A national coordinator for implementation of the EITI has also been appointed. The National Oil Agency will strive to conduct the licensing round for the Exclusive Zone transparently, consistent with the ORML and the EITI.

27. **Regarding financial sector reform, the BCSTP intends to make progress in the following areas**: (i) implementing the new charts of accounts and quarterly financial reporting by banks, which are essential for effective off-site inspection; to this effect, the BCSTP has requested technical assistance from the Fund; (ii) improving on-site and off-site inspection; the BCSTP will issue new regulations on capital adequacy, internal control and auditing, bank financial reporting, and credit to employees by December 2007; and (iii) putting in place a functioning regulatory regime for anti-money-laundering. Once the NA gives final approval to the AML/CFT law, the implementation regulations, which the BCSTP has already prepared, will be issued.

28. **Pressing ahead with reforms in key sectors, such as agriculture, transportation, and energy, is of fundamental importance if living standards are to improve on a sustainable basis**. We intend to work closely with the World Bank and other development partners to promote agricultural marketing, commercial fishing, and tourism-related services. We will also address EMAE's financial and technical weaknesses through tariff and other reforms and attract investment to upgrade our infrastructure, including the airport runway.

D. Debt Management

29. **The government is fully aware of the importance of ensuring debt sustainability after HIPC and MDRI debt relief**. We will refrain from new external borrowing, particularly on commercial terms, and redouble our efforts to seek full delivery of HIPC debt relief from the remaining official creditors, including several multilateral and regional creditors. We have initiated discussions on debt cancellation with Angola and Portugal and will try to conclude these agreements as soon as possible, thereby securing adequate financing assurances from creditors to enable the Fund to disburse its share of the topping up assistance.

E. Statistical Issues and Capacity Building

30. **Further improvements in statistics are needed.** The National Institute of Statistics, notwithstanding limited capacity and funding, has made significant progress in improving our national accounts statistics. It has revised GDP in recent years with improved coverage and updated sectoral weights. However, the consumer price index is still compiled using weights based on a decade-old household expenditure survey. Within our very tight budget constraints, we will consider providing some financial support for a new survey. Further progress will also be made to improve budget classification and the consistency between monetary and fiscal data. In addition, to strengthen policy implementation and our capacity building, the government will work with the EU for early appointment of a Resident Economic Advisor.

F. Program Monitoring

31. **The quantitative performance criteria for end-December 2007 (sixth review of the program) remain unchanged** (Table I.1). The nonaccumulation of external payment arrears (as defined in the attached updated Technical Memorandum of Understanding (TMU) is a continuous performance criterion, as are the injunctions against imposing or intensifying restrictions on current payments, introducing new or modifying existing multiple currency practices, concluding bilateral payments agreements that are inconsistent with Article VIII of the Fund's Articles of Agreement, or imposing new or intensifying existing import restrictions for balance of payments purposes. To facilitate our public financial management reforms and support our efforts to improve the investment climate, structural performance criteria and benchmarks are set for end-December 2007 (see Table I.2).

32. **To simplify the use of adjustors in program monitoring, we will only include the unblocked oil funds in the indicative targets on NIR, net domestic assets (NDA), and net credit to the government in 2008.** These unblocked funds are the once-a-year transfers from the NOA to the budget for current-year use. This change will not alter the underlying fiscal and monetary policies; nor will it affect the performance criteria through December 2007. Excluding the remaining balance of the NOA, which is blocked by law, in the indicative

targets would enhance monitoring in 2008. The NIR target, as modified, will be consistent with the concept of usable reserves in the balance of payments.

33. **The attached revised Technical Memorandum of Understanding (TMU) sets out the modalities of program monitoring.** This includes definitions of performance criteria and indicative targets; application of adjustors for deviations from programmed amounts of oil signature bonuses, budget support, and net external debt service payments; and data sources and frequency of data reporting.

34. **We have recently provided a draft Annual Progress Report on the PRSP to the Fund and the World Bank**. We look forward to their assessment of the progress we have made in implementing our Poverty Reduction Strategy

Table 1. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2007 and 2008
(Billions of dobras, unless otherwise specified)

	2006		2007					2008	
	Sep. 30		Jun. 30	Jun. 30	Jun 30	Sep. 30	Dec. 31	March 31	Jun. 30
	Base (stocks)	Base (stocks, excl. NOA)	Perf. Criteria Country Report 07/102	Perf. Criteria Country Report 07/102(with adjustors)	Actual	Ind.Target Country Report 07/267	Perf. Criteria Country Report 07/267	Ind.Target	Ind.Target
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	...	...	-97.0	-97.0	-97.0	-116.3	-137.3	-22.6	-80.1
2. Ceiling on changes in net bank financing of the government (cumulative from end–September 2006; billions of dobras at program exchange rate) [1,2,3,4]	-126.8	-20.8	-32.4	162.3	-60.7	-73.9	-33.8	103.2	151.9
3. Ceiling on changes in net domestic assets of the central bank (cumulative from end–September 2006; billions of dobras at program exchange rate) [1,2,3,4]	-289.8	-183.8	-19.6	175.1	-86.5	-7.8	26.3	156.4	133.3
4. Floor on changes in the net international reserves of the central bank (cumulative from end–September 2006; US$ millions) [4,5,6]	41.8	33.4	1.9	-14.1	4.9	2.5	1.0	-4.9	-2.8
5. Ceiling on central government's outstanding external payment arrears (stock, US$ millions) [7]	...	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0
6. Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (cumulative flows from January 2005, € millions) [8,9]	...	...	1.6	1.6	0.0	1.6	1.6	1.6	1.6
7. Ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP (stock, US$ millions) [10]	...	...	1.0	1.0	0.0	1.0	1.0	1.0	1.0
Memorandum items:									
Base money (ceiling; billions of dobras)	273.2	...	302.5	...	318.2	406.3	337.0	350.3	349.6
Currency Issued (ceiling; billions of dobras)	94.4	...	105.0	...	88.7	96.8	124.5	135.2	122.0
Oil signature bonuses including accrued interest on NOA (US$ millions, cumulative from beginning of year)	0.5	...	28.8	...	16.0	28.9	29.0	0.0	0.0
Transfer from NOA to the budget (US$ millions, cumulative from beginning of year)	...	...	8.0	...	8.0	8.0	8.0	0.0	3.0
Net external debt service payments (cumulative from beginning of the year, billions of dobras at program exchange rate) [11]	-35.4	...	-211.0	...	-213.2	-216.6	-220.0	-3.1	-6.3
Official external program support (cumulative from beginning of the year, billions of dobras at program exchange rate) [12]	7.8	...	0.0	...	0.0	31.4	41.8	0.0	50.0

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

[1] For 2007, the ceiling will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service; and by deviations in the opposite direction in external program support and oil bonu

[2] For 2008, the ceiling will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service; and by deviations in the opposite direction in external program support and transfer

[3] The ceiling will be adjusted downward by the amount of accumulated domestic arrears. For end-June 2007, ceilings were adjusted for domestic areas totaling Dobras 6.5 billion.

[4] The National Oil Account (NOA) at the Central Bank is included in 2007 and excluded in 2008.

[5] For 2007, the floor on net international reserves will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service (including repayments to Nigeria), and by deviations in the same direction for oil bonus

[6] For 2008, the floor on net international reserves will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service (including repayments to Nigeria), and by deviations in the same direction for transfers

[7] This is a continuous performance criterion.

[8] This performance criterion applies not only to debt as defined in point No. 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24, 2000), but also to commitments contracted or guaranteed for which value has not been receive

[9] With a grant element of less than 50 percent.

[10] Debt is defined as in point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24), 2000. Excludes US$15 million in loans from Nigeria during 2002–04, which are to be repaid from signature bonuses in 2007.

[11] Includes US$15 million repayment to Nigeria in 2007.

[12] Official external program support, as defined in the TMU, valued at the program exchange rate of 12,549 dobras per U.S. dollar (valued at projected average exchange rate of 13,935 dobras per U.S. dollar in fiscal table).

Table I.2. São Tomé and Príncipe: Structural Performance Criteria and Benchmarks
March 2007–June 2008

Action	**Performance Criteria / Benchmark**	**Status**
March 2007		
• Adopt decree establishing the new public accounting plan and the related manual of accounting procedures, consistent with the organic public finance law and the public financial management system (SAFE).	Performance Criteria	New accounting plan issued in May 2007. The manual was prepared in September 2007.
• Publish the Handbook of the Oil Resource Management Law (ORML) by posting it on the government website (planned for January 2007).	Benchmark	Handbook prepared but not posted.
• Issue regulations to implement anti–money- laundering and financing of terrorism (AML) law, notably for the Central Risk Unit within the BSCTP and "know-your-client" rules for banks.	Benchmark	Regulations prepared, pending NA approval of the AML law.
June 2007		
• Issue new prudential regulations on credit classification, liquidity, transactions with related parties, and limits on bank net open foreign currency positions.	Performance Criteria	Three regulations (credit classification, liquidity, and transactions with related parties) were issued in August; the regulation on net open foreign currency positions was issued in November 2007.
• Produce the monthly budget execution report (TOFE) using upgraded SAFINHO.	Benchmark	Reports are prepared monthly.
• Finalize the installation of 3,000 prepaid electricity metering systems.	Benchmark	About 1,000 meters installed by September 2007.
September 2007		
• Prepare the 2008 budget in line with the new organic budget law (SAFE) for submission to the National Assembly.	Benchmark	Budget being prepared for submission to NA by October 31, 2007.
December 2007		
• Make progress toward the fully integrated computerized public financial management system (eSAFE) by: (i) the issuance of an administrative decree by the Minister of Finance to establish the IT office; and (ii) the issuance of tenders for the procurement of IT equipment for upgrading SAFINHO.	Performance Criteria	
• Adopt Petroleum Sector Strategy to develop the Exclusive Exploration Zone (EEZ).	Benchmark	
• Issue new regulations on capital adequacy, internal control and auditing, bank financial reporting, and credit to employees.	Benchmark	
March 2008		
• Establish a Directorate of Accounting and an IT office. Install IT equipment.	Benchmark	
• Revise the commercial codes, with external technical assistance, in order to reduce the cost and time of doing business in São Tomé and Príncipe.	Benchmark	
June 2008		
• Revise the mechanism for setting the daily official exchange rate to keep the spread between the official and commercial banks exchange rates within the permissible range.	Benchmark	
• Prepare regulations under the SAFE law.	Benchmark	
• Put in place new modules to implement the public accounting system and train users.	Benchmark	

APPENDIX I. ATTACHMENT II—TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This technical memorandum of understanding (TMU) contains definitions and adjuster mechanisms that are intended to clarify the measurement of variables in Table 1, Quantitative Performance Criteria, PRGF Arrangement, 2006–07, which is attached to the Memorandum of Economic and Financial Policies. Unless otherwise specified, all quantitative performance criteria and benchmarks will be evaluated in terms of cumulative flows from end-September 2006.

Provision of Data to the Fund

2. Data with respect to all variables subject to performance criteria and indicative targets will be provided to Fund staff monthly with a lag of no more than four weeks for data on the net domestic assets and net international reserves of the Central Bank of São Tomé and Príncipe (BCSTP) and eight weeks for other data. The authorities will transmit promptly to Fund staff any data revisions. For variables that are relevant for assessing performance against program objectives but are not specifically defined in this memorandum, the authorities will consult with Fund staff as needed on the appropriate way of measuring and reporting. Performance criteria included in the program, as defined below, refer to domestic primary balance of the central government, net bank financing of the central government, net domestic assets and net international reserves of the central bank, external payments arrears, nonconcessional medium and long-term external debt, and short-term external debt.

Definitions

3. **Government** is defined for the purposes of this TMU to comprise the central government, which includes all governmental departments, offices, establishments, and other bodies that are agencies or instruments of the central authority of São Tomé and Príncipe. The central government does not include the operations of state-owned enterprises.

4. **Government domestic revenue (excluding oil revenue)** comprises all tax and nontax revenue of the government (in domestic and foreign currency), excluding foreign grants, the receipts from the local sale of in-kind grants (e.g., crude oil received from Nigeria, food aid, etc.), and any gross inflows to government on account of oil signature bonus receipts and accrued interest in the National Oil Account (NOA). Revenue will be measured on a cash basis as reported in the table of government financial operations prepared by the Directorate of Budget and the Directorate of Treasury in the Ministry of Planning and Finance.

5. **Domestic primary expenditure** comprises all government spending assessed on a commitment basis (base *compromisso*), excluding (i) foreign-financed capital expenditure; (ii) foreign-financed expenditure under the overseas scholarship program that is externally financed; and (iii) scheduled interest payments. Reporting of government domestic expenditure will be based on the state budget execution prepared every month by the

Directorate of Budget and the Directorate of Treasury in the Ministry of Planning and Finance.

6. Within domestic primary expenditure, **propoor expenditure** refers to government outlays recorded in the budget nomenclature that have a direct effect on reducing poverty, as agreed with the IMF and World Bank staffs. These expenditures, which include both current and capital outlays, are defined as follows:

a. **Propoor current spending**: These cover the following ministries and expenditure categories (by budget code) as described in the matrix below:

Code	Description of expenditure	Ministry of Education	Ministry of Health	Ministry of Labour
01.00.00	Despesa com Pessoal	x	x	x
02.01.05	Outros bens duradouros	x	x	
02.02.02	Combustiveis e lubrificantes	x	x	x
02.02.04	Alimentacao	x		
02.02.05	Medicamentos	x	x	
02.02.06	Roupas e clasados	x	x	x
02.02.09	Outros bens nao duradouros	x	x	
02.03.01.01	Agua e energia	x	x	x
02.03.02	Conservacao de bens	x	x	
02.03.06	Comunicacoes	x	x	x
04.02.01	Instituicoes particulares	x		x
04.03.01	Particulares (Junta de Saude)	x		x
04.04.02	Outras transferencias para exterior		x	
06.01.00	Ensino e formacao		x	
06.04.01	Custos recorrentes de projectos	x		
06.04.04.02	Outros Diversos	x	x	

Expenditures on fuels and lubricants (*combustíveis e lubrificantes*) that are effected for administrative purposes are excluded. Likewise, food (*alimentação*) and clothing and shoes (*roupas e calçados*) supplied to administrative staff are excluded.

For 2007 onward, the definition of propoor current spending, defined in the matrix above, will be based on the new budget nomenclature.

b. **Propoor capital spending:** This covers projects that are deemed to have a direct impact on alleviating poverty in the following sectors: education, health, social safety nets, agriculture and fisheries, rural development, planning and finance, youth and sports, provision of potable water, and electrification.

7. The **domestic primary balance** is defined as the difference between government domestic revenue and domestic primary expenditure. This balance for end-September 2006 was assessed at DB –109.6 billion, broken down as follows:

Government domestic revenue:	Db 217.3 billion
Less: Government primary expenditure (as defined in paragraph 5)	Db 326.9 billion
Equals: Domestic primary balance:	Db –109.6 billion

8. **Domestic arrears** are defined as the difference between expenditure on a commitment basis and cash payments (amounts past due and unpaid).

9. **The program exchange rate** for the purposes of this TMU will be Db 12,548.5 per U.S. dollar. The exchange rate of the dobra against the euro will be 15,952.93 and against the SDR will be 18,526.31.

10. **Net bank financing of the central government (NCG)** is defined as the stock of all outstanding claims on the government held by the BCSTP, less all deposits held by the central government with the BCSTP, plus the stock of all outstanding claims on the government held by deposit money banks (DMBs),[1] less all deposits held by the central government with DMBs as they are reported monthly by the BCSTP to the IMF staff. The National Oil Account (NOA) at the BCSTP is included in 2007 and excluded in 2008. All foreign exchange–denominated accounts will be converted to dobras at the program exchange rate. At end-September 2006, outstanding net bank financing of the government was assessed at Db –126.8 billion, broken down as follows:

BCSTP credit, including use of IMF resources:		Db 105.8 billion
Less: government deposits with BCSTP:		Db 226.3 billion
Of which:	National Oil Account (NOA)	Db 106.0 billion
	Treasury foreign currency–denominated accounts	Db 43.9 billion
	Treasury local currency–denominated accounts	Db 28.7 billion
	Account for HIPC relief[2]	Db 20.3 billion
	Account for MDRI relief[3]	Db 0.0 billion
	Counterpart deposits	Db 22.6 billion
	PRGF disbursement account	Db 4.7 billion

[1] Deposit money banks (DMBs) refer to other depository corporations, as defined in the *Monetary and Financial Statistics Manual.*

[2] Pending the use of HIPC debt relief for propoor spending.

[3] Pending the use of MDRI relief for propoor spending.

Equals: Net credit to government by the BCSTP:	Db –120.5 billion
Plus: DMBs credit:	Db 0.0 billion
Less: Government deposits with DMBs (including counterpart funds):	Db 6.3 billion
Equals: Net bank financing of the government:	Db 126.8 billion

11. **Base money** is defined as the sum of currency issued—which consists of currency outside banks and cash in vaults—and bank reserves, at the program exchange rate. Bank reserves refer to reserves of commercial banks held with the central bank and include reserves in excess of the reserve requirements. At end-September 2006 base money was assessed at dobras 273.2 billion, calculated as follows:

Currency issued:	Db 94.4 billion	
Of which:	Cash in vaults:	Db 13.7 billion
	Currency outside banks:	Db 80.7 billion
Plus: Bank reserves:		Db 178.7 billion
Of which:	In dobras	Db 80.5 billion
	In foreign currency	Db 98.2 billion
Equals: Base money:		Db 273.2 billion
Of which:	In dobras	Db 175.0 billion

12. **Net international reserves** (NIR) of the BCSTP are defined for program-monitoring purposes as short term-term foreign assets of the BCSTP minus short-term external liabilities. All short-term foreign assets that are not fully convertible external assets readily available to and controlled by the BCSTP (i.e., they are pledged or otherwise encumbered external assets, including but not limited to the HIPC umbrella SDR account and assets used as collateral or guarantees for third-party liabilities) will be excluded from the definition of NIR. The NOA at the BCSTP is included in 2007 and excluded in 2008. All values are to be converted to U.S. dollars at actual market exchange rates prevailing at the test date. At end-September 2006 NIR was assessed at Db 524.6 billion, calculated as follows:

Net international reserves:		Db 524.6 billion
Of which:	Gross reserves:	Db 552.3 billion
	Of which: NOA	Db 106.0 billion
	Short-term liabilities:	Db –27.6 billion
Plus: Other foreign assets:		Db 91.9 billion
Plus: Medium and long-term liabilities:		Db –53.6 billion

Equals: Net foreign assets:	Db 563.0 billion

Memorandum item:

Net international reserves minus NOA minus bank foreign currency deposits with the central bank	Db 320.4 billion

13. **Net domestic assets** of the central bank of São Tomé and Príncipe are defined as the difference between base money and net foreign assets of the BCSTP, all at programmed exchange rates. The NOA at the BCSTP is included in 2007 and excluded in 2008. All foreign-denominated accounts will be converted to dobras at the program exchange rate. At end-September 2006, net domestic assets were assessed at dobras –289.8 billion, calculated as follows:

Base money:	Db 273.2 billion
Less: Net foreign assets:	Db 563.0 billion
Equals: Net domestic assets of the BCSTP:	Db –289.8 billion

14. **Treasury deficit** of the BCSTP is defined as revenue (excluding unrealized valuation changes) minus costs minus investment.

15. The performance criterion on **short-term external debt** refers to the outstanding stock of external debt with an original maturity of one year or less (including overdraft positions) and owed or guaranteed by the government or the BCSTP.[4] At end-September 2006 the stock of short-term external debt stood at US$16.0 million.[5]

16. The performance criterion on **nonconcessional medium- and long-term external debt** refers to the contracting or guaranteeing of external debt with original maturity of more than one year by the government or the BCSTP.[6] [7] Debt rescheduling and restructuring are

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[4] The term "debt" is defined in accordance with point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (Decision No. 12274-(00/85) August 24, 2000).

[5] This amount includes three nonconcessional loans from Nigeria totaling US$15 million that were previously classified under nonconcessional medium-term external debt. They were reclassified as short-term debt after a joint World Bank-IMF debt sustainability analysis mission in April 2006.

[6] This performance criterion applies not only to debt as defined in point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* adopted on August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received.

[7] The concessionality of loans is assessed according to the reference interest rate by currency published by the Development Assistance Committee of the Organization for Economic Cooperation and Development. For loans of terms of no less than 15 years, the 10-year average of commercial interest reference rates for the currency in which the loan is denominated will be used. For loans of shorter terms, the six-month average will apply. A loan is deemed to be on concessional terms if, on the date of initial disbursement, the ratio of the present value of the loan, calculated on the basis of the reference interest rate, to the nominal value of the loan is less than 50 percent (in other words, a grant element of at least 50 percent). For currencies with no available reference interest rates, the SDR rate will be used. This performance criterion does not apply to Fund resources.

excluded from the ceilings set on nonconcessional borrowing. Medium- and long-term debt will be reported by the Debt Management Unit of the Ministry of Finance and Planning and (as appropriate) by the BCSTP, measured in US dollars at current exchange rates. The government will consult with IMF staff before contracting obligations if it is uncertain as to whether those obligations are within the performance criterion limits.

17. The nonaccumulation of new **external payment arrears** is a continuous performance criterion. Government external payment arrears are defined as all unpaid external public debt obligations, according to the data established by the Debt Management Unit of the Ministry of Planning and Finance and (as appropriate) by the BCSTP, except for arrears pending rescheduling arrangements. The latter will be considered technical arrears. Debt would be deemed to be in arrears when it has not been paid by the time it is due, unless arrears have been otherwise contractually defined. The performance criterion relating to external arrears does not apply to those pending the signing of bilateral agreements in the context of debt-rescheduling with the Paris Club and other bilateral creditors.

18. **Net external debt service payments** are defined as debt service due less interim HIPC debt relief (including multilateral and bilateral relief) and the accumulation of any new external payment arrears, including technical arrears.

19. **Official external program support** is defined as grants and loans, including in-kind aid when the products are sold by the government and receipts are freely usable by the budget, and other exceptional financing provided by foreign official entities and incorporated into the budget. Amounts assumed in the program consistent with this definition are shown in the memorandum item entitled “official external program support” of Table1.

Use of Adjusters

20. **Deviations in receipts of oil signature bonuses, including accrued interest on NOA, in official external program support, and in net external debt service payments,** from amounts projected for the program (see Table I.1) will trigger adjustments for net bank financing of the central government, net domestic assets of the BCSTP, and net international reserves, as indicated below. These deviations will be calculated cumulatively from end-September 2006 (see Table 1).

21. **Ceilings on net bank financing (NCG) of the central government and net domestic assets (NDA) of the BCSTP:** Monthly differences between actual and projected receipts of oil signature bonuses, official external program support, and net external debt service payments in foreign exchange will be converted to dobras at the program exchange rate and aggregated from end-September 2006 to the test date. The ceilings will be adjusted downward by the amount of accumulated domestic arrears. For 2007 the ceilings on NCG and NDA will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service, and by deviations in the opposite direction in external program support and oil bonuses, including accrued interest

on the NOA. The downward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million. For 2008, the ceilings will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service, and by deviations in the opposite direction in external program support and transfers from the NOA to the budget that exceed US$3 million. The downward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

22. **Floor on net international reserves (NIR) of the BCSTP:** The quarterly difference between actual and projected receipts of oil signature bonuses, including accrued interest on NOA; official external program support; and net external debt service payments will be converted to dobras at the program exchange rate and aggregated from end-September 2006 to the test date. For 2007, the floor on NIR will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service (including repayments to Nigeria), and by deviations in the same direction for oil bonuses, including accrued interest on NOA. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million. For 2008, the floor on NIR will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service, and by deviations in the same direction for transfers from the NOA to the budget that exceed US$3 million. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million. In addition, the NIR floor will be lowered by the amount that disbursements under the PRGF arrangement are lower than expected.

Data Reporting

23. The following information will be provided to the IMF staff for the purpose of monitoring the program.

i. Fiscal Data

The Directorate of Budget at the Ministry of Planning and Finance will provide to IMF staff, within two months after the end of each month or quarter, except for the public investment program (PIP), which will be provided three months after each quarter:

- Monthly data on central government operations for revenues, expenditure, and financing, including detailed description of net earmarked resources (*recursos consignados*)

- Monthly data on net credit to the government by the BCSTP, recorded account by account in a format fully compatible with the monetary accounts of the BCSTP
- Monthly detailed data on tax and nontax revenues
- Monthly detailed data on current and domestically financed capital expenditure on commitment (compromisso) and cash payments (caixa)
- Monthly data on domestic arrears by type
- Quarterly data on official external program support (nonproject)
- Quarterly data on the execution of the public investment program (PIP) by project and sources of financing
- Quarterly data on project grant and loan disbursement (HIPC and non-HIPC)
- Quarterly data on bilateral HIPC debt relief
- Quarterly data on project loan disbursements
- Latest outstanding petroleum price structures and submission of new pricing structures (within a week of any changes)

ii. Monetary Data

The BCSTP will provide to IMF staff, within three weeks from the end of each month, the monetary accounts of the BCSTP; other monetary data will be provided within six weeks after the end of each month for monthly data, within two months after the end of each quarter for quarterly data, and within two months after the end of each year for annual data. Daily data will be provided every week no later than the Wednesday following the end of the week, and weekly data will be provided no later than two weeks after the end of the week. The BCSTP will provide:

- Daily data on exchange rates, to be posted on the central bank's web site.
- Daily data on interest rates, to be posted on the central bank's web site.
- Daily liquidity management table, including base money and currency in circulation (see attachment), to be posted on the central bank's web site.
- Weekly net international reserve position, to be posted on the central bank's web site
- Weekly balance sheet data of BCSTP (in BCSTP and IMF formats)
- Monthly balance sheet data of BCSTP (in BCSTP and IMF formats)
- Monthly balance sheet data of individual deposit money banks (in BCSTP and IMF formats)
- Monthly consolidated balance sheet data of deposit money banks (in BCSTP and IMF formats)
- Monthly monetary survey (in BCSTP and IMF formats)
- Monthly central bank foreign exchange balance (Orçamento cambial)

- Quarterly table on bank prudential ratios and financial soundness indicators
- Quarterly data on the BCSTP's financial position (profit and loss statement, treasury deficit, budget execution)

iii. External Debt Data

The Debt Management Unit at the Ministry of Planning and Finance will provide to IMF staff, within two months after the end of each month,

- Monthly data on amortization and interest on external debt by creditor: scheduled, subject to debt relief or rescheduling, and paid
- Quarterly data on disbursements for foreign-financed projects and program support loans

iv. National Accounts and Trade Statistics

The following data will be provided to IMF staff:

- Monthly consumer price index data, provided by the National Institute of Statistics within one month after the end of each month
- Monthly data on imports (value and import taxes collected and arrears) and commodity export values, provided by Customs within two months after the end of each month
- Monthly data on petroleum shipments and consumption (volumes and cif prices, by product), provided by Customs

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

Fifth Review under the Three-Year Arrangement under the Poverty Reduction and Growth Facility—Informational Annex

Prepared by the African Department
(In consultation with other departments)

Approved by Jean A. P. Clément and Scott Brown

December 4, 2007

- **Relations with the Fund**. Describes financial and technical assistance by the IMF and provides information on the safeguards assessment and exchange rate system. At end-October 2007, outstanding PRGF loans amounted to SDR 2.49 million. Completion of the fifth review would allow a disbursement equivalent to SDR 0.423 million.

- **Relations with the World Bank Group**. Describes IDA program and portfolio; and IMF-World Bank collaboration in specific areas.

- **Relations with the African Development Group**. Describes the African Development Fund (ADF) and Technical Assistance Facility (TAF) ongoing projects.

- **Statistical Issues**. Describes the availability and quality of macroeconomic statistics.

Contents Page

Appendices

APPENDIX I—RELATIONS WITH FUND

(As of October 31, 2007)

I. Membership Status: Joined: September 30, 1977; Article XIV

II. General Resources Account:	**SDR Million**	**Percent Quota**
Quota	7.40	100.00
Fund holdings of currency	7.40	100.05

III. SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	0.62	100.00
Holdings	0.02	3.20

IV. Outstanding Purchases and Loans:	**SDR Million**	**Percent Quota**
PRGF Arrangements	2.49	33.67

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
PRGF	Aug 01, 2005	Jul 31, 2008	2.96	2.12
PRGF	Apr 28, 2000	Apr 27, 2003	6.66	1.90
SAF	Jun 02, 1989	Jun 01, 1992	2.80	0.80

VI. Projected Payments to Fund
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2007	2008	2009	2010	2011
Principal	…	…	0.09	0.29	0.13
Charges/Interest	0.01	0.04	0.04	0.03	0.03
Total	0.01	0.04	0.13	0.32	0.16

VII. Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	December 2000
Assistance committed	
by all creditors (US$ Million)	99.20
Of which: IMF assistance (US$ million)	0.00
(SDR equivalent in millions)	0.00 [1]
Completion point date	March 2007
Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	0.00
Interim assistance	0.00
Completion point balance	0.00
Additional disbursement of interest income	0.00
Total disbursements	0.00

[1] Excludes commitment of additional enhanced HIPC assistance of SDR 0.824 million subject to receipt of satisfactory financing assurances from other creditors.

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI):

I. MDRI-eligible debt (SDR Million)[1 2]	1.05
Financed by: MDRI Trust	1.05
Remaining HIPC resources	0.00

II. Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGF**	**Total**
March 2007	N/A	1.05	1.05

[1] The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

[2] Excludes the portion of debt relief to be financed by additional enhanced HIPC assistance, which is subject to receipt of satisfactory financing assurances from other creditors.

IX. Safeguards Assessments:

Under the Fund's safeguards assessment policy, Central Bank of Sao Tome and Principe (CBSTP) was subject to a full safeguards assessment with respect to the PRGF arrangement approved on August 1, 2005. The assessment, which was completed on August 2, 2004, found vulnerabilities in the area of financial reporting, internal audit and internal control. Measures to strengthen the control framework and help safeguard Fund resources were proposed. Some recommendations have been implemented, including contracting annual external audits, endorsing plans to modernize the BCSTP's internal audit function, and adopting International Financial Reporting Standards (IFRS) as the bank's accounting framework. Progress in the implementation of IFRS has been slow.

IX. Exchange Arrangements:

The IMF classifies São Tomé and Príncipe’s exchange rate regime as managed floating with no pre-announced path for the exchange rate. The official exchange rate is determined daily as a weighted average of the previous day’s selling rates in the commercial banks and the outcomes of central bank foreign exchange auctions. In early 2006, the multiple currency practice related to the spread between central bank buying and selling rates was eliminated, and the spread was set at 2 percent. The authorities intend to remove the exchange restriction on transfers abroad of dividends with the new Investment Code. The remaining exchange restriction and multiple currency practices are related to the occasional shortage of foreign exchange in the formal market as a result of the rationing by the central bank of foreign exchange sold at auctions, and the existence of multiple exchange markets (i.e., the official rate, the auction rate, commercial bank rates, exchange bureau rates and the rates of the parallel market) in the absence of a mechanism to ensure that spreads among rates for spot transactions in these markets do not diverge by more than 2 percent at any given time. The intervention currency for the dobra is the U.S. dollar. The official selling exchange rate was Db. 13,607 per U.S. dollar on September 28, 2007.

X. Article IV Consultation:

The Executive Board concluded the last Article IV consultation with São Tomé and Príncipe on March 6, 2006.

XI. Financial Sector Assessment Program (FSAP), Reports on Observance of Standards and Codes (ROSCs), and Offshore Financial Center (OFC) Assessments:

None.

XII. Technical Assistance:

September 2007: STA mission on government finance statistics.

July 2007: STA mission on monetary and financial statistics.

July 2007: MCM mission on banking supervision

March 2007: FAD mission on public financial management.

March 2007: MCM mission on the foreign exchange market.

March 2007: STA mission on balance of payment statistics.

February 2007: LEG mission on tax laws.

November/December 2006: LEG mission on tax codes.

November/December 2006: MCM mission on banking supervision.

November/December 2006: MFD missions on foreign exchange market and monetary operations.

August 2006: MFD mission on banking supervision.

June 2006: MFD mission to assess implementation of technical assistance.

April/May 2006: STA mission on monetary and financial statistics.

February 2006: MFD mission on monetary operations and liquidity management.

January 2006: MFD mission on the foreign exchange market.

December 2005: LEG/MFD mission on the exchange system.

August/September 2005: MFD mission on banking supervision and foreign exchange operations.

February 2005: STA technical assistance mission on national accounts statistics.

January 2005: MFD mission on monetary operations and liquidity management.

December 2004: STA mission to advice on compilation and reporting of monetary statistics.

October 2004: STA technical assistance mission on government finance statistics.

September 2004: MFD multi-sector mission to develop foreign exchange and interbank money markets.

July–September 2004: MFD expert mission on banking supervision.

June 2004: STA technical assistance mission on balance of payments statistics.

July 2004: MFD expert mission on monetary operations.

June 2003: STA technical assistance mission on balance of payments statistics.

March and June 2003: STA technical assistance missions on national accounts statistics.

March 2003 and April 2004: Visits by MFD advisors on monetary policy and banking supervision.

March 2003: STA technical assistance mission on national accounts statistics.

January 1998–December 2001: MFD advisor on the conduct of monetary policy, banking supervision, and foreign exchange management.

June 2001: MFD mission on handling of banking crisis and foreign exchange market organization.

XIII. Resident Representative:

The Fund does not have a Resident Representative office in São Tomé and Príncipe since October 2006.

APPENDIX II—RELATIONS WITH THE WORLD BANK GROUP

(As of November 08, 2007)

IDA operations

1. São Tomé and Príncipe joined the World Bank and IDA in 1977. New lending was suspended between 1992 and 2000 because the country lacked an appropriate macroeconomic framework.

2. The World Bank FY06–09 country assistance strategy (CAS) was well received by the Board in June 2005. Its two principal objectives are (i) to support implementation of the PRSP and (ii) to provide timely assistance to ensure that São Tomé and Príncipe is prepared to maximize the benefits of oil revenues. Given the small size of the program, the CAS is tightly focused on activities in the oil and social sectors, public sector management, and assistance with the HIPC Initiative.

3. Despite its small project portfolio, the Bank program is relatively large for such a small country. There is a broad ESW and AAA program covering oil issues, support for PRSP implementation, assistance with achieving the HIPC completion point, and analysis of trade issues through the Trade Diagnostic Study. A PEMFAR (Public Expenditure Review, Public Finance Management Review and Procurement Review) has been delivered to the authorities and is awaiting government comments. The Bank also supports government reforms by providing advisory services in the petroleum sector, telecommunications, and the environment. An Institutional Development Grant (IDG) was approved in early 2005 to support the government's judicial reform program. A GEF (Global Environmental Fund) was approved in late 2004 to support the drafting of a national action plan to adapt to environmental and global warming impacts. A grant was approved in May 2006 to support statistical capacity building. The Bank is preparing a Development Policy Operation (DPO) of US$4.0 million to be delivered in FY08 based on the implementation of the Government's reform program. .

4. Current IDA commitments for the two current projects amount to US$11.5 million, of which US$6.3 million is undisbursed. The Bank supports the health and the education sectors through its Social Sector Project of US$6.5 million, of which US$1.5 million consists of an IDA grant. The Bank supports the PRSP process, public expenditure management, and petroleum sector supervision through its Governance Capacity Building Technical Assistance Project of US$5 million. The Bank foresees US$2 million additional financing in FY08 for the latter project to support the Government to successfully develop its Exclusive Economic Zone. The two projects are rated marginally satisfactory; their performance is hampered by political instability, weak management, and limited absorptive capacity.

IFC operations

5. São Tomé and Príncipe is not a member of the IFC. FIAS has reviewed the country's tax system and private sector investment.

Contact persons

6. Questions may be addressed to Rafael Muñoz Moreno (telephone: 202-458-8928).

Table1. Statement of IDA Credits as of November 08, 2007

(Millions of U.S. dollars)

Credit Number	Fiscal Year	Purpose	IDA Commitment [1]	Undisbursed
1590	1985	Economic rehabilitation	5.0	0.0
A029	1987	Special African Facility	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	0.3
2343	1992	Health and education	11.4	0.7
3428	2000	Public resource management project	7.5	1.9
3429	2000	Public resource management technical assistance	2.5	0.0
3902	2004	Social sector support project	6.5	3.0
3993	2005	Governance Capacity Building technical assistance	5.0	2.3
	Total:		83.4	8.2
Of which: repaid			7.8	

[1] Less cancellation.

IMF-World Bank collaboration in specific areas

7. IMF and World Bank staffs collaborate on (i) macroeconomic discussions with the government; (ii) monitoring the PRSP implementation process (JSAN); (iii) analysis and reforms in oil revenue management, the setting up of a computerized public expenditure management system, and the PRSP process; and (iv) other structural reforms, including tax reform. Table 2 briefly describes each area and the specific policy advice support each institution provides.

Table 2. Areas of Bank-Fund Collaboration

Area	Description	Specialized Advice/Reforms Supported by the Fund	Specialized Advice/Reforms Supported by the Bank
PRSP implementation process	Regular Bank and Fund missions Elaboration of JSAN on PRSP and on PRSP First Annual Progress Report	Economic program consistent with PRGF arrangement.	Reforms in education and health sectors Judicial reform and advice on setting up tribunals of arbitration for business disputes Reform of public finance management and improved transparency of budgetary process Public expenditure review in the health sector
Oil revenue management	Regular Bank and Fund missions and Bank technical assistance missions	Advice on the use of oil proceeds consistent with Oil Revenue Management Law (ORML). Follow-up on transparency and governance issues.	Advice on the use of oil proceeds consistent with ORML Technical assistance to strengthen capacity of the country to address analysis, understanding, and management of petroleum-related topics, including, but not limited to, technical assistance: to the National Agency for Oil (ANP); for strategy on oil sector development, including its Exclusive Economic Zone; and on implementation of the ORML, including establishment of oversight and control committees.
Public expenditure and external debt management	Bank and Fund technical assistance and other missions	Recommendations for reform of public expenditure management systems	Analysis and advice on reform of the public finance management (PFM) system, notably assistance with the design of a fully integrated, computerized budget and public expenditure management system; and the implementation of the Commonwealth Secretariat's debt-recording management system and procurement reforms.
Other structural reforms	Bank and Fund technical assistance and supervision missions	Banking sector supervision, foreign exchange auction management, liquidity management, central bank safeguards assessment. Technical assistance on tax reform including new personal and corporate income tax codes, tax procedural codes, and investment code.	Social sector support policies and capacity building (social sector support project) Assistance to asses the financial situation of EMAE and develop an action plan to reform State Owned Enterprises Diagnostic and Trade Integration Study (DTIS) Simplification of business registration procedures

APPENDIX III—RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of August 15, 2007)

1. São Tomé and Príncipe became a member of the African Development Bank Group in 1976. To date, the Bank Group has financed 25 operations in the country. The net commitments amount to UA 90.4 million,[1] comprising UA 89.4 million of African Development Fund (ADF) [2] and Technical Assistance Facility (TAF) resources and UA 1.00 million of Nigerian Trust Fund (NTF) resources. The sectors benefiting from AfDB Group financing are agriculture (26 percent), transport (25 percent), multi-sector [3] (21 percent), social sector (17 percent), and public utilities (11 percent). These operations have helped build and rehabilitate basic economic and social infrastructure (roads, airport, electricity, water, schools, and health centers) and have strengthened São Tomé and Príncipe's economic and institutional capacities. The AfDB has had a national program office since 1999.

2. The AfDB has three ongoing projects in water and sanitation and hydrous diseases, human resource development and agriculture. These projects, in accordance with the PRSP, focus on the main factors affecting poverty. The disbursement rate was 35.20 percent as of August 2007. The water and sanitation and hydrous diseases project is close to completion. Two of these projects have started recently, namely the human resource development project and the second phase of the livestock development project approved in May 2006 to help diversify the economy. The human resource development project will tackle cross-sectoral capacity-building by providing for training in literacy, information, and community organization, as well as specialized vocational training adapted to specific demands, particularly in the oil and tourist sectors.

3. The AfDB Group assistance strategy for 2005–09 (Country Strategy Paper 2005–09) rests on two pillars: poverty reduction in rural area and promotion of governance in public finance management. The indicative country allocation on ADF-X resources (2005–07) is UA 4.5 million in the form of grants. The first pillar will help promote and diversify the country's economic base, especially the agricultural and rural sector, and reinforce operations in the social sectors. Under this pillar, the livestock development support project-phase II (UA 4 millions) was approved in May 2006. The second pillar will support macroeconomic reforms and governance, through an institutional support project on governance and a technical assistance on the PRSP process, which will help improve public finance management and institutional capacity building to prepare the country for the forthcoming oil era. Given the considerable needs for institutional capacity building, the AfDB will finance strategic economic and sector studies, such as the Country Governance Profile; the joint study with the World Bank on the integrated fiduciary assessment (PER/CFAA/CPAR); the

[1] The exchange rate for August 2007 is UA 1 = US$1.53122.

[2] ADF is the concessional window (or grant for ADF-X for high debt countries), on the same conditions as IDA, of the African Development Bank Group.

[3] Institutional support and structural adjustment programs.

transport sector study; and the insular costs study. Furthermore, the AfDB will finance regional capacity building initiatives, within CEMAC, ECCAS, the African Portuguese-speaking countries and the small insular countries.

4. In addition, the AfDB will continue to provide the country with financial assistance through the enhanced HIPC initiative. In April 2001 the AfDB approved debt relief of US$34.35 million in end 1999 NPV terms. In light of the delay in the HIPC process, the AfDB extended its interim debt relief period until the country reaches the completion point in May 2007 with an additional assistance (topping up) of US$ 9.08 million in end-2005 NPV terms.

Table 1. Ongoing Projects as of August, 2007

(Millions of UA) [1]

Title of Projects	Window	Commitment	Disbursement Rate
Water and sanitation and hydrous diseases	ADF ADF grant	3.2 1.0	91.16 percent 92.85 percent
Support for human resource development	ADF ADF grant	3.50 0.50	5 percent 43.6 percent
Livestock Development Project – Phase II	ADF grant	4.0	1.44 percent
Total		*12.2*	*35.20 percent*

[1] Exchange rate for August 2007 is UA 1 = US$1.53122

APPENDIX IV. STATISTICAL ISSUES

Introduction

1. Although economic data are generally adequate for surveillance, serious financial, human, and technological resource constraints have slowed down efforts to strengthen the statistical system.

2. São Tomé and Príncipe has participated in the Fund's General Data Dissemination System (GDDS) since April 20, 2004. The metadata and plans for improvement have not been updated since the original metadata were posted on the DSBB. Over the period 2003–06, the country has benefited from technical assistance from STA and other providers, largely under the GDDS project for Lusophone Africa.

National accounts

3. Statistics on GDP/GNP are compiled on a yearly basis and provided at the time of the Article IV consultation. STA provided technical assistance in national accounts (NA) to the National Statistics Institute (NSI) during February–March 2005 and January 2006 in the context of a GDDS project for Lusophone countries. Low response rate and/or insufficient rigor of the responses to the business surveys, including those from important enterprises, continue to affect the quality of the business data compiled.

4. A new GDP series (2001-2006) became available in early-2007. The new GDP estimates (2001=100) cover: (i) GDP by production approach at current and constant prices; and (ii) cross-classification tables by industry sectors. The revised series reflect more accurately economic developments in recent years. Based on the most recent population census, corporation census, and living conditions survey, higher weights are now attached to the sectors that experienced faster growth, such as trade, transportation and communication, and services. Despite the considerable upward revision in GDP, São Tomé and Príncipe remains a low income country, with GDP per capita amounting to about $771 in 2006, compared to $497 before this revision. While the revision of the GDP series is a significant improvement, a number of shortcomings remain. Further improvements would require input from a new household expenditure survey (rather than living conditions survey), using producer prices, and better estimates for agricultural production.

Consumer prices

5. The CPI is calculated monthly and reported to AFR with a lag of one month. Since 1997 the CPI weights have been based on a three-month household survey conducted in 1995. Thus, an updated and more comprehensive household expenditure survey is needed. Current price surveys only cover the capital, although there are plans to implement regional surveys.

Government finance statistics

6. Detailed revenue and expenditure data are compiled and reported to AFR. The main areas that need to be strengthened are (i) Ministry of Planning and Finance (MOF) monitoring of expenditures on projects financed by donors and (ii) financing items. All project loans financed by donors are programmed in the budget, but some are executed independently. The government has asked development partners to help it record all external assistance in the budget. Recording of financing items is expected to improve as debt data management capacity is strengthened.

7. A STA government finance statistics (GFS) mission was undertaken in October 2004 to help the MOF compile and disseminate GFS for the general government in accordance with the IMF's Government Finance Statistics Manual 2001(GFSM 2001). The mission prepared bridge tables showing correspondence between national budget classification and GFSM 2001 concepts used to compile GFS for reporting to STA and AFR, as well as in MOF policy work. Given the importance of oil-related revenues, the mission also reviewed the classification of oil revenues under the Oil Revenue Management Law and made recommendations on classification of such transactions. In September 2007, a STA follow-up mission found some progress with regard to the recommendations made by the 2004 mission. In particular, in January 2007 a new budget law was approved that significantly improved national budget classifications. Notwithstanding these efforts, faster statistical progress is hampered by an inadequate accounting system.

Monetary and financial statistics

8. STA missions provided technical assistance on monetary statistics in December 2004, April/May 2006, and July 2007. The accuracy of monetary data has improved although the lags with which the Central Bank of São Tomé and Principe (BCSTP) reports to the IMF have increased again in recent months.

9. The missions found that the BCSTP monthly trial balance sheets were broadly adequate to compile monetary statistics in line with the *Monetary and Financial Statistics Manual (MFSM).* However, the plan of accounts of the other depository corporations is not adequate to derive monetary statistics consistent with the *MFSM*, particularly with regard to the sectorization of institutional units.

10. A follow-up mission for implementing the standardized report forms (SRFs) for reporting monetary and financial statistics to the IMF was held for June 2007. The mission assisted in finalizing these forms and in deriving the integrated monetary database to meet the data needs of the BCSTP, STA, and AFR. The mission also provided on-the-job-training to compilers.

External sector statistics

11. There are significant weaknesses in the collection of source data related to merchandise trade. Some transactions, including certain imports related to investment, are not fully captured in the balance of payments (BoP). Monthly data on the main exports and

imports are reported to AFR regularly but with some lags in recent months, and unit prices and volumes of exports are only occasionally included. Annual BoP data up to 2003 were reported to STA in 2004.

12. The GDDS Lusophone project has targeted a substantial improvement in the source data, including the response rate to the surveys, and in the methodology for compiling the BOP in line with the *Fifth Edition of the Balance of Payments Manual*. A mission in June 2003 reviewed the shortcomings of reported current and financial account transactions and concluded that weaknesses were mainly due to under coverage, including of foreign direct investment and commercial bank reports on international transactions.

13. A follow-up mission in June 2004 found that despite efforts to implement the previous recommendations, several measures, in particular those related to improving source data, were only partially implemented, if at all. As a result, inconsistencies in the classification of BoP operations persisted and certain components continued to be largely estimated. Resource constraints, particularly with regard to qualified staff, contribute to the lack of improvement in the response rate to surveys. The mission recommended improving coordination and data sharing among data-producing agencies, intensifying contacts with survey respondents, and using alternative sources to improve source data. In March 2007, a follow-up STA mission found that little progress has been achieved in implementing recommendations of previous missions, owing primarily to resource constraints in the Central Bank of São Tomé e Principe. The mission assisted the authorities in reconciling balance of payments data and outlined a set of recommendations and detailed work plan to improve compilation capacity.

14. The authorities have built on previous efforts to strengthen debt data management. A unit was created in late 2003 within the MOF. The authorities are reconciling debt records with creditors and the Commonwealth Secretariat debt recording and management system (CS-DRMS) is being operationalized.

Common Indicators Required for Surveillance
(As of July 31, 2007)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange rates	Jul 2007	Jul 2007	D	D	D
International reserve assets and reserve liabilities of the monetary authorities [1]	Jun 2007	Jul 2007	M	M	M
Reserve/base money	Jun 2007	Jul 2007	D	D	D
Broad money	May 2007	Jul 2007	M	M	M
Central bank balance sheet	Jun 2007	Jul 2007	M	M	M
Consolidated balance sheet of the banking system	May 2007	Jul 2007	M	M	M
Interest rates [2]	Jul 2007	Jul 2007	D	D	D
Consumer Price Index	Jun 2006	Jul 2007	M	M	M
Revenue, expenditure, balance and composition of financing [3] – general government [4]	NA	NA	NA	NA	NA
Revenue, expenditure, balance and composition of financing [3]– central government	Mar 2007	May 2007	M	M	M
Stocks of central government and central government-guaranteed debt [5]	Dec 2006	Mar 2007	A	I	A
External current account balance	Dec 2005	Apr 2006	A	I	A
Exports and imports of goods	Mar 2007	Apr 2007	A	I	A
GDP/GNP	2006	Mar 2007	A	I	A
Gross external debt	Dec 2006	Mar 2007	Q	Q	I

[1] Includes reserve asset pledged or otherwise encumbered as well as net derivative positions.

[2] Central bank's reference rate

[3] Foreign, domestic bank, and domestic non-bank financing.

[4] The general government consists of the central government (budgetary funds, extrabudgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); not available (NA).

Press Release No. 07/306
FOR IMMEDIATE RELEASE
December 21, 2007

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fifth Review of São Tomé and Príncipe's PRGF Arrangement and Approves PRGF and HIPC Topping-Up Assistance Disbursements

The Executive Board of the International Monetary Fund (IMF) today completed the fifth review of São Tomé and Príncipe's economic performance under a three-year Poverty Reduction and Growth Facility (PRGF) arrangement and the review of assurances for the disbursement of the Fund's share of topping-up under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative. The completion of the PRGF review enables the release of an amount equivalent to SDR 422,000 (about US$700,000), which would bring total disbursements under the PRGF arrangement to SDR 2.5 million (about US$4 million).

The three-year arrangement was approved on August 1, 2005 (see Press Release No. 05/187), for a total amount of SDR 2.96 million (about US$4.6 million) to support the government's economic program for 2005-08.

In completing the review, the Executive Board approved a waiver of the nonobservance of an end-June 2007 structural performance criterion related to the issuance of prudential regulations, based on remedial measures taken by the authorities.

In addition, the Executive Board approved the disbursement of topping-up HIPC assistance of SDR 824,000 (equivalent to US$1.2 million). Together with accrued interest, the total disbursement to São Tomé and Príncipe amounts to SDR 868,000 (about US$1.4 million).

In commenting on the Executive Board's discussion on São Tomé and Príncipe, Mr. Murilo Portugal, First Deputy Managing Director and Acting Chair, stated:

"São Tomé and Príncipe's recent economic performance has been encouraging. Real GDP growth has remained robust in 2007, inflation fell significantly, the domestic primary fiscal deficit was reduced, and international reserves have exceeded the targets under the PRGF-supported program.

"The authorities are committed to consolidate the stabilization gains and safeguard fiscal sustainability. They will continue to strengthen policy implementation and improve public financial management. In particular, it will be necessary to contain personnel costs and non-priority expenditure to make room for increased poverty-related spending while reducing the primary fiscal deficit. The central bank is committed to implementing a proactive monetary policy to manage liquidity growth and counter inflationary pressures stemming from the rising oil import costs. Continued fiscal adjustment will further support the reduction of inflation.

"Intensified structural reforms will aim at achieving sustained private sector-led growth and improving the investment climate, in particular by reducing administrative costs and delays in starting a business. The authorities also need to press ahead with plans to reform the financial sector and enhance the institutional framework for transparent management of oil exploration and receipts.

"In view of the uncertain oil prospects, it will be important to continue to pursue prudent fiscal and external financing strategies so as to maintain debt sustainability over the medium term. The authorities are committed to strengthening debt management and refraining from external borrowing on nonconcessional terms," Mr. Portugal said.

Statement by Laurean W. Rutayisire Executive Director for São Tomé and Príncipe
Decembr 21, 2007

On behalf of my São Tomé and Príncipe authorities, I would like to thank the Board, Management and Staff for their continued support and useful advice to São Tomé and Príncipe. My authorities are grateful to the international community for increasing its external assistance to São Tomé and Príncipe. They particularly thank creditors for providing sufficient assurances for the disbursement of the Fund's share of topping-up under the HIPC initiative.

I. Recent Developments

As expected at the time of the 4th Review under the PRGF, economic activity has remained robust in 2007. Real output growth is projected to reach 6 percent this year, driven by tourism-related construction, commerce and services, boosted by foreign direct investment. My authorities maintained their prudent policy stance aimed at reducing inflation. As a result of their sustained efforts, inflation went down to 14 percent in June 2007 from a peak of 26 percent in August 2006.

In the **fiscal sector**, domestic revenue in the first half of the year have been lower than expected owing to lower than projected imports duties and nontax revenue, although income tax collection improved. In light of this development, public expenditure, notably domestically-financed capital expenditure and HIPC-related social spending was contained accordingly. As result, the primary fiscal deficit met the performance criterion for end-June 2007. Strongly committed to maintain fiscal sustainability, the authorities have continued to adjust domestic petroleum prices to changes in international prices as evidenced by the increases from 13 to 24 percent in oil-related products in the archipelago in September 2007. Likewise, electricity and water tariffs were increased by 40 to 60 percent to recover production costs and hence reduce burden on scarce public resources. In July 2007, the authorities agreed on 35 percent increase in wages, instead of 18 percent as initially programmed. They also agreed on payment of other wage-related benefits following the negotiations with civil service unions.

The implementation of fiscal reforms is advancing. The Minister of Planning and Finance has been producing monthly budget execution reports using the pilot budget preparation and execution program (SAFINHO). The approval of the tax reform package is experiencing a delay as some elements of this package are still under discussion at the National Assembly. The US Millenium Challenge Corporation (MCC) has approved a threshold program that will provide technical assistance for strengthening revenue administration.

In the **monetary sector**, the Central Bank of São Tomé and Príncipe's (BCSTP) continued efforts to mop up excessive liquidity, consistent the net international reserves objective in a context of a flexible exchange rate regime, have born fruit. Indeed, continued sterilization of use of oil bonuses and HIPC savings, and containment of net credit to government resulted in a decline of the base money growth from over 110 percent in mid-2006 to about 20 percent in the second quarter of 2007, thereby contributing to the sharp reduction in inflation. The exchange rate which remains market-determined depreciated slightly by 3 percent and the spread between the central bank and commercial banks exchange rate halved since the resumption of foreign exchange auctions in December 2006.

The strengthening of the central bank's operations is progressing well with notably a proactive communication strategy and a closer collaboration with the Ministry of Finance to improve liquidity forecast and inform the central bank's foreign exchange operations. The four planned prudential regulations have been issued, although with some delays due to difficulties to secure the needed technical assistance in this area. The Central Bank has also set up the Central Risk Unit and started implementing the "know-your-clients" rules for banks.

On **structural reforms**, my authorities have prepared and sent to the NA a series of revised legislations aimed at improving the business climate. These include, among others, the investment code, the revised labor code. It is their intention to submit to the NA a legislation that will reduce the cost of investing and doing business in São Tomé and Príncipe. The restructuring of the electricity and water company (EMAE) is well underway. In addition to the adjustment of tariffs, about 1000 prepaid electricity meter systems has been installed in an effort to improve revenue collection.

Despite the uncertainty surrounding oil reserves, significant progress has been made in enhancing transparency and governance in the **oil resources management**. With World Bank support, the Oversight Committee for auditing and supervising petroleum receipts and expenditures is now operational. The Minister of Natural Resources and Environment issued an order in August 2007 verifying São Tomé and Príncipe's formal adherence to the Extractive Industries Transparency Initiative (EITI). A national coordinator for implementation of the EITI has also been appointed. The National Oil Agency will strive to conduct the licensing round for the Exclusive Zone transparently, consistent with the ORML and the EITI.

Overall, **performance under the program** in the first semester of 2007 has been satisfactory, with all quantitative performance criteria and structural benchmarks for end-June 2007 met. However, as noted above, the structural performance criterion for end-June 2007 on the four prudential regulations was met with delay. As this delay was beyond my authorities' control, they request a waiver for the non-observance of this performance criterion. Based on this satisfactory performance, my authorities are requesting Board approval for the completion of the fifth review of the PRGF-supported program.

II. Financial policies for 2008

The authorities remain committed to macroeconomic stabilization and sustained economic growth. In 2008, policies will continue to be geared towards greater macroeconomic stabilization through further fiscal consolidation and prudent monetary policy. The main objectives of the program for 2008 are to (i) maintain a real GDP growth at 6 percent; (ii) reduce inflation to 9-12 percent; (iii) safeguard international reserves equivalent to about 4 months of imports; and (iv) accelerate the implementation of the reform agenda in order to lay the basis of a private sector-led growth. My authorities stand ready to adjust their policies as needed to meet their program objectives.

In the **fiscal sector**, the 2008 budget which is consistent with the fiscal program under the PRGF has been submitted to the NA for approval. It aims to reduce the domestic primary fiscal deficit to 4.8 percent of GDP compared to the projected 7 percent in 2007. This fiscal consolidation will come mainly from the expenditure side because the revenue impact of the envisaged direct tax reforms, which aim to reduce distortions, would be largely neutral in 2008. The deficit will be financed in part by statutory drawings from the National Oil Account (NOA) and by assistance under the World Bank's Development Policy Operation (DPO) facility.

In addition to the implementation of tax reforms, once they are approved by the NA, fiscal reforms will essentially focus on strengthening tax and customs management and public expenditure management. In particular, a comprehensive wage study will be undertaken as part of the DPO-supported program with a view to revising the salary structure with improved incentives for civil servants, and thereby avoiding the recourse to ad hoc increases in wages. My authorities also intend to review their contribution to the Joint Development Authority (JDA) and make it more consistent with domestic budget constraints and oil revenue prospects. They will increase pro-poor spending through systematic application of the execution mechanisms contained in the new Organic Budget Law and continue to work closely with external development partners to accelerate implementation of foreign-funded projects, while ensuring adequate resources for domestically-funded investment projects. In order to strengthen the monitoring and execution of the 2008 budget, including the use of debt relief resources, my authorities will continue to upgrade SAFINHO and training users. With assistance from multilateral and bilateral donors, efforts will be made to develop SAFINHO into a fully fledged eSAFE system incorporating all public accounts.

The main objective of the **monetary policy** is to reduce annual inflation to 9-12 percent by the end of 2008. This will be achieved by ensuring that the 12-month base money growth remains on a declining trend. To this end, the central bank will continue to use foreign exchange sales to mop up liquidity, consistent with the NIR objective. The central bank is committed to deepening foreign exchange market reform, with a view to complying with obligations under Article VIII, Sections 2(a), 3, and 4 of the IMF's Articles of Agreement.

The adoption of the investment code which foresees, among others, the elimination of exchange restriction on transfer abroad of dividends will be critical in this regard. The Central bank intends to continue with its communication strategy of informing the market on its monetary and exchange policies, and information-sharing meetings with the Ministry of Planning and Finance to ensure the attainment of the program objectives. Following the issuance of the four prudential regulations, the central bank is awaiting the NA's approval of the AML/CFT law to press ahead with the financial sector reform. In order to further strengthen its banking supervision, the central bank is requesting Fund technical assistance in the implementation of the new charts of accounts and quarterly financial reporting by banks.

On **structural reforms**, my authorities intend to make concrete progress in enhancing the investment climate through regulatory reform and upgrading infrastructure. They will work closely with donors to press ahead with reforms in key areas such agriculture, transportation and energy. They believe that the approval by the NA of the new investment code and revised labor code will be a positive step towards a more attractive business climate.

As regards **debt management**, my authorities are fully aware of the importance of ensuring debt sustainability after HIPC and MDRI debt relief. They will refrain from new external borrowing, particularly on commercial terms, and redouble their efforts to seek full delivery of HIPC debt relief from the remaining official creditors. As sufficient assurances for the disbursement of the Fund's share of topping-up under the HIPC initiative have been secured, I request the support of Executive Directors for the proposed decision on this issue.

III. Conclusion

São Tomé and Príncipe has continued to maintain a satisfactory implementation of its economic program supported by the PRGF, thus demonstrating continuous commitment to macroeconomic stabilization and reform. My authorities remain committed to their reform program but given the uncertainty in oil production prospects, they still count on the international community to make further progress towards its objectives of sustained growth and poverty reduction. I therefore call on the international community to continue providing such support.