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Sierra Leone: 2010 Article IV Consultation and First Review Under the Three-Year Arrangement Under the Extended Credit Facility, Request for Modification of Performance Criterion, and Financing Assurances Review—Staff Report; Public Information Notice and Press Release on the Executive Board Discussion; and Statement by the Executive Director for Sierra Leone.

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of a combined discussion of the 2010 Article IV Consultation with Sierra Leone and first review under the three-year arrangement under the extended credit facility, request for modification of performance criterion, and financing assurances review, the following documents have been released and are included in this package:

- The staff report for the combined 2010 Article IV Consultation and First Review Under the Three-Year Arrangement Under the Extended Credit Facility, Request for Modification of Performance Criterion, and Financing Assurances Review, prepared by a staff team of the IMF, following discussions that ended on October 8, 2010, with the officials of Sierra Leone on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on November 18, 2010. 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 Public Information Notice (PIN) and Press Release summarizing the views of the Executive Board as expressed during its December 6, 2010 discussion of the staff report on issues related to the Article IV consultation and the IMF arrangement, respectively.

- A statement by the Executive Director for Sierra Leone.

The documents listed below have been separately released.

Letter of Intent sent to the IMF by the authorities of Sierra Leone
Memorandum of Economic and Financial Policies by the authorities of Sierra Leone
Technical Memorandum of Understanding

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

SIERRA LEONE

Staff Report for the 2010 Article IV Consultation, First Review Under the Three-Year Arrangement Under the Extended Credit Facility, Request for Modification of Performance Criterion, and Financing Assurances Review

Prepared by the African Department

(In consultation with other departments)

Approved by Doris C. Ross and Dominique Desruelle

November 18, 2010

Fund relations. The Executive Board approved on June 4, 2010 a three-year ECF arrangement in an amount equivalent to SDR 31.11 million (30 percent of quota). One disbursement in the amount of SDR 4.44 million was made at the time of the approval.

Past Surveillance. During the 2008 Article IV consultation, Executive Directors observed that enhancing domestic revenue mobilization and strengthening public expenditure management should be a high priority in order to improve the fiscal position and create space for poverty-reducing and infrastructure spending. Directors also called for steps to strengthen bank supervision and implement structural reforms to promote private sector activity. While progress has been made—notably a goods and services tax was introduced, tax administration reforms continued, and bank supervision has improved—further progress is needed in broadening the tax base, rebuilding infrastructure, and developing the private sector.

Staff team. The mission comprised Mr. Mikkelsen (head), Ms. Saxena, Mr. Million and Mr. Stepanyan (all AFR) and Mr. Palmason (SPR). It was assisted by Messrs. Tjirongo and Sandy (Resident Representative Office). Mr. Itam (OED) participated in several meetings.

Discussions. Discussions were held in Freetown, September 8–22, 2010 and in Washington DC, October 4–8, 2010. The mission met with President Koroma, Finance Minister Kamara, Central Bank Governor Sesay, parliamentarians, other government officials, and representatives of civil society and donors.

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Abbreviations and Acronyms

ACC	Anti-Corruption Commission
BOP	Balance of Payments
BSL	Bank of Sierra Leone
DfID	U.K. Department for International Development
DSA	Debt Sustainability Analysis
DTD	Domestic Taxpayer Department
EC	European Commission
ECF	Extended Credit Facility
EU	European Union
FHCI	Free Health Care Initiative
FMR	Financial Management Regulation
FSDP	Financial Sector Development Plan
GBAA	Government Budgeting and Accountability Act
GDP	Gross Domestic Product
GST	Goods and Services Tax
HIPC	Highly Indebted Poor Countries
IMF	International Monetary Fund
JICA	Japan International Cooperation Agency
LTO	Large Taxpayer Office
MDAs	Ministries, Departments, and Agencies
MDG	Millennium Development Goal
MDRI	Multilateral Debt Relief Initiative
MEFP	Memorandum of Economic and Financial Policies
MOFED	Ministry of Finance and Economic Development
MTEF	Medium Term Expenditure Framework
NEER	Nominal Effective Exchange Rate
NRA	National Revenue Authority
PC	Performance Criterion
PFM	Public Financial Management
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
PV	Present Value
REER	Real Effective Exchange Rate
SDR	Special Drawing Right
TA	Technical Assistance
TMU	Technical Memorandum of Understanding

Executive Summary

- **After the economic slowdown in 2009, the outlook this year for Sierra Leone is more favorable.** Growth is expected to pick up due to buoyant output in the service and agriculture sectors. However, inflation will remain in double digits this year owing to the one time jump in prices from the introduction of the goods and services tax, but is expected to decline to single digits in 2011.

- **Program performance was satisfactory in the first half of 2010**. All quantitative performance criteria for end-June 2010 were met. The two structural benchmarks for end-June on implementation of an automatic fuel pricing mechanism and adoption by the Bank of Sierra Leone of new off-site surveillance guidelines were implemented with delays.

- **Article IV consultation discussions** focused on the authorities' development priorities and their financing while maintaining a competitive economy and a sustainable debt outlook. The authorities intend to increase public spending on rebuilding basic infrastructure and improving health care services and fund this by improving tax administration and exploiting the revenue potential from the mining sector. The exchange rate is broadly aligned with its fundamentals, and the risk of debt distress remains moderate.

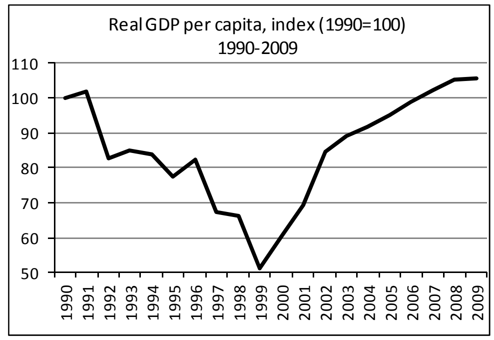
- **Fiscal spending in the second half of 2010 is projected to overshoot the program** because of higher health and infrastructure outlays, higher interest payments, and the clearing of arrears to oil marketing companies. While part of this increase will be funded by higher tax revenues, the authorities are requesting an increase in the program target for net domestic bank financing for end-2010. To support this request, the authorities have committed to a budget framework for 2011 that envisages higher domestic revenue and moderate domestic borrowing. Moreover, they have raised royalties on diamonds and eliminated existing fuel subsidies.

- **Structural reforms** will focus on improving tax administration, strengthening public financial management, and deepening the financial sector. The first two reform areas will help create fiscal space for capital and social spending while the latter complements these efforts by encouraging private sector development.

- **The risks to the program reflect fiscal uncertainties, but they appear to be manageable.** In particular, the development of the public sector wage bill is a concern, following the more than doubling of salaries to health care professionals earlier this year.

I. BACKGROUND

1. **Although macroeconomic stability has been achieved, Sierra Leone remains a post-conflict country whose growth prospects hinge on rebuilding infrastructure and developing an accessible financial sector.** The rebuilding efforts that followed the end of the civil conflict in 2001 are far from complete—the country still suffers from lack of basic infrastructure and weak institutions. Despite relatively high economic growth in recent years, per capita income remains low, poverty is pervasive (estimates show that about 60 percent of the population remains below the poverty line), and Sierra Leone ranks at the bottom of the UN's Human Development Index.



Development Indicators: Sierra Leone (SLE) and Sub-Saharan Africa (SSA)

	1990		2000		2007	
	SLE	SSA	SLE	SSA	SLE	SSA
GDP per capita (US$)	712	2488	403	2877	679	3718
Human Development Index 1/	…	0.45	…	0.50	0.36	0.53
Life expectancy at birth (years)	40	53	42	53	47	55
Adult literacy rate 2/	…	51	…	61	38	64

Sources: Human Development Report, UNDP and IMF staff calculation.
1/ In 2007, Sierra Leone ranked 180 out of 182 countries for which this index was calculated.
2/ Percentage of population aged 15 years and over.

2. **The Government of Sierra Leone launched in 2009 the Agenda for Change to identify the key policy priorities for its poverty reduction strategy through 2012.** The Agenda for Change identifies lack of infrastructure as the key impediment to economic growth and presents a strategy to accelerate public investments in infrastructure and promote private sector development. The strategy also identifies a need to support agricultural development and gradually strengthen health and education services. Although external donors have provided substantive concessional resources to finance an increase in public spending on infrastructure and social development, the financing gaps to implement the strategy are still significant. The focus of the current ECF-supported program is to create fiscal space for those spending priorities by strengthening tax performance and improving the public financial management system, as well as deepening the financial sector.

3. **The medium term outlook for the Sierra Leonean economy is favorable.** Following a period of slow growth, real GDP growth is expected to recover to 4.5 percent in 2010 and increase gradually to 6 percent by 2012, benefiting from the recent completion of the Bumbuna I power station, investment in basic infrastructure, and initiatives to improve the business climate and increase agricultural productivity. The global economic recovery would increase export demand for minerals and cash crops, which should contribute to

exchange rate stability. Combined with expanding domestic food production, this should ease inflationary pressures. Monetary and exchange rate policies will aim at returning to single-digit inflation next year. However, import coverage of gross foreign exchange reserves is expected to decline from the current relatively high level as imports rebound with economic recovery and expansion in investment.

II. Policy Challenges Ahead

4. **Against the backdrop of a difficult international economic environment with continued weak external demand and a likely decline in external budget support to Sierra Leone, the discussions focused on** (i) development priorities and fiscal sustainability; (ii) domestic revenue potential including from mining; (iii) competitiveness of the economy; and (iv) the outlook for debt sustainability.

A. Development Priorities and Fiscal Sustainability

5. **The authorities are determined to implement the Agenda for Change—Sierra Leone's poverty reduction strategy paper (PRSP).** They are embarking on an acceleration of public investments in basic infrastructure to remove one of the key constraints to create an enabling environment for businesses and to reach a sustainable growth path. At the same time, to ensure broad-based economic growth, where the quality of life for all Sierra Leoneans improves, more investment is needed in health and education. The authorities therefore intend to expand public spending on two fronts, in particular, in the coming years:

(i) **Development of basic infrastructure.** The authorities have identified priority projects for roads, energy, water, and sanitation systems across the country (Box 1). The plan will require a more than 10-fold increase in public infrastructure investment in the period 2011–13 compared to 2008–10. Only about one-fourth of the increase in investment is financed from current donor commitments and the projected medium-term budget. However, a significant increase in commitments of concessional project financing is expected from several donors, including the African Development Bank, the European Union (EU), Japan International Cooperation Agency (JICA), the Islamic Development Bank, and India. Nevertheless, a substantial residual financing gap for the three years will need to be closed by either raising domestic resources or identifying additional sources of external financing.

(ii) **Improvements in health care.** To reduce infant and maternal mortality and achieve the MDGs, the government launched a new free health care initiative (FHCI) in April 2010. The initiative involves provision of cost-free medical care and drugs to these vulnerable groups, hiring of health professionals and a significant improvement in the compensation to professional health workers to ensure elimination of user fees in all government hospitals and health centers. This initiative nearly doubled the domestically financed expenditure on health care in 2010. The annual total cost for 2010–12 is estimated at 2.8 percent of GDP. About 40 percent of this reflects the costs of medicines and other expenses, which are currently funded outside of the budget by donors. Staff emphasized the importance of transparently showing the full medium-term cost of this initiative in the budget to ensure the sustainability of the initiative as donor support tapers off.

Box 1. Sierra Leone: Infrastructure Needs, 2010–13

The absence of basic infrastructure is a major obstacle to economic growth in Sierra Leone. The civil war destroyed most of the key transport system, power generation and distribution installations, and water pipelines. The government considers the achievements made since the end of the war as insufficient and it intends to accelerate investments in infrastructure in the coming years. To this end, the government has identified a number of priority projects to develop infrastructure for (i) roads, (ii) energy; and (iii) water and sanitation systems. So far, external donor contributions to infrastructure development have been relatively small. During 2008–10, donors provided US$301 million in project support, of which only US$36 million was intended for infrastructure development. For the same period, out of US$113 million domestically financed capital expenditures, the government spent US$68 million on infrastructure.

The government expects that closer cooperation with external donors, including nontraditional donors like the Islamic Development Bank, India, and China, will generate a stronger interest in supporting investments in infrastructure. For 2011-13, the government estimates an infrastructure need of US$1.4 billion, of which, based on current commitments, donors are projected to finance about US$176 million and the government US$161 million. This leaves a financing gap of about US$1.1 billion, or 15 percent of 2011–13 GDP (Table 1). The government expects that donors could provide an additional US$335 million. Furthermore, the plan is to attract private investors to construct and own the Bumbuna II hydropower station at an estimated cost of US$624 million. The remaining financing gap is US$96 million, which accounts for 1.4 percent of 2011–13 GDP. To finance this remaining gap, the government is considering two options: (i) increasing domestic revenues; and (ii) issuing long-term government bonds. However, the authorities are cognizant of the need to further develop the bond market in Sierra Leone before any significant amounts of long term-bonds could be issued at a reasonable financing cost. Therefore, the focus will need to be on domestic revenue mobilization.

The identified key infrastructure projects include:

Road projects: (i) reconstructing key roads connecting different regions of the country such as Makeni-Matotaka, Kenema-Koindu, Freetown- Conakry and the Port Loko-Lungi roads; and (ii) building rural roads and roads connecting rural areas with main inter-region roads.

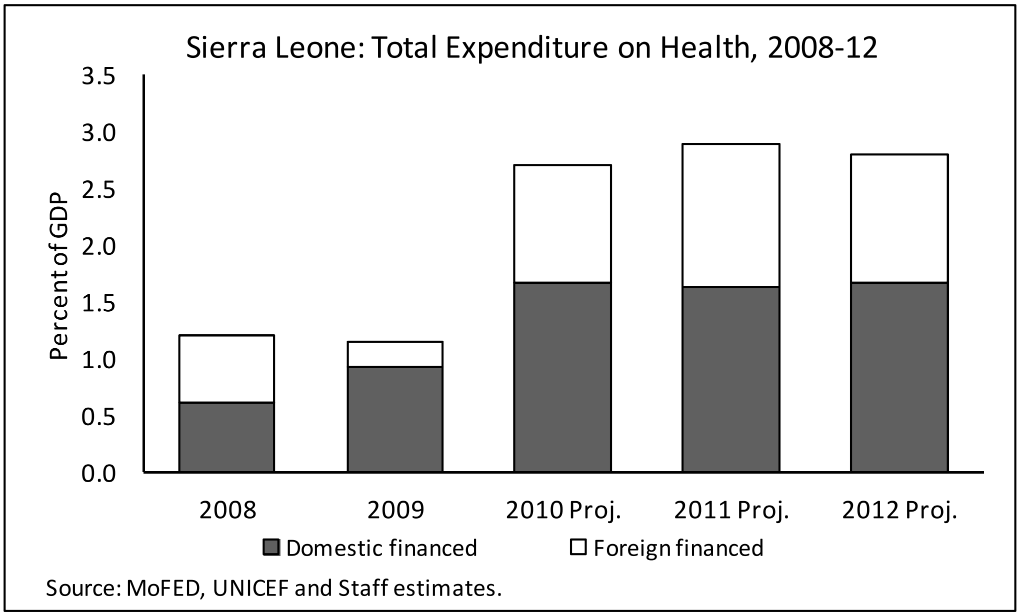
Energy projects: (i) Bumbuna II hydropower station; (ii) creating capacity for generation of renewable energy through mini-hydro dams and solar energy at the rural level; (iii) extending capacity of thermal power generation at Bo and Western Area; and (iv) expanding and rehabilitating of transmission and distribution networks across the country.

Water and sanitation projects: (i) rehabilitating water supply in key provincial and district headquarter towns such as Mile 91, Pujehun, Kabbala and Makeni; (ii) improving access to drinking water in Freetown especially through installation of sub-mains; (iii) constructing of boreholes in rural areas; and (iv) providing safe drinking water in government hospitals across the country.

Table 1. Sierra Leone: Financing for Infrastructure Developments, 2008–13

	2008–2010			2011–2013				Possible ways to close the gap		
	Total financed	Foreign financed	GoSL financed	Total financing need	Foreign financing	GoSL financing	Financing gap	Donor financing	FDI	Remaining gap
				(In percent of GDP)						
Roads	0.71	0.03	0.68	6.2	1.7	1.1	3.4	2.6	0.0	0.8
Energy	0.08	0.05	0.04	12.3	0.8	1.3	10.2	0.8	9.0	0.4
Of which: Bumbuna II	…	…	…	9.0	0.0	0.0	9.0	0.0	9.0	0.0
Water	1.03	0.55	0.48	1.5	0.0	0.0	1.5	1.4	0.0	0.1
Total	1.82	0.62	1.20	20.0	2.5	2.3	15.1	4.8	9.0	1.4

Source: GoSL and IMF staff estimates



6. **The authorities are conscious of the challenge to finance the envisaged increase in priority spending.** With an anticipated gradual reduction in external budget support, the authorities are considering issuing longer-term government bonds to fund an increase in infrastructure spending. Staff pointed out the need to carefully analyze the financing costs of issuing longer-term bonds because of the lack of depth of financial markets in Sierra Leone. Moreover, to maintain debt sustainability, there is no scope for increasing non-concessional borrowing beyond the domestic financing already envisaged in the medium-term fiscal framework. Given tight budget constraints and weak project implementation capacity, staff advised the authorities to select projects with the highest priority, contain nonpriority spending, and strengthen domestic revenue collections. While the authorities acknowledged the need to focus more on containing nonpriority spending, they were confident that tax revenue would rise in the future from newly signed iron ore mining projects.

B. Revenue Potential from Mining

7. **Efficiency gains from goods and services tax (GST) and other taxes notwithstanding, there is a need to find new avenues to raise revenue to generate sufficient fiscal space to implement the government's investment plans for infrastructure and social services.** While the implementation of the 6.5 percent royalty on diamonds and elimination of GST exemptions would help, a more significant revenue potential lies in the country's vast mining resources. The estimated mining potential, including recently signed agreements for iron ore mining, could raise total exports 10-fold while revenue from royalties alone could increase by about 6 percent of GDP (Box 2).

Box 2. Sierra Leone: Mining Exports and Revenue Potential

Although mining has been an important economic activity in Sierra Leone since the 1930s, a significant potential for extraction and export of minerals remains untapped. Key minerals are rutile, bauxite, diamonds (alluvial and hard-rock deposits), gold, and iron ore. Other minerals include lignite, clays, base metals (copper, nickel, molybdenum, lead, and zinc), chromite, and platinum. Before the conflict, the mining sector played a major role in economic activity: GDP (20%), exports (90%), and fiscal revenues (4%). The Mines and Minerals Act of 2009 is expected to contribute to restoring the sector as the main engine of economic growth.

The general geology suggests that endowments are abundant and that new exploration and development would open new mines under the right conditions. The basic information available on the mineral potential of Sierra Leone is very poor, and the geological data is incomplete and outdated. The World Bank (*Tapping the Mineral Wealth for Human Progress—A Break With the Past, 2005*) has estimated that successful realization of the large-scale mineral potential of the country in diamonds, gold, rutile, and bauxite, could result in the establishment of four new mines, in addition to reactivation of three existing mines. As a result, total annual mineral export revenues could top US$370 million.

While the mining of iron ore dates back to the 1930s, it was abandoned in the 1980s. But with renewed market interest in minerals, an existing mine is being restored by a foreign investor (Marampa, London Mining). In addition, new exploration has discovered 10.5 billion tons of iron ore deposits (Tonkolili, African Minerals). Annual production is conservatively estimated at 35 million tons annually in the medium term. Potentially, it could be as much as 45–75 million tons annually, if fully implemented over the next decade. Chinese investors have reportedly expressed interest in the project.

Preliminary geological investigations in the 1960s identified favorable conditions for hard-rock gold minerals. Potentially, the volume of gold production could increase from 6,000 to 300,000 oz under the right conditions. But more systematic exploration is needed to determine the extent of gold deposits.

Exports of major mineral deposits could range from US$370 million to US$3.3 billion annually in the next decade. This compares to mineral exports of US$203 million (total exports of US$341 million) in 2010 (Table 1). Revenue from royalties alone could range from US$16 million to US$114 million annually (assuming royalty rates of 6.5% on diamonds, 5% on gold, and 3% on other minerals) compared to US$3 million for the same commodities in 2010. Even at the lower end of this potential range, it would be a major contribution to exports and fiscal revenue, raising the low fiscal revenue-to-GDP ratio and lowering the high debt-to-exports ratio. New policy measures taken in 2010 increased the royalty rate on diamonds to 6.5 percent.

Table 1: Mining Potential in Sierra Leone

	Volume (000)			Value (US$ million)				Royalties (US$ m.)		
					potential				potential	
	current	potential	% change	current	lower	higher	% share	current	lower	higher
Rutile (tons)	71	330	367	33	139	154	5	0	4	5
Bauxite (tons)	646	2,500	287	31	65	120	4	1	2	4
Diamonds (cts)	481	692	44	132	77	190	6	2	5	12
Gold (oz)	6	300	5,072	7	90	362	11	0	5	18
Iron ore (tons)	0	35,000	…	0	…	2,499	75	…	…	75
Total				203	370	3,325	100	3	16	114
In percent of GDP (2010)				*10.7*	*19.4*	*174.5*		*0.1*	*0.8*	*6.0*
In percent of fiscal revenue								*1.2*	*6.3*	*45.9*
In percent of exports				*59.5*	*108.5*	*975.1*				

8. **Two mining lease agreements on iron ore, signed by the government earlier this year, could increase tax revenues significantly.** While staff previously had raised strong concerns about the extensive tax exemptions provided in the first agreement (ratified by parliament in early 2010), the fiscal regime in a second mining lease agreement ratified in August is more attractive for the government, despite containing some tax concessions. Staff reiterated its position that the fiscal framework defined in the current tax legislation and the new Mines and Minerals Act is appropriate and should be applied to all future mining investments. While the authorities argued that limited tax concessions were necessary to attract investors for the second project, they are committed to applying the existing fiscal regime in the future. The related revenue potential from royalties, income tax, and licenses could be substantial in the medium term. Estimates prepared by staff indicate that annual tax revenues from iron ore could reach 10–12 percent of GDP in 2014–15, if the projects are implemented as planned. Staff stressed that at this early stage, when uncertainties about timing and production amounts remain significant, it is important to manage expectations and contain spending until the revenue starts to be collected.

C. Competitiveness of the Economy

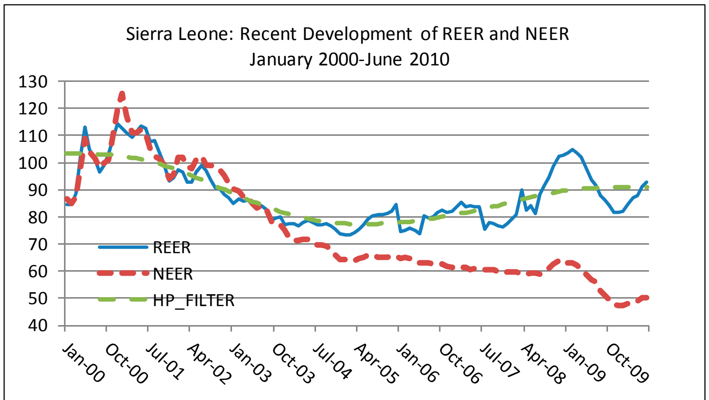
9. **Staff sees the value of the leone as broadly in line with fundamentals.** The mission discussed with the authorities the results of its analysis of external stability and structural competitiveness.

10. **The exchange rate assessment:** Sierra Leone's exchange rate regime is classified as floating, with the value of the leone determined by the market. The Bank of Sierra Leone (BSL) maintains a weekly foreign exchange auction, which is used mainly to sterilize domestic government spending financed by foreign grants and loans. The competitiveness of the leone was assessed using the three CGER approaches and an alternative approach based on monthly observations (Box 3). Despite sensitivity to methodological differences, none of the approaches used show significant exchange rate deviations from estimated equilibrium values at end-2009. The authorities welcomed the staff's assessment and agreed to maintain exchange rate flexibility to allow full adjustment to exogenous shocks.

11. **Structural competitiveness:** The World Bank's *Doing Business Report 2010* ranks Sierra Leone 148th out of 183 countries in the world, and 22nd among 46 Sub-Saharan African countries. Sierra Leone's world ranking improved from 160 in 2008 to 148 in 2010 as the economy underwent structural reforms. For example, business start-up has become easier with the establishment of a one-stop shop for business registration. In addition, tax administration has been simplified with better training and equipment at the tax authority, a consolidated income tax act, and a new value added tax that replaced seven existing indirect taxes. However, the authorities understand the need to further improve the business climate, especially by rationalizing tax administration, reducing bureaucracy, enforcing contracts and developing property rights.

Box 3. Sierra Leone: Exchange Rate Assessment

After depreciating in the first half of the 2000s, the real effective exchange rate (REER) has started to recover, though with significant fluctuations. More recently, the REER appreciated strongly at the onset of the global crisis in late 2008, mainly reflecting price compression among major European trading partners and a strong depreciation of the British pound. However, this trend reversed with the marked depreciation of the leone in 2009, resulting in a depreciation of the REER of about 30 percent from its peak in early 2009 to early 2010. This depreciation was caused mainly by a decline in export proceeds and transfers due to the second round effects of the global economic crisis.

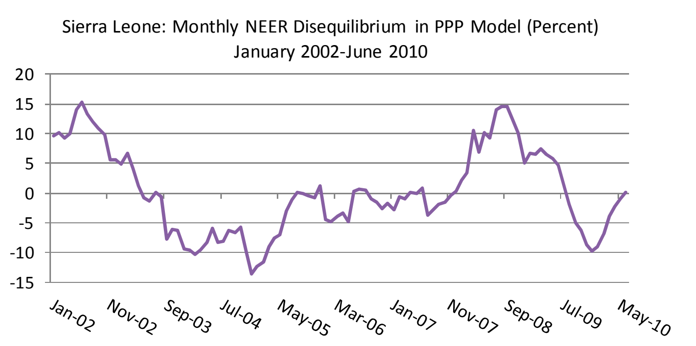


Sources: IMF, Information Notice System; and Fund staff estimates and projections.

Assessing the exchange rate with tools developed by the Consultative Group on Exchange Rates (CGER) indicates that the real effective exchange rate in 2009 was very close to its estimated equilibrium level and thus broadly aligned with macroeconomic fundamentals. Specifically, the exchange rate was within a range of less than 5 percent of the estimated equilibrium rate in 2009**.**

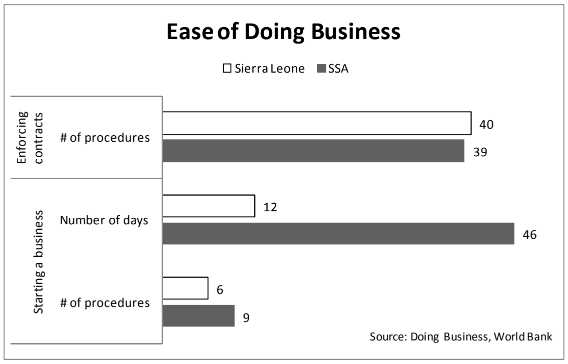
Methodology used	Assessment in 2009	REER over/under valuation
Macroeconomic Balance	No misalignment	+0.3 %
External Sustainability	Broadly in line	+3.3 %
Equ. real exchange rate	No misalignment	+1.1 %

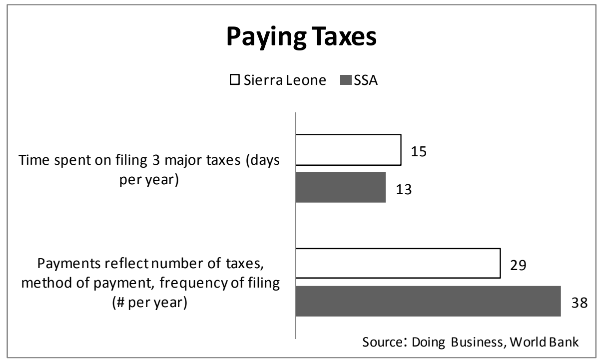
In addition to the standard CGER approaches, the relationship between the nominal effective exchange rate (NEER), the relative price between Sierra Leone and trading partners, and international oil prices has been analyzed using monthly data. By defining equilibrium according to this modified Purchasing Power Parity model, the exchange rate was found to be practically fully aligned with price fundamentals. While the variation around equilibrium has been quite volatile in recent years, the NEER was only 0.2 percent away from its equilibrium in June 2010.



Sources: IMF, Information Notice System; and Fund staff estimates.

It should be emphasized that data limitations, model selection, and structural changes in the economy severely limit the scope for precise point estimates of the equilibrium exchange rate in the context of a post-conflict country like Sierra Leone. This applies particularly to the two indirect CGER approaches that depend critically on estimating current account norms that are not well defined in post-conflict circumstances





12. **The multiple-price Dutch auction system applied by BSL gives rise to a multiple currency practice (MCP) subject to Fund jurisdiction.** The current auction system has been in operation before the start of the current ECF arrangement. Staff continues to work towards a resolution of this issue in the context of a more comprehensive review involving MCPs of this nature in a number of countries.

D. Debt Sustainability

13. **Sierra Leone's risk of debt distress remains moderate.**[1] Although the present value of external debt-to-export ratio remains close to the 100 percent threshold, external debt indicators are expected to remain below the DSA thresholds through 2030. Staff reiterated the need for continued prudent macroeconomic policies and reliance on grants and highly concessional resources to finance government operations. The authorities concurred and explained that the government is reaching out to a broader group of donors to seek concessional financing for development programs. Staff welcomed the authorities' resolve to strengthen debt management; they are in the process of adopting a new debt management law and are seeking technical assistance from the Bank and the Fund to develop a medium-term debt management strategy (MTDS). The dialogue with commercial creditors over debt relief is ongoing and the IDA Debt Reduction Facility is scheduled for implementation in 2011. The authorities are also pursuing negotiations with a few remaining official bilateral creditors in line with the enhanced HIPC Initiative.[2]

III. Recent Economic Developments and Program Performance

14. **While economic activity has shown signs of a pickup in 2010, inflation has remained high** (Figure 1 and Table 1).

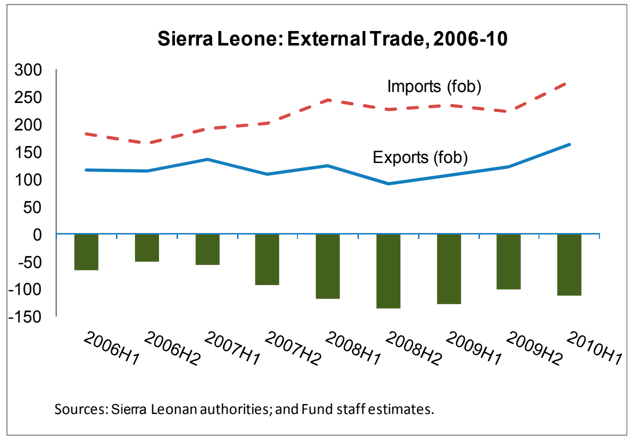
- Real GDP growth decelerated to 3.2 percent in 2009 owing to weak output in mining and manufacturing. However, economic activity appears to have picked up in 2010,

[1] Debt Sustainability Analysis (DSA) 2010, www.imf.org.

[2] Agreements on the delivery of the HIPC relief are still pending with China, Kuwait, and Saudi Arabia.

reflected by marked growth in the services sector, buoyant agricultural production, and a rebound in exports. While lower fuel and domestic food prices eased inflationary pressures during most of 2009, inflation jumped by about 7 percent in the first two months of 2010 due to the introduction of the GST and higher domestic fuel prices. However, seasonally adjusted monthly inflation rates have stabilized since then, and inflation was 18.5 percent in the 12 months through September, but it is expected to decline to 16 percent by year-end.

- The external current account deficit declined to 8.4 percent of GDP in 2009 from 11.5 percent of GDP in 2008. While exports were basically flat in 2009, imports declined, reflecting weaker economic growth and lower oil prices. However, exports picked up in 2010 because of higher diamond export volumes and prices. Despite BSL interventions to support the leone in 2009, gross international reserves increased to 6.1 months of imports at end-2009, reflecting the SDR allocation in 2009. Gross reserves declined to 5.2 months of imports at end-June 2010 because of a recovery of imports and temporary delays in external budget support.

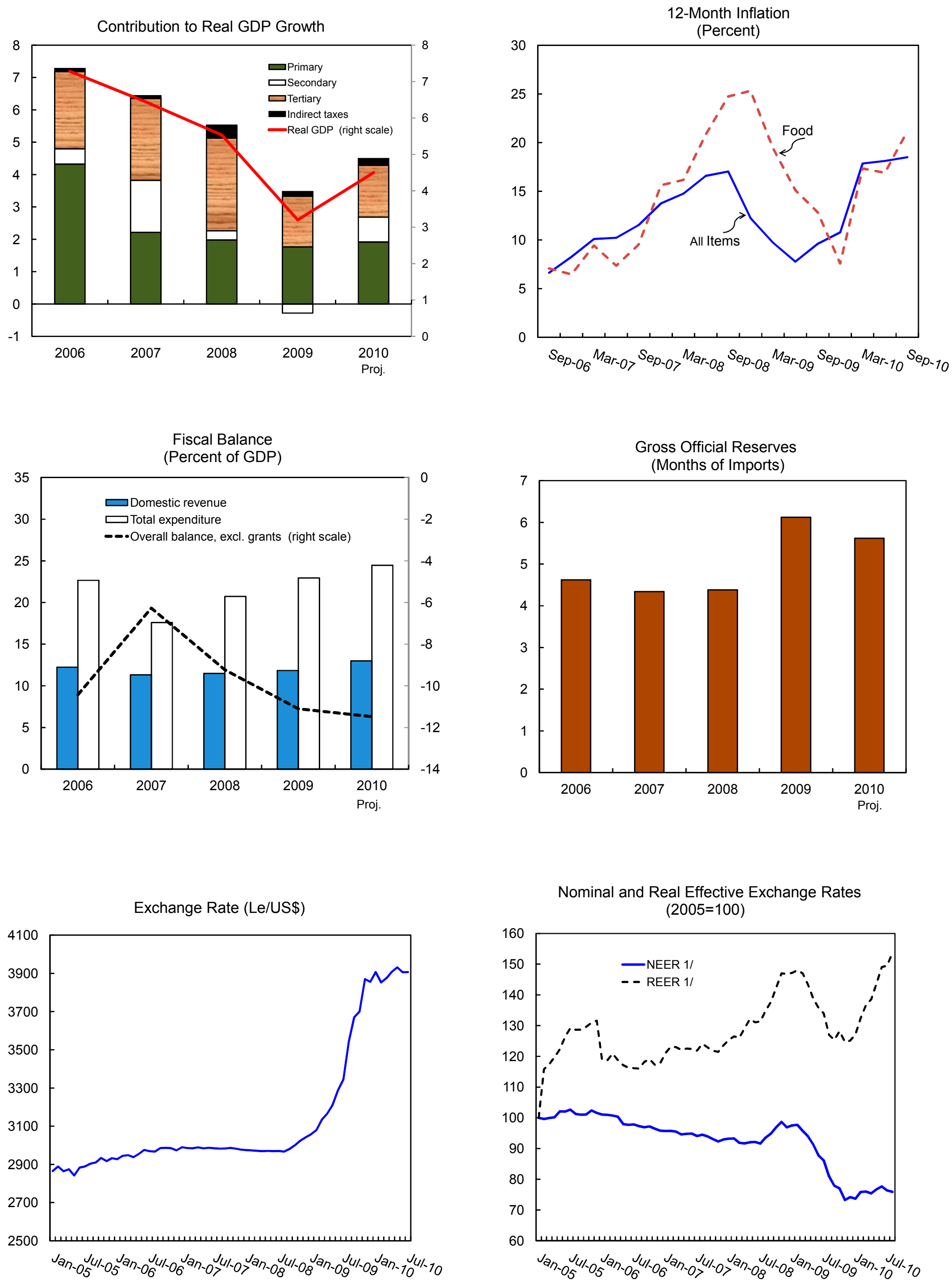


- The exchange rate stabilized in the first half of 2010 after a depreciation of about 28 percent in 2009. The BSL continued to supply foreign currency to the market through foreign exchange auctions, although the offered amount decreased from US$2 million per week in January to less than US$1 million per week in September, reflecting reduced pressures in the market.

15. **Fiscal policy performance during the first half of 2010 was broadly satisfactory (Tables 2 and 3).** The overall deficit, excluding grants, was 6.1 percent of GDP, compared to 6.3 percent of GDP in the program. Revenue collections were above the target and current spending was close to the program, but the wage bill was higher owing to hiring in the health sector. Capital expenditures were below program because of shortfalls in external project support, while domestically financed capital spending was higher than envisaged.

16. **In the first two months of the third quarter of the year, however, budgetary spending accelerated.** Despite continued improvement in revenue collections, this caused an unexpected deterioration in the fiscal position. The increase in spending was spread across many items, including wages for hiring another 3,000 health care staff to implement the FHCI, increased compensation to military families, higher than anticipated debt service payments, keeping the emergency power project beyond June, and payments to complete important road projects. In addition, arrears to oil marketing companies (0.3 percent of GDP) were cleared. The increased financing need in July and August was covered mostly by drawing on overdrafts in the BSL amounting to 1.2 percent of GDP.

Figure 1. Sierra Leone: Selected Macroeconomic Indicators, 2006-10
(Percent changes, unless indicated otherwise)



Sources: Sierra Leonean authorities; and IMF estimates and projections.
1/ Alternative calculation with weights based on economic importance of the three main currencies (USD, EUR, and GBP).

17. **Monetary policy remained tight through the third quarter of 2010.** As envisaged in the program, the BSL managed to halt the monetary expansion that took place toward the end of 2009. As a result, reserve and broad money grew only about 3 and 5½ percent, respectively, in the first half of 2010 (Table 4). Despite the slowdown in money growth, credit to the private sector expanded by about 40 percent in the 12 months through June. Following a significant improvement in the quality of banks' loan portfolios in the last few years, the ratio of nonperforming loans to gross loans increased to 13.6 percent in June 2010 from 10.6 in December 2009 (Table 9). Notwithstanding the significant direct credits from the BSL to the Government in the third quarter of the year, reserve money was contained in line with the program. The BSL sold a substantial amount of its holdings of treasury securities to the commercial banks to absorb the liquidity created by the fiscal expansion. As a result, interest rates on treasury bills increased by 400 basis points in the third quarter to about 18 percent.

18. **Program performance was satisfactory in the first half of 2010.** All quantitative performance criteria for end-June 2010 were met (MEFP Table 1). The two structural benchmarks for end-June (implementing an automatic fuel pricing mechanism and adopting new off-site surveillance guidelines) were implemented but with a delay (MEFP Table 2). Similarly, two of the three structural benchmarks for September were implemented with a slight delay: the commissioner and the deputy commissioner were hired for the Domestic Tax Department (DTD); and amendments to the Government Budget and Accountability Act and the Financial Management Regulation were submitted to the parliament to ensure that only viable capital projects enter into the budget.

IV. Program Issues

19. **Consistent with the Agenda for Change, the key program objective is to raise growth by increasing investments in infrastructure and developing the private sector.** In order to achieve this objective, the focus will remain on (i) creating fiscal space for improving basic infrastructure and social services while maintaining macroeconomic stability; (ii) strengthening tax performance and improving public financial management (PFM) systems; and (iii) developing the financial sector by making it more accessible and strengthening BSL independence and supervisory role.

A. Policies for the Remainder of 2010

20. **Budget expenditures for 2010 are projected to be 1.2 percent of GDP higher than programmed, partly financed by higher revenue collections**. Spending is projected to increase in the second half of the year due to additional needs to implement the national development priorities: hiring an additional 3,000 health care workers under the FHCI, maintaining an emergency power project, and investing in additional infrastructure, particularly roads. Moreover, foreign interest payments are projected to increase owing to exchange rate changes. On the financing side, payments for clearing arrears to oil marketing companies are projected to exceed the program by 0.3 percent of GDP stemming from unpaid

subsidies accumulated because of delays in implementing a new automatic domestic fuel pricing framework. On the revenue side, the GST is continuing to exceed expectations; therefore, for the year as a whole, domestic revenue has been revised up by 0.6 percent of GDP. As a result, the overall fiscal deficit, excluding grants, is projected to increase to 11.5 percent of GDP, compared to 10.8 percent of GDP in the program. On this basis, there is a need to revise the program target for net domestic bank financing from 2.4 percent of GDP to 3.3 percent of GDP in 2010. In the event that domestic revenue exceeds the revised projection for 2010, the authorities have agreed to reduce net domestic bank financing correspondingly (MEFP ¶10).

21. **While recognizing the tremendous needs of the country, staff stressed the importance of maintaining budget discipline and limiting the use of overdrafts in the BSL.** Staff raised concerns about the significant use of overdrafts in the BSL to finance the fiscal expansion in the third quarter of 2010.[3] The use of direct financing from the BSL, except for smoothing purposes, to finance government spending hinders liquidity management and the overall objectives of monetary policy. Looking forward, the authorities committed to strengthening budget discipline, increasing revenue collection, containing nonpriority expenditures, and reducing overdrafts with the BSL. To this end, the authorities (i) made the increase in diamond royalties to 6.5 percent effective in November 2010; (ii) implemented, by end-October 2010, a new automatic domestic fuel price framework that will eliminate existing subsidies within a few months; and (iii) reduced government overdrafts with the BSL by about Le 30 billion (0.4 percent of GDP) in early November 2010, and committed to amending the BSL Act to limit direct BSL credit to the government, including overdrafts, to 5 percent of the previous year's domestic revenues (MEFP ¶29).

22. **Monetary policy will seek to contain inflationary pressures from the introduction of the GST and the fiscal expansion.** The monetary program has been maintained as envisaged in the program. Reserve money growth is targeted at 7.5 percent in 2010 to keep inflation below 16 percent by end-2010. The BSL will stand ready to tighten monetary policy further, should inflationary pressures increase. With a stable leone against the US dollar, the amount offered in the foreign exchange auction will remain at a reduced level for the rest of 2010. The program end-December targets for net domestic assets and gross international reserves have been maintained.

23. **On the structural program,** the two benchmarks for end-December 2010—establishing a credit reference bureau and integrating the GST administration within the Large Taxpayer Office—are on schedule to be met (MEFP Table 3).

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[3] BSL overdrafts or "ways and means" increased to about 2.5 percent of GDP in the third quarter. Note that "ways and means" are only used as within-budget-year financing and any outstanding amounts need to be settled within 90 days after the end of the fiscal year. In the past, outstanding amounts, generally below 1 percent of GDP, have been repaid by issuing treasury bills to the BSL.

B. Policies for 2011

24. **The macroeconomic outlook is positive for 2011.** The economy is expected to grow by 5.2 percent, while inflation should return to single-digits. This will be supported by an increase in public investment and a monetary policy aimed at achieving single digit inflation and maintaining a flexible exchange rate.

Fiscal policy

25. **Fiscal policy in 2011 is to boost infrastructure investment to support sustained economic growth.** The authorities are preparing the 2011 budget that envisages higher domestic revenue and a significant increase in capital spending, mainly financed by external grants or concessional loans (MEFP ¶16–19). Fiscal policy will be anchored by keeping domestic financing from banks and nonbank financial institutions close to 2 percent of GDP.

26. **The authorities are focused on raising revenues.** Domestic revenue is projected to increase to 13.3 percent of GDP from 13 percent of GDP in 2010, reflecting an increase in diamond royalties to 6.5 percent, continued efficiency gains from GST, and benefits from tax administration reforms. Although royalties could begin to be collected from the new iron ore mining projects, the authorities have prudently incorporated only the annual license fees into the budget projection for 2011. Grants remain at 6.8 percent of GDP as the anticipated decrease in budget support by 0.9 percent is offset by an increase in project grants. Privatization proceeds are projected to yield an additional 0.6 percent of GDP.

27. **On the expenditure side, the authorities foresee a shift from current to capital spending.** To build basic infrastructure, capital spending is projected to increase by 1.8 percentage points of GDP to 10.2 percent of GDP in 2011, mostly financed by external project grants and concessional project loans. Current expenditures are envisaged to decline, reflecting containment of non-priority spending on goods and services, and savings arising from the termination of the emergency power project.[4] However, spending for preparations of the 2012 elections will partially offset these savings. The wage bill assumes a 15 percent increase in basic salaries and includes the full year effect of the new hiring in the health sector.

28. **Domestic bank financing will decline in 2011, while external project financing and privatization proceeds will increase.** The overall fiscal deficit, excluding grants, is projected to increase to 12.5 percent of GDP from 11.5 percent of GDP in 2010. Net domestic financing from banks and nonbank financial institutions is projected to decline to 2.3 percent of GDP in 2011 from 3.5 percent of GDP in 2010. The decline in domestic bank financing and the switch

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[4] Budgeted spending on goods and services is 0.3 percentage points of GDP below the budget for 2010 (excluding the emergency power project). This saving reflects lower allocations for travel, vehicles, office equipment, and other nonpriority goods and services.

from current to capital spending will support private sector development and help achieve lower inflation in 2011.

Monetary and exchange rate policies

29. **Monetary policy will aim to achieve single digit inflation by the end of 2011.** Continued tight monetary policy, combined with the reduction in annual inflation because of a base effect stemming from the 7 percent price jump in January-February 2010, is projected to achieve a significant reduction in inflation in 2011. Reserve money is envisaged to grow by 14 percent and broad money by 20 percent; this should accommodate a 31 percent growth in private credit. With constrained government access to direct credit from the BSL and active use of the repo and reserve repo instruments, liquidity management is expected to improve.

30. **The authorities are committed to maintaining a flexible exchange rate to facilitate adjustment to external shocks.** The BSL will limit its foreign currency sales to absorbing foreign-financed budget spending and smoothing short-term market volatility (MEFP ¶21). With a rebound in exports and prudent macro policy, the volume of BSL's foreign exchange auctions is expected to remain low in 2011.

Financing assurances

31. **The government is making good faith efforts to resolve external arrears to commercial creditors;** those are estimated at US$240 million at end-2009. The authorities continue to engage creditors and have made goodwill payments to avoid litigation. They secured a grant to fund the preparatory work for an IDA debt-buy-back program. Once implemented, possibly as early as end-2011, external commercial debt could be reduced by over 90 percent. Government policy is that no creditor will be exempted from participating in the program. Ongoing efforts to resolve these arrears provide sufficient financing assurances for the Fund-supported program.

Structural reforms

32. **The authorities are committed to stepping up structural reforms to complement the scaling up of public investment and providing for other development priorities.** Reforms will focus on

- **Improving tax administration:** To reduce inefficiencies arising from separate tax departments and to enhance tax compliance, the National Revenue Authority (NRA) will integrate GST operations with the Large Taxpayer Office (LTO) and Medium Taxpayer Office (MTO). In addition, the NRA will step up efforts to improve tax compliance by implementing a small taxpayer regime and applying penalties for noncompliance (MEFP ¶23–24).

- **Strengthening PFM:** The authorities aim to strengthen the Medium Term Expenditure Framework (MTEF) by enhancing the planning, monitoring and evaluation process for capital projects. They also plan to improve the quality of the workforce in the public sector by implementing a multiyear pay reform. Budget execution will continue to be strengthened by the rolling out of IFMIS to ministries, departments and agencies (MEFP ¶25–27).

- **Strengthening the financial sector:** The BSL will enhance the conduct of its monetary policy by establishing a benchmark interest rate. The independence of the BSL will be strengthened, as will its supervisory role in reducing vulnerabilities (with the adoption of new off-site surveillance guidelines for banks). The BSL will also limit its direct credit to the government, which will foster the development of bond markets. Access to credit will be enhanced by establishing a credit reference bureau and strengthening the payments and settlements system. In addition, the Anti-Money Laundering (AML) Act 2005 has been revised to include provisions for combating the financing of terrorism (CFT); these are to be submitted to the parliament by the end of the year (MEFP ¶28–33).

V. Program Risks

33. **There are risks to budget implementation in the short and medium term.** The pressure to increase wages outside of the health care sector continues and the budget cost of the FHCI could be higher than envisaged if donor support does not come through as projected. The budget will be strained further if revenue collections from higher royalties on diamonds do not materialize, while the authorities have committed to large infrastructure projects. To reduce these fiscal risks, a timely implementation of the public service pay reform will be important. In addition, efforts are required to improve tax performance through reforming tax administration and eliminating discretionary tax incentives. In the medium term, tax revenue from mining may be lower than anticipated if the new mining projects do not fully materialize.

34. **Sierra Leone has adequate capacity to meet its financial obligations to the Fund**. The country has established a record of timely servicing its obligations to the Fund, and the DSA places Sierra Leone at a moderate risk of debt distress (Table 6). Debt service to the Fund would remain modest in absolute terms, and below 1.5 percent of exports of goods and services throughout the program period.

VI. Ex Post Assessment

35. **As Sierra Leone is a member with a longer-term program engagement with the Fund, an Ex Post Assessment (EPA) update has been circulated to the Executive Board (**www.imf.org). The EPA focused on program objectives and design, as well as key lessons from the experience. The update found that the authorities and donors agree that the Fund has been an essential advisor on macroeconomic policy. Key EPA recommendations include

continued focus on strengthening capacity through technical assistance, setting ambitious but realistic revenue targets, formulating structural benchmarks that are of macro-critical importance, and fostering better coordination among the authorities, donors and the Fund to conduct a more forward-looking discussion of the macroeconomic framework for the following fiscal year, thus reinforcing the budget preparation process.

VII. Staff Appraisal

36. **After a period of economic slowdown, the outlook for Sierra Leone appears more favorable.** Growth is expected to pick up due to strong growth in the services sector and buoyant agricultural production. However, inflation is projected to remain in double digits this year owing to the introduction of the GST, but it is expected to decline to single digits in 2011.

37. **A key constraint to economic growth in the medium term is the lack of basic infrastructure.** While sustained strong growth is a necessary condition to achieve a significant reduction in poverty, a challenge for the authorities in the coming years will be to strike the right balance between spending on basic infrastructure and on social services. Staff welcomes the authorities' current effort to accelerate infrastructure investments and encourages donors to expand their support.

38. **A sustainable fiscal policy is critical for macroeconomic stability.** Mobilizing more domestic revenues and containing nonpriority spending will continue to create fiscal space for investments in infrastructure and human resources. Staff is thus encouraged by the authorities' resolve to raise royalties on diamond production, strengthen tax administration, and eliminate all subsidies on domestic fuel prices. On the spending side, it is important to contain the wage bill by raising compensation to public servants to more competitive levels only in the context of a multiyear pay reform.

39. **Staff welcomes the authorities' commitment to fully apply the fiscal regime for mining in accordance with the Mines and Minerals Act and current tax legislation.** While the fiscal regime in a recent mining lease agreement for iron ore represents an improvement compared to agreements signed in the past, in staff's view no tax incentives were needed to make the project economically attractive. Notwithstanding these tax concessions, the medium-term revenue potential from this mining agreement could be significant. However, in view of the uncertainty about the exact amounts and timing, staff recommends that new spending decisions should not be made before the increase in revenue materializes.

40. **The fiscal expansion in the second half of 2010 has created a challenge for monetary policy.** Staff welcomes BSL's steadfastness to neutralize the liquidity effect of this expansion by significantly stepping up its open market operations. Staff also supports the BSL's commitment to reduce inflation to single digits in 2011 and to establish a benchmark monetary policy interest rate. The BSL should continue to enhance banking supervision and closely monitor developments of nonperforming loans.

41. **There are no concerns about competitiveness and external stability at present.** Staff calculations show that the leone is broadly aligned with its fundamentals. The authorities are encouraged to maintain exchange rate flexibility to allow adjustment to exogenous shocks.

42. **The DSA for Sierra Leone shows limited room for additional borrowing**. Staff recommends that the authorities rely on grants and highly concessional loans for financing their development program. The authorities' resolve to strengthen debt management is welcomed.

43. **Staff supports the authorities' commitment to accelerate structural reforms**. The focus on improving tax administration, strengthening public financial management, and deepening the financial sector is appropriate. The first two reform areas will help create fiscal space for capital and social spending while the latter complements these efforts by encouraging private sector investment and activity.

44. **Staff supports the authorities' request to modify the target on net domestic bank credit to the government,** given the measures taken by the authorities to improve revenue collection, constrain nonpriority spending, and reduce the government's access to overdrafts with the BSL, as well as the authorities' commitment to a 2011 budget consistent with macroeconomic and fiscal sustainability. Staff recommends completion of the first ECF review and the financing assurances review.

45. Staff recommends that the next Article IV consultation take place in accordance with the 2010 Decision on consultation cycles.

Table 1. Sierra Leone: Selected Economic Indicators

	2008	2009	2010 Prog.	2010 Proj	2011 Proj	2012 Proj	2013 Proj	2014 Proj
	(Annual percentage change, unless otherwise indicated)							
National account and prices								
GDP at constant prices	5.5	3.2	4.8	4.5	5.2	6.0	6.0	6.0
GDP deflator	11.1	5.3	13.3	15.0	8.5	7.3	6.3	6.0
GDP at market prices	5,826	6,330	7,605	7,605	8,678	9,874	11,125	12,496
(in billions of local currency)								
Consumer prices (end-of-period)	12.2	10.8	12.5	16.0	9.5	8.0	7.5	7.0
Consumer prices (average)	14.8	9.2	15.5	17.6	9.1	8.7	7.7	7.2
External sector								
Terms of trade (deterioration -)	-2.3	-10.5	5.7	3.6	3.2	2.0	0.6	0.9
Exports of goods (US$)	-3.0	-1.0	25.9	25.7	15.4	13.2	11.7	10.2
Imports of goods (US$)	24.8	-2.6	14.7	18.0	8.6	11.1	-9.1	-8.6
Average exchange rate	2,985	3,410	…	…	…	…	…	…
(local currency per U.S. dollar)								
Nominal exchange rate change (depreciation -)	-2.2	-26.7	…	…	…	…	…	…
Real effective exchange rate (depreciation -)	-11.6	-3.2	…	…	…	…	…	…
Gross international reserves, months of imports	4.4	6.1	5.7	5.6	4.9	4.6	4.3	4.1
Money and credit								
Domestic credit to the private sector	56.8	45.4	32.2	26.1	31.4	18.3	16.5	17.0
Base money	9.6	19.3	8.0	8.0	14.4	15.8	14.7	14.5
M2	30.4	28.1	15.2	11.8	20.5	17.7	18.6	15.7
91-day treasury bill rate (in percent) 1/	9.1	14.0	...	18.1	...	...	...	...
	(Percent of GDP, unless otherwise indicated)							
National accounts								
Gross capital formation	14.8	14.9	16.1	16.3	18.9	19.4	19.0	19.3
Government	6.2	7.1	8.1	8.4	10.2	10.2	9.3	9.3
Private	8.6	7.8	7.9	7.9	8.7	9.2	9.7	10.0
National savings	3.3	6.6	7.1	6.8	9.4	9.9	9.7	10.1
External sector								
Current account balance								
(including official grants)	-11.5	-8.4	-9.0	-9.5	-9.5	-9.5	-9.3	-9.2
(excluding official grants)	-15.4	-12.8	-12.7	-12.9	-11.6	-11.3	-10.9	-10.6
External public debt (including IMF)	31.2	36.1	33.8	39.8	28.1	29.2	30.1	30.5
Central government budget								
Overall balance	-4.7	-3.2	-3.9	-4.7	-5.7	-5.0	-4.4	-4.4
(excluding grants)	-9.2	-11.1	-10.8	-11.5	-12.5	-10.6	-9.5	-9.4
Revenue	11.5	11.8	12.4	13.0	13.3	14.3	14.4	14.5
Grants	4.5	7.9	7.0	6.8	6.8	5.6	5.0	5.0
Total expenditure and net lending	20.7	22.9	23.3	24.5	25.8	24.9	23.9	23.9

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.
1/ For 2010 data is for September.

Table 2. Sierra Leone: Fiscal Operations of the Central Government
(In billions of leone)

			June, 2010		2010 Full year		2011	2012
	2008	2009	Prog.	Act.	Prog.	Proj.	Proj.	Proj.
Total revenue and grants	934	1,250	662	634	1,475	1,505	1,748	1,963
Revenue	670	749	433	438	946	988	1,157	1,412
Tax	589	660	477	493	839	878	1,033	1,271
Personal Income Tax	110	122	66	65	148	148	175	203
Corporate Income Tax	62	61	38	37	76	76	88	103
Goods and Services Tax	…	…	92	108	197	250	299	404
Imports sales tax 1/	123	129	71	82	…	…	…	…
Domestic sales tax 1/	14	11	21	26	…	…	…	…
Excises	70	107	66	63	137	137	147	162
Import duties	161	170	100	84	216	204	229	285
Mining royalties and license	19	20	9	8	41	31	65	79
Others	31	40	13	20	25	32	30	35
Of which: Five indirect taxes 1/	24	29	…	…	…	…	…	…
Non-tax	80	89	48	54	107	110	124	141
Grants	265	500	229	196	529	517	591	550
Budget support	115	290	118	60	283	265	179	179
Debt relief	28	25	2	29	14	20	20	21
Project grants	121	186	109	108	232	232	392	351
Expenditures and net lending	1,207	1,452	914	900	1,770	1,861	2,240	2,456
Current expenditures	848	1,000	570	573	1,151	1,219	1,356	1,448
Wages and salaries	334	402	237	245	506	515	566	645
Goods and services	285	350	198	179	339	366	359	406
Of which : Emergency Power Project	83	59	282	275	11	31	0	0
Subsidies and transfer	109	145	84	96	170	186	258	216
Of which : Foreign-financed transfers for elections	…	…	…	…	…	…	44	…
Interest	120	103	51	53	136	152	172	182
Domestic	109	89	44	46	117	135	151	160
Foreign	12	14	7	7	19	16	22	22
Capital expenditure	359	452	344	327	619	642	884	1,007
Foreign financed	284	345	196	164	418	418	652	701
Domestic financed	75	107	148	162	202	224	232	306
Net lending	0	0	0	0	0	0	0	0
Overall balance								
Including grants	-273	-202	-252	-266	-295	-356	-492	-493
Excluding grants	-538	-703	-481	-462	-824	-873	-1,083	-1,043
Financing	273	202	252	266	295	356	492	493
External financing (net)	143	155	63	54	162	175	271	333
Borrowing	163	198	87	84	213	237	345	380
Project	163	160	87	57	185	185	304	351
Budget	0	39	0	27	28	52	41	29
Amortization	-20	-43	-24	-29	-51	-62	-74	-46
Domestic financing (net)	158	47	186	198	133	181	221	157
Bank	218	109	192	221	180	250	152	144
Central bank	120	163	149	178	157	227	113	127
Commercial banks	98	-54	43	42	23	23	39	17
Nonbank	-60	-62	-5	-23	-47	-69	69	13
Non bank financial institutions	-34	-25	54	16	18	18	43	43
Privatization proceeds	4	10	0	0	8	8	49	0
Change in arrears	-46	-59	-26	-55	-74	-95	-24	-30
Floats (checks payable & outstanding commitments)	16	12	-33	16	0	0	0	0
Errors and omissions/financing gap	-28	1	3	14	0	-1	0	3
Memorandum item:								
Total poverty expenditures	330	362	252	294	417	417	476	541
Domestic primary balance, including grants	-133	-254	-234	-244	-270	-304	-259	-161
Public domestic debt	1,280	1,244	…	… …	…	1,425	1,646	1,803

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.
1/ Replaced by GST on January 1, 2010.

Table 3. Sierra Leone: Fiscal Operations of the Central Government
(In percent of GDP)

			June, 2010		2010 Full year		2011	2012
	2008	2009	Prog.	Act.	Prog.	Proj.	Proj.	Proj.
Total revenue and grants	16.0	19.7	8.7	8.3	19.4	19.8	20.1	19.9
Revenue	11.5	11.8	5.7	5.8	12.4	13.0	13.3	14.3
Tax	10.1	10.4	6.3	6.5	11.0	11.5	11.9	12.9
Personal Income Tax	1.9	1.9	0.9	0.9	1.9	1.9	2.0	2.1
Corporate Income Tax	1.1	1.0	0.5	0.5	1.0	1.0	1.0	1.0
Goods and Services Tax	…	…	1.2	1.4	2.6	3.3	3.4	4.1
Imports sales tax 1/	2.1	2.0	0.9	1.1	…	…	…	…
Domestic sales tax 1/	0.2	0.2	0.3	0.3	…	…	…	…
Excises	1.2	1.7	0.9	0.8	1.8	1.8	1.7	1.6
Import duties	2.8	2.7	1.3	1.1	2.8	2.7	2.6	2.9
Mining royalties and license	0.3	0.3	0.1	0.1	0.5	0.4	0.7	0.8
Others	0.5	0.6	0.2	0.3	0.3	0.4	0.3	0.4
Of which: Five indirect taxes 1/	0.4	0.5	…	…	…	…	…	…
Non-tax	1.4	1.4	0.6	0.7	1.4	1.4	1.4	1.4
Grants	4.5	7.9	3.0	2.6	7.0	6.8	6.8	5.6
Budget support	2.0	4.6	1.6	0.8	3.7	3.5	2.1	1.8
Debt relief	0.5	0.4	0.0	0.4	0.2	0.3	0.2	0.2
Project grants	2.1	2.9	1.4	1.4	3.1	3.1	4.5	3.5
Expenditures and net lending	20.7	22.9	12.0	11.8	23.3	24.5	25.8	24.9
Current expenditures	14.6	15.8	7.5	7.5	15.1	16.0	15.6	14.7
Wages and salaries	5.7	6.3	3.1	3.2	6.6	6.8	6.5	6.5
Goods and services	4.9	5.5	2.6	2.4	4.5	4.8	4.1	4.1
Of which: Emergency Power Project	1.4	0.9	3.7	3.6	0.1	0.4	0.0	0.0
Subsidies and transfer	1.9	2.3	1.1	1.3	2.2	2.4	3.0	2.2
Of which: Foreign-financed transfers for elections	…	…	…	…	…	…	0.5	…
Interest	2.1	1.6	0.7	0.7	1.8	2.0	2.0	1.8
Domestic	1.9	1.4	0.6	0.6	1.5	1.8	1.7	1.6
Foreign	0.2	0.2	0.1	0.1	0.3	0.2	0.2	0.2
Capital expenditure	6.2	7.1	4.5	4.3	8.1	8.4	10.2	10.2
Foreign financed	4.9	5.5	2.6	2.2	5.5	5.5	7.5	7.1
Domestic financed	1.3	1.7	1.9	2.1	2.7	2.9	2.7	3.1
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance								
Including grants	-4.7	-3.2	-3.3	-3.5	-3.9	-4.7	-5.7	-5.0
Excluding grants	-9.2	-11.1	-6.3	-6.1	-10.8	-11.5	-12.5	-10.6
Financing	4.7	3.2	3.3	3.5	3.9	4.7	5.7	5.0
External financing (net)	2.5	2.4	0.8	0.7	2.1	2.3	3.1	3.4
Borrowing	2.8	3.1	1.1	1.1	2.8	3.1	4.0	3.8
Project	2.8	2.5	1.1	0.7	2.4	2.4	3.5	3.5
Budget	0.0	0.6	0.0	0.4	0.4	0.7	0.5	0.3
Amortization	-0.3	-0.7	-0.3	-0.4	-0.7	-0.8	-0.9	-0.5
Domestic financing (net)	2.7	0.7	2.4	2.6	1.7	2.4	2.5	1.6
Bank	3.7	1.7	2.5	2.9	2.4	3.3	1.8	1.5
Central bank	2.1	2.6	2.0	2.3	2.1	3.0	1.3	1.3
Commercial banks	1.7	-0.9	0.6	0.6	0.3	0.3	0.4	0.2
Nonbank	-1.0	-1.0	-0.1	-0.3	-0.6	-0.9	0.8	0.1
Non bank financial institutions	-0.6	-0.4	0.7	0.2	0.2	0.2	0.5	0.4
Privatization proceeds	0.1	0.2	0.0	0.0	0.1	0.1	0.6	0.0
Change in arrears	-0.8	-0.9	-0.3	-0.7	-1.0	-1.3	-0.3	-0.3
Floats (checks payable & outstanding commitments	0.3	0.2	-0.4	0.2	0.0	0.0	0.0	0.0
Discrepancy/financing gap	-0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:								
Total poverty expenditures	5.7	5.7	3.3	3.9	5.5	5.5	5.5	5.5
Domestic primary balance, including grants	-2.3	-4.0	-3.1	-3.2	-3.6	-4.0	-3.0	-1.6
Public domestic debt	22.0	19.7	…	… .	…	18.7	19.0	18.3
Nominal GDP (in billions of local currency)	5,826	6,330	7,605	7,605	7,605	7,605	8,678	9,874

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.
1/ Replaced by GST on January 1, 2010.

Table 4. Sierra Leone: Monetary Accounts 1/

(In billions of leone; unless otherwise indicated)

	2008	2009	2010						2011
			Mar.	June		Sept.	Dec.		
			Act.	Prog.	Act.	Prog.	Prog.	Proj.	Proj.
				I. Monetary Survey					
Net foreign assets	832	1,542	1,447	1,388	1,345	1,359	1,370	1,371	1,398
Net domestic assets	599	335	424	673	665	790	866	775	1,174
Domestic Credit	967	1,280	1,357	1,536	1,587	1,634	1,727	1,752	2,099
Claims on central government (net)	536	647	680	847	854	894	828	898	1,050
Claims on other public sector 2/	17	31	35	36	41	36	36	53	53
Claims on private sector	413	601	643	653	693	704	794	758	996
Other items (net) 3/	-397	-980	-968	-907	-964	-888	-927	-977	-968
Money and quasi-money (M3)	1,431	1,877	1,870	2,061	2,009	2,149	2,237	2,146	2,572
Broad money (M2)	1,124	1,439	1,409	1,597	1,520	1,665	1,733	1,608	1,938
Foreign exchange deposits	307	437	461	464	490	484	504	537	634
				II. Bank of Sierra Leone					
Net foreign assets	479	1,005	905	832	834	804	815	815	743
Net domestic assets	-7	-442	-341	-244	-250	-207	-207	-207	-48
Claims on other depository corporations	4	6	14	6	-10	6	6	1	18
Claims on central government (net)	144	287	334	444	446	476	470	498	611
Claims on other public sector 2/	0	0	0	0	0	0	0	0	0
Claims on private sector	7	7	12	9	9	9	9	8	8
Other items (net) 3/	-167	-747	-705	-721	-699	-715	-710	-719	-685
Reserve money	472	563	565	589	584	597	608	608	695
Currency in circulation	383	486	469	434	468	436	465	498	556
Commercial bank deposits	89	77	96	155	116	161	143	109	139
Memorandum items:				(Annual percentage change)					
Reserve money	9.6	19.3	23.2	28.6	27.5	27.5	8.0	8.0	14.4
M3 (Money and quasi-money)	26.1	31.1	26.4	35.4	32.1	28.8	15.2	14.3	19.9
Credit to the private sector	56.8	45.4	33.6	31.4	39.4	26.6	32.2	26.1	31.4
Velocity (GDP/M3)	4.1	3.4	4.1	3.7	3.8	3.5	3.4	3.5	3.4
Money multiplier (M3/Reserve money)	3.0	3.3	3.3	3.5	3.4	3.6	3.7	3.5	3.7
Credit to the private sector (in percent of GDP)	7.1	9.5	8.4	8.6	9.1	9.3	10.4	10.0	11.5
Gross Reserves (in US$ millions)	209	336	326	328	313	325	336	336	326

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.

1/ End of period

2/ Include public enterprises and the local government.

3/ Including valuation.

Table 5. Sierra Leone: Balance of Payments
(In millions of U.S. dollars; unless otherwise indicated)

	2008	2009	2010		2011	2012	2013	2014
			Prog.	Proj.	Proj.	Proj.		
Current account	-223.7	-155.1	-171.1	-181.6	-201.0	-220.9	-234.1	-250.4
Trade balance	-196.0	-186.6	-174.9	-199.3	-192.9	-206.2	-213.6	-224.3
Exports, f.o.b.	274.1	271.3	350.2	341.0	393.7	445.8	498.0	548.6
Of which: diamonds	147.7	105.5	139.1	132.1	155.0	178.1	199.4	216.6
Imports, f.o.b	-470.0	-457.9	-525.1	-540.4	-586.6	-652.0	-711.6	-772.9
Of which: oil	-151.5	-92.7	-126.9	-131.8	-150.9	-174.1	-194.4	-213.4
Services (net)	-64.0	-63.2	-53.5	-64.9	-71.9	-79.4	-86.1	-93.1
Income (net)	-74.8	-35.0	-43.6	-29.9	-32.5	-36.0	-39.3	-42.1
Of which: interest on public debt	-3.9	-4.2	-4.5	-3.5	-3.9	-4.9	-6.0	-6.5
Transfers	111.1	129.8	100.9	112.5	96.4	100.7	104.8	109.2
Official transfers	77.7	83.3	70.8	64.8	43.6	42.3	41.5	40.7
Other transfers	33.4	46.5	30.0	47.7	52.9	58.4	63.3	68.5
Capital and financial account	199.7	263.2	130.2	141.0	182.5	224.4	239.3	267.8
Capital account	48.6	71.0	60.8	60.8	98.3	86.0	89.4	99.5
Of which: project support grants	40.5	56.8	53.4	58.2	95.4	82.8	64.9	70.2
Financial account	151.1	192.2	69.4	80.1	84.2	138.5	150.0	168.2
Foreign direct and portfolio investment	59.2	79.4	51.1	45.9	48.7	59.9	64.9	70.2
Other investment	91.9	112.8	18.2	34.2	35.5	78.6	85.1	98.0
Public sector (net)	48.0	45.9	45.5	49.1	72.9	87.5	86.8	94.7
Disbursements	54.7	56.8	53.4	59.4	84.0	93.5	96.6	106.4
Amortization	-6.7	-10.9	-8.0	-10.3	-11.1	-6.0	-9.8	-11.6
Monetary authorities	0.0	128.1	0.0	0.0	0.0	0.0	0.0	0.0
Change in net foreign assests of commercial banks	0.3	-23.1	0.4	2.0	-19.9	-20.9	-20.1	-22.5
Other, including errors and omissions	43.6	-38.1	-27.7	-16.9	-17.5	12.1	18.4	25.8
Overall balance	-24.0	108.1	-40.9	-40.6	-18.5	3.5	5.2	17.4
Financing								
Central bank net reserves (- increase)	24.0	-108.1	40.9	40.6	18.5	-3.5	-5.2	-17.4
Gross reserve change	6.0	-126.9	0.0	0.0	9.9	-10.0	-5.0	-5.0
Use of Fund loans	18.0	18.8	40.9	40.6	8.5	6.5	-0.2	-12.4
Purchases	18.0	18.8	43.0	42.8	13.5	13.5	6.8	0.0
Repurchases	0.0	0.0	-2.1	-2.1	-5.0	-7.0	-7.0	-12.4
Exceptional financing	0.0	0.0	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	0.0
Memorandum items:				(Percent of GDP)				
Current account	-11.5	-8.4	-9.0	-9.5	-9.5	-9.5	-9.3	-9.2
Trade Balance	-10.0	-10.1	-9.2	-10.5	-9.1	-8.8	-8.5	-8.2
Capital and Financial Account	8.0	16.2	8.3	8.3	9.5	9.1	8.7	8.8
Overall Balance	-1.2	5.8	-2.1	-2.1	-0.9	0.2	0.2	0.6
Official aid (grants and loans)	8.9	10.5	9.6	9.6	10.6	9.4	8.9	8.9
Budget support in US$ (grants and loans)	77.7	82.9	77.8	77.8	53.6	53.0	52.2	51.4
Gross International Reserves								
(US$ millions)	209	336	336	336	326	336	341	346
Months of imports	4.4	6.1	5.7	5.6	4.9	4.6	4.3	4.1
excluding SDR allocation of 2009	4.4	3.8	3.5	3.5	3.0	2.9	2.7	2.6
National currency per US dollar (average)	2,984.6	3,410.2	…	…	…	…	…	…

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.

Table 6. Sierra Leone: Indicators of Capacity to Repay the Fund

		Projection								
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fund obligations based on existing credit										
(in millions of SDRs)										
Principal	0.0	1.4	3.3	4.6	4.6	8.1	9.9	10.8	9.4	9.4
Charges and interest 1/	0.1	0.0	0.0	0.2	0.2	0.1	0.1	0.1	0.1	0.0
Fund obligations based on existing and prospective credit										
(in millions of SDRs)										
Principal	0.0	1.4	3.3	4.6	4.6	8.1	9.9	12.1	12.6	14.3
Charges and interest 1/	0.1	0.0	0.0	0.2	0.2	0.2	0.2	0.2	0.1	0.1
Total obligations based on existing and prospective credit										
In millions of SDRs	0.1	1.4	3.3	4.8	4.8	8.3	10.0	12.3	12.7	14.4
In millions of US$	0.2	2.1	5.0	7.3	7.4	12.7	15.3	18.7	19.3	22.0
In percent of exports of goods and services	0.1	0.5	1.1	1.4	1.3	2.0	2.2	2.5	2.3	2.5
In percent of debt service 2/	1.2	13.3	25.0	40.9	32.2	41.5	44.7	47.1	44.6	44.9
In percent of GDP	0.0	0.1	0.2	0.3	0.3	0.5	0.5	0.6	0.6	0.6
In percent of Gross International Reserves	0.1	0.6	1.5	2.2	2.2	3.7	4.4	5.3	5.4	6.0
In percent of quota	0.1	1.4	3.2	4.6	4.7	8.0	9.7	11.8	12.2	13.9
Outstanding Fund credit										
In millions of SDRs	46.7	73.4	79.0	83.2	83.1	75.0	65.1	53.0	40.4	26.1
In millions of US$	72.0	111.2	120.0	126.6	126.6	114.3	99.4	80.9	61.7	39.8
In percent of exports of goods and services	22.2	28.1	26.5	24.7	22.2	18.3	14.6	10.9	7.3	4.5
In percent of debt service	477.5	697.1	602.7	705.6	554.3	374.0	289.8	203.1	142.3	81.3
In percent of GDP	3.9	5.8	5.7	5.4	5.0	4.2	3.4	2.6	1.8	1.1
In percent of Gross International Reserves	21.4	33.1	36.8	37.6	37.1	33.0	28.3	22.7	17.1	10.9
In percent of quota	45.0	70.7	76.2	80.3	80.1	72.3	62.8	51.1	39.0	25.2
Net use of Fund credit (in millions of SDRs)	12.2	26.8	5.6	4.3	-0.2	-8.1	-9.9	-12.1	-12.6	-14.3
Disbursements	12.2	28.2	8.9	8.9	4.5	0.0	0.0	0.0	0.0	0.0
Repayments	0.0	1.4	3.3	4.6	4.6	8.1	9.9	12.1	12.6	14.3
Memorandum items:										
Exports of goods and services (in millions of US$)	324	395	454	512	570	626	681	742	841	891
Debt service (in millions of US$)	15	16	20	18	23	31	34	40	43	49
Nominal GDP (in millions of US$)	1,856	1,914	2,112	2,333	2,527	2,735	2,928	3,135	3,356	3,591
Gross International Reserves (in millions of US$)	336	336	326	336	341	346	351	356	361	366
Quota (millions of SDRs)	104	104	104	104	104	104	104	104	104	104

Source: IMF staff estimates and projections.

1/ There are no interest payments to the Fund in 2010-11.

2/ Total debt service includes IMF repayments.

Table 7. Sierra Leone: Schedule of Disbursements Under the ECF Arrangement, 2010-2012

Availability	Disbursements In millions of SDRs	Disbursements In percent of quota	Conditions for Disbursement
May 15, 2010	4.44	4.28	Effectiveness of the three-year ECF arrangement
November 15, 2010	4.44	4.28	Board completion of the first review based on observance of performance criteria for June 30, 2010
May 15, 2011	4.44	4.28	Board complettion of the second review based on observance of performance criteria for December 31, 2010
November 15, 2011	4.44	4.28	Board completion of the third review based on observance of performance criteria for June 30, 2011
May 15, 2012	4.44	4.28	Board completion of the fourth review based on observance of performance criteria for December 31, 2011
November 15, 2012	4.44	4.28	Board completion of the fifth review based on observance of performance criteria for June 30, 2012
May 15, 2013	4.47	4.32	Board completion of the sixth review based on observance of performance criteria for December 31, 2012
Total disbursements	**31.11**	**30.00**	

Table 8. Sierra Leone: Millennium Development Goals

	1990	1995	2000	2005	2008
Goal 1: Eradicate extreme poverty and hunger					
Employment to population ratio, 15+, total (%)	64	65	65	64	64
Employment to population ratio, ages 15-24, total (%)	39	41	44	41	42
GDP per person employed (annual % growth)	-20	-9	1	4	4
Income share held by lowest 20%	1.1	..	..	6.1	..
Malnutrition prevalence, weight for age (% of children under 5)	..	..	24.7	28.3	..
Poverty gap at $1.25 a day (PPP) (%)	45	..	..	20	..
Poverty headcount ratio at $1.25 a day (PPP) (% of population)	63	..	..	53	..
Prevalence of undernourishment (% of population)	45	43	..	47	..
Vulnerable employment, total (% of total employment)	..	..	..	..	..
Goal 2: Achieve universal primary education					
Literacy rate, youth female (% of females ages 15-24)	..	..	..	37	44
Literacy rate, youth male (% of males ages 15-24)	..	..	..	60	64
Persistence to last grade of primary, total (% of cohort)	..	..	..	..	..
Primary completion rate, total (% of relevant age group)	..	..	..	81	81
Total enrollment, primary (% net)	..	..	..	..	..
Goal 3: Promote gender equality and empower women					
Proportion of seats held by women in national parliaments (%)	..	6	9	15	13
Ratio of female to male enrollments in tertiary education	..	..	40	..	..
Ratio of female to male primary enrollment	69	..	71	90	90
Ratio of female to male secondary enrollment	57	..	71	69	69
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	..	..	..	23.2	..
Goal 4: Reduce child mortality					
Immunization, measles (% of children ages 12-23 months)	..	..	37	67	67
Mortality rate, infant (per 1,000 live births)	169	166	161	157	155
Mortality rate, under-5 (per 1,000)	290	283	274	265	262
Goal 5: Improve maternal health					
Adolescent fertility rate (births per 1,000 women ages 15-19)	..	146	139	130	126
Births attended by skilled health staff (% of total)	..	..	42	43	..
Contraceptive prevalence (% of women ages 15-49)	..	..	4	5	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	2,100	..
Pregnant women receiving prenatal care (%)	..	..	68	81	..
Unmet need for contraception (% of married women ages 15-49)	..	..	..	..	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases					
Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	..	..	61	52	..
Condom use, population ages 15-24, female (% of females ages 15-24)	..	..	..	..	..
Condom use, population ages 15-24, male (% of males ages 15-24)	..	..	..	..	..
Incidence of tuberculosis (per 100,000 people)	207	279	377	509	574
Prevalence of HIV, female (% ages 15-24)	..	..	..	1.3	1.3
Prevalence of HIV, male (% ages 15-24)	..	..	..	0	0
Prevalence of HIV, total (% of population ages 15-49)	0.2	1.0	1.2	1.6	1.7
Tuberculosis cases detected under DOTS (%)	..	29	33	36	37
Goal 7: Ensure environmental sustainability					
CO2 emissions (kg per PPP $ of GDP)	0.2	0.3	0.4	0.3	..
CO2 emissions (metric tons per capita)	0.1	0.1	0.1	0.2	..
Forest area (% of land area)	43	41	40	38	..
Improved sanitation facilities (% of population with access)	..	12	12	11	11
Improved water source (% of population with access)	..	57	57	53	53
Marine protected areas, (% of surface area)	..	..	..	..	..
Nationally protected areas (% of total land area)	..	..	..	4.1	4.1
Goal 8: Develop a global partnership for development					
Aid per capita (current US$)	15	51	43	69	99
Debt service (PPG and IMF only, % of exports, excluding workers' remittances)	10	62	46	9	4
Internet users (per 100 people)	0.0	0.0	0.1	0.2	0.3
Mobile cellular subscriptions (per 100 people)	0	0	0	14	18
Telephone lines (per 100 people)	0	0	0	..	..
Other					
Fertility rate, total (births per woman)	5.5	5.5	5.4	5.3	5.2
GNI per capita, Atlas method (current US$)	190	200	150	230	320
GNI, Atlas method (current US$) (billions)	0.8	0.8	0.6	1.2	1.8
Gross capital formation (% of GDP)	10.0	5.6	6.9	17.4	19.7
Life expectancy at birth, total (years)	40	39	43	46	48
Literacy rate, adult total (% of people ages 15 and above)	..	..	..	35	38
Population, total (millions)	4.1	4.0	4.2	5.1	5.6

Source: World Development Indicators database, 2009.

Table 9. Sierra Leone: Financial Soundness Indicators of the Banking System, 2005–10

	2005	2006	2007	2008	2009	2010 June
	(Percent, end of period, unless otherwise indicated)					
Capital adequacy						
Regulatory capital ratio 1/	35.7	33.3	35.0	43.5	34.0	29.5
Regulatory tier 1 capital ratio 2/	10.3	17.0	16.7	18.7	18.8	16.6
Asset quality						
Nonperforming loans to total gross loans	…	…	25.6	17.9	10.6	13.6
Nonperforming loans (net of provisions) to regulatory capital	…	…	28.5	4.6	9.5	9.3
Earnings and profitability						
Return on assets	8.1	5.8	3.1	2.2	1.6	1.2
Return on equity	28.0	17.0	10.3	7.2	4.0	3.8
Liquidity						
Ratio of net loans to total deposits	27.5	26.5	27.7	33.9	41.5	43.6
Liquidity ratio 3/	53.0	58.9	53.3	62.0	53.4	34.7
Statutory minimum liquidity ratio 3/ 4/	34.0	28.5	25.7	25.0	29.0	33.2
Share of foreign exchange deposits in total deposits	30.7	32.4	36.5	32.2	34.5	35.4
	(Number of banks not complying)					
Prudential ratios at year-end						
Capital adequacy	0	0	0	0	1	1
Minimum liquidity ratio	0	0	0	0	1	1
Minimum capital	0	1	1	1	2	0
Limit of single large exposure 5/	0	2	1	2	4	5
Memorandum Item:						
Number of banks	7	8	10	13	14	13

Source: Bank of Sierra Leone.

1/ Capital requirement over risk-weighted assets (solvency ratio).

2/ Core capital (Tier I) over total assets.

3/ Calculated taking into account both domestic currency and foreign currency deposits. Liquid assets include domestic currency cash in vault, claims on the BSL, claims on discount houses, and government securities.

4/ Effective November 2007, minimum liquidity includes 40 percent of demand deposits and 20 percent of quasi-money to be held in either cash or treasury bills.

5/ A single large exposure of an institution is any exposure that is 2 percent or more of its capital base.

APPENDIX: SIERRA LEONE—LETTER OF INTENT

November 17, 2010

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

Dear Mr. Strauss-Kahn:

The attached Memorandum of Economic and Financial Policies (MEFP) supplements the one attached to my letter to you dated May 18, 2010. It describes recent economic developments and progress in the implementation of the ECF-supported program during the first half of 2010 and presents our policies planned for the remainder of 2010 and 2011.

All June 2010 quantitative performance criteria and indicative targets were met. The two structural benchmarks for June were met, but with a slight delay: the automatic domestic fuel-pricing formula was adopted in October to bring the domestic pump prices in line with international oil prices and the BSL adopted the new off-site surveillance guidelines for banks in November.

Although fiscal policy remained on target in the first half of 2010, spending accelerated in the second half of the year due to unanticipated expenditures on emergency power project, hiring of health care workers, higher interest payments, outlays for road construction, and payments of arrears to oil marketing companies because of delays in implementing full pass-through of international fuel prices. While tax collections are anticipated to exceed program projections, mostly explained by very good performance of the GST introduced in January, additional domestic financing of 0.9 percent of GDP will be required in 2010. Hence, the Government of Sierra Leone (GoSL) requests that the target for end-December 2010 on net domestic bank credit to the central government be modified. To further boost domestic revenue in 2011, we have raised royalties on diamonds to 6.5 percent, in line with the Mines and Minerals Act 2009. The GoSL is committed to present to Parliament a 2011 budget that constrains non-priority spending and target net domestic bank financing of about 2 percent of GDP.

On this basis, the GoSL requests that the second disbursement be made available upon completion of the first review under the ECF arrangement.

The GoSL believes that the policies set forth in the attached MEFP and Technical Memorandum of Understanding (TMU) are adequate to achieve the objectives of the new program, but stands ready to take any further measures that become necessary for this purpose, in consultation with the Fund. The GoSL will consult with the Fund in advance of revisions to the policies contained in the MEFP and continue to provide the staff of the IMF the information required to accurately assess Sierra Leone's progress in executing the policies in the MEFP. The second, third, and fourth reviews under the current program shall take place in June 2011, December 2011 and June 2012, respectively. Furthermore, the GoSL will continue to consult with the IMF on its economic and financial policies, in accordance with the IMF's policies on such consultations.

The GoSL agrees, in line with its commitment to transparency and accountability, to the publication of this letter, its attachments, and the related staff report in accordance with the procedures for publication.

Very truly yours,

________/s/__________	____________/s/_____________
Samura M. W. Kamara	Sheku S. Sesay
Minister of Finance and Economic Development	Governor of Bank of Sierra Leone

Attachments

ATTACHMENT I. SIERRA LEONE: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

I. INTRODUCTION

1. This memorandum reviews recent economic developments and outlines the macroeconomic policies and structural reforms that the Government of Sierra Leone (GoSL) will pursue under the current Extended Credit Facility (ECF).

II. RECENT ECONOMIC DEVELOPMENTS

2. **Economic activity appears to have picked up in 2010.** Exports of diamonds have rebounded and indicators point to buoyant agricultural output. Real GDP growth is projected at 4.5 percent in 2010, compared to 3.2 percent in 2009. While lower fuel and domestic food prices eased inflationary pressures during most of 2009, inflation rose in the first half of 2010 due to the depreciation of the leone in late 2009, the introduction of the goods and services tax (GST) in January, and higher domestic fuel prices. The CPI increased by 18 percent in the 12 months through August 2010. However, so far this year, the leone has been stable against the US dollar.

3. **Fiscal policy was broadly implemented as programmed through June.** Revenue collections were above the target and current spending was close to the program, but the wage bill was higher due to higher than anticipated hiring in the health care sector. Capital expenditures were lower than programmed due to shortfalls in external project support. However, domestically financed capital spending was higher than envisaged.

4. **Monetary policy remained tight in the first half of 2010.** Growth in reserve money and broad money decelerated significantly in the first half of 2010, as programmed. Private sector credit continued to expand in the first half of 2010, albeit at a slower pace. With a stable value of the leone, the amount offered on the BSL's weekly foreign exchange auctions fell as envisaged in the program to less than US$1 million by June.

5. **Program performance was satisfactory in the first half of 2010.** All June 2010 quantitative performance criteria and indicative targets were met (Table 1) and the two structural benchmarks for June have been implemented, though with some delay (Table 2). Moreover, two of the structural benchmarks for September have been implemented, though with a slight delay, and the remaining benchmark is expected to be implemented in November 2010.

III. MEDIUM-TERM FRAMEWORK

6. **The medium term outlook for the Sierra Leonean economy is favorable.** Real GDP growth is expected to recover to 4.5 percent in 2010 and increase to 6 percent by 2012, benefiting from the recent completion of the Bumbuna power station, investment in basic infrastructure, and initiatives to improve the business climate and raise agricultural productivity. The global economic recovery will increase export demand for minerals and

cash crops, which should contribute to exchange rate stability. Combined with expanding domestic food production, this should ease inflationary pressures. Monetary and exchange rate policies will also aim at returning to single-digit inflation, with inflation projected to decline from 16 percent in 2010 to 8 percent in 2012. However, import coverage of gross foreign exchange reserves is expected to decline from 6.1 months in 2009 to 4.6 months in 2012, as imports recover with economic recovery and expansion in investment.

7. **The economic impact of newly signed mining lease agreements for iron ore could be significant.** Assuming full implementation of the planned investments, exports and tax revenue would increase substantially in the medium- and long-term. However, since these projects are still in their infancy and there are uncertainties about the timing and production volumes, they have not been incorporated in the medium-term macroeconomic projections. Moving forward, the government wishes to level the playing field for new mining investments and it will therefore apply the fiscal regime defined in the Mines and Minerals Act (MMA) 2009 and existing tax and custom acts to future mining lease agreements. Also, the government will consider, as stipulated for in the MMA, demanding an equity stake in future larger mining projects to participate in windfalls and to gain insight into the mining business.

8. **Consistent with the priorities laid out in the Agenda for Change 2008–12 (PRSP II), the emphasis will be to create fiscal space to improve basic infrastructure while maintaining macroeconomic stability**. Since grants and concessional budget financing from donors are likely to decline to pre-crisis levels in the next few years, the government recognizes the urgent need to increase domestic revenue and strengthen the efficiency of public spending. Reflecting efficiency gains from the introduction of GST and improvement in tax administration, the aim is to raise domestic revenue above 13.5 percent of GDP by 2012. To achieve this target, the GoSL will fully apply the fiscal regime stipulated in existing tax and customs acts and will resist issuing discretionary tax exemptions. Fiscal space will further be created by containing non-priority spending, and raising public sector efficiency, especially on project selection and implementation. The GoSL is committed to keeping domestic financing below 2 percent of GDP to maintain debt sustainability and prevent crowding out of the private sector.

9. **Debt sustainability will remain a priority.** The GoSL is committed to a conservative strategy of external borrowing on concessional terms. A comprehensive national debt law and procedures manual will be adopted in 2010. In collaboration with the Public Debt Unit of Ministry of Finance and Economic Development (MOFED), government agencies are working on improving the quality of debt data and reporting in order to better monitor commitments, disbursements, and debt service obligations. The Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) will be electronically linked with IFMIS. In order to further improve on debt management, the Government is requesting assistance from the World Bank and the Fund with respect to developing a comprehensive Medium-Term Debt Management Strategy (MTDS).

IV. Policies for the Remainder of 2010

10. **The fiscal deficit is projected to be higher than programmed in 2010.** Fiscal spending has accelerated in the second half of 2010 due to the hiring of an additional 3,000 health care staff, unanticipated outlays for the emergency power project that was supposed to expire in June, payments of arrears on fuel subsidies, and additional infrastructure projects particularly on roads. For the year, total expenditures, including payments of arrears, are projected to be 1.5 percentage points of GDP higher than programmed. On the revenue side, the GST continues to perform better than anticipated and revenues are therefore projected to exceed the program target by 0.6 percentage points of GDP. With unchanged program budget support grants and loans, domestic bank financing is projected to increase to 3 percent of GDP from 2.1 percent as envisaged in the program. The overall fiscal deficit, excluding grants, is projected to increase to 11.5 percent of GDP from 10.8 percent of GDP in the program. In case domestic revenues, including any prepayment of taxes, exceed Le 988 billion, the additional revenue will be used to reduce domestic bank financing in 2010.

11. **The GoSL has consolidated several existing tax incentives from a number of sector-specific acts into the tax and customs acts.** The aim is to maintain the current incentives without introducing new ones, while working towards eliminating all discretionary tax incentives and exemptions. To this end, the GoSL has submitted the Revenue Management Act 2010 to Parliament for enactment. The purpose of the act is to regulate the granting of tax incentives and discretionary duty waivers. Furthermore, to evaluate the costs and benefits of this policy, the GoSL will prepare a policy review by March every year covering the previous calendar year. This review will contain a list of all projects that have benefited from the catalogue of incentives, specify the purpose of the projects, and report foregone revenue. The review will be made publicly available and submitted to the Parliament.

12. **A new Mines and Minerals Act came into effect on January 1, 2010.** In line with the act, a 6.5 percent royalty for diamond mining became effective in November 2010. The annual revenue effect is estimated at 0.2 percent of GDP.

13. **Monetary policy will remain tight to prevent the second round effects of the increase in inflation from the introduction of the GST earlier this year and from higher domestic fuel prices.** Reserve money is targeted to grow by 7.5 percent in 2010, consistent with 14 percent growth in broad money. Despite higher domestic financing of the budget, private sector credit is still anticipated to expand by a healthy 26 percent in 2010. The BSL will stand ready to tighten monetary policy further, should inflationary pressures increase. With a stable leone against the US dollar, the amount offered in the foreign exchange auction will remain at a reduced level.

14. **Direct credit from the BSL to the government increased significantly in the second half of the year to finance accelerated budgetary spending.** In September,

government overdrafts in BSL amounted to about 2.7 percent of GDP. However, almost immediately, the BSL was able to withdraw liquidity by selling significant amounts of its holding of treasury bills to keep monetary policy on course. The GoSL recognizes shortcomings of relying on central bank financing. Hence overdrafts in BSL was reduced to about Le 175 billion in early November 2010 and will be further reduced to Le 150 billion (2 percent of GDP) by end-November 2010. In line with the BSL Act, all direct credits provided in 2010 will be repaid no later than 93 days after end-2010. Also, the GoSL is committed to revise the BSL Act to limit the use of direct credit to government in the future (see section VI).

V. POLICIES FOR 2011

15. **Macroeconomic policies for 2011 will aim at improving basic infrastructure and social services while maintaining macroeconomic stability.** This should help facilitate higher economic growth and lower inflation.

Fiscal policy

16. **The 2011 budget** envisages higher domestic revenue, a significant increase in capital spending, mainly financed by external grants or concessional loans, and a moderate domestic financing need.

17. **On the revenue side,** domestic revenue is projected to increase to 13.3 percent of GDP from 13 percent of GDP in 2010, reflecting an increase in diamond royalties to 6.5 percent and continued efficiency gains from GST. This projection does not incorporate any revenue from ongoing iron ore investment projects, except for the annual license fee. Grants remain at 6.8 percent of GDP as the decrease in budget support by 0.9 percentage points is compensated by an increase in project grants. Privatization proceeds are projected at 0.6 percent of GDP, reflecting sales of shares in Rokel Bank and Sierra Leone Commercial Bank, as well as proceeds from the concession of the port in Freetown.

18. **On the expenditure side,** a shift from current to capital spending is envisaged**.** In line with the priorities laid out in the Agenda for Change to build basic infrastructure, capital spending will increase from 8.4 percent of GDP in 2010 to 10.2 percent in 2011, financed by external grants and concessional project loans (7.5 percent of GDP) and domestic sources (2.7 percent of GDP). Wages and salaries are envisaged to decrease from 6.8 percent of GDP in 2010 to 6.5 percent in 2011, reflecting a 15 percent increase in basic salaries and savings accruing from the pay reform that would start implementation in the second half of the year. In order to conduct fair, peaceful and democratic elections in 2012, current expenditures will include Le 20 billion (0.3 percent of GDP) on elections, with additional donor support of Le 44 billion.

19. **The overall fiscal deficit, excluding grants, is envisaged to increase to 12.5 percent of GDP from 11.5 percent of GDP in 2010.** However, domestic bank

financing is projected to decline to 1.8 percent of GDP from 3.3 percent of GDP in 2010, reflecting an increase in external project financing and privatization proceeds.

Monetary and exchange rate policies

20. **Monetary policy will aim to achieve single digit inflation by the end of 2011**. Reserve money is envisaged to grow at 14 percent that will imply a 20 percent growth in broad money and will accommodate a 31 percent growth in private credit. With a constrained access to direct credit from the central bank by the GoSL, liquidity management will be eased.

21. **The authorities are committed to maintaining a flexible exchange rate to facilitate adjustment to external shocks.** The BSL will limit its foreign currency sales to absorb foreign-financed budget spending and smooth short-term market volatility.

VI. STRUCTURAL REFORMS

22. **The structural reform program will complement macroeconomic policies to promote an efficient public sector and higher sustainable private sector-led economic growth.** Structural policies will continue to focus on improving tax administration, strengthening public financial management, and developing the financial sector (Tables 2 and 4). Policies for the two latter areas will be based on the Integrated Public Financial Management Reform Program (IPFMRP) and the Financial Sector Development Plan (FSDP), respectively.

Improving tax administration

23. **The GoSL will further step up efforts to improve tax administration and broaden the tax base**. The current tax administration suffers from inefficiencies arising from separate tax departments for GST and income and it is not conducive to enhance tax compliance. To this end, the National Revenue Authority (NRA) will integrate GST operations (taxpayer services, filing and returns processing, and coordinated audit operations) with the Large Taxpayer Office (*Structural Benchmark for December 2010*). Moreover, NRA will transfer all eligible taxpayers to the Medium Taxpayer Office (MTO) and integrate the GST administration with MTO to improve the efficiency of tax collections (*Structural Benchmark for September 2011*).

24. **The NRA will step up efforts to improve tax collection and compliance.** Measures include applying penalties for non-filing of returns and underestimation of quarterly installment payments; and levying and collecting interest on late payment of tax. In a similar vein, a new small taxpayer regime will be implemented to improve voluntary compliance (*Structural Benchmark for December 2011*).

Strengthening public financial management

25. **The GoSL will strengthen the Medium-Term Expenditure Framework (MTEF) by enhancing the planning, monitoring and evaluation process for capital projects.** The government will fully integrate a three-year public investment plan with the budget process for 2012 budget in line with the amendments to the Government Budget and Accountability Act (*Structural Benchmark for December 2011*).

26. **The GoSL is committed to building a high quality workforce in the public sector.** To improve working conditions for the public service and to attract staff of high caliber, the government will develop and start implementing a multiyear pay reform (*Structural Benchmark for June 2011*). The reform will (i) realign current discrepancies in qualifications and grade placements; (ii) decompress the wage structure; (iii) retrench redundant staff; and (iv) gradually raise compensation to competitive levels financed partly from the restructuring and, if necessary, a moderate increase in the total public sector wage bill.

27. **The roll out of IFMIS to MDAs will continue to strengthen budget execution.** So far, IFMIS has been rolled out to 11 key MDAs with 2 additional MDAs in the process, accounting for about 65 percent of expenditures. The MOFED will continue to provide training and support to IFMIS users across MDAs to ensure that activities are properly and adequately captured within the system.

Financial sector measures

28. **The independence of the BSL will be strengthened by amending the BSL and Banking Acts (***Structural Benchmark for June 2011*). The amendments will enhance the independence of the BSL and align the acts with the Basel Core Principles for Effective Supervision, as recommended by recent IMF TA missions.

29. **There is a need to limit the use of BSL direct credits to the government.** This will encourage the government to improve its cash flow management and support the development of securities market. Also, the amendments to the BSL Act will (i) set a limit of the annual flow of direct credits to the government (loans and advances) to 5 percent of the actual domestic revenue in the previous budget year; (ii) require that such direct credits are repaid within 93 days from the end of the financial year (repayments may be made with marketable treasury bills that mature before the 93 day deadline); and (iii) stipulate that the BSL may purchase government securities strictly for monetary policy purposes and provided that such purchases are only made in the secondary market. While these amendments are not likely to be approved before mid-2011, the government and the BSL are committed to adhere to the above principles for BSL direct credits to the government from the beginning of 2011.

30. **The BSL will strengthen its supervisory role to reduce the vulnerabilities arising in the financial sector from NPLs**. This will be achieved by developing a new IT platform and filling open staff positions in the Banking Supervision Department of the BSL. Also, the BSL will gradually move to a risk-based supervision system. In addition, the BSL has aimed to increase the minimum capital requirement from Le 15 billion to Le 30 billion over a five-year period, starting in 2010.

31. **To develop a long-term capital market,** the MOFED and the BSL will engage market participants, including the commercial banks, NASSIT and other non-bank financial institutions, to develop a long-term bond market consistent with the government's financing need. The GoSL will also strengthen the capital market regulatory structure and governance by enacting the Securities and Exchange Commission's (SEC) Act and implement associated regulations, and deepen the long-term capital market with the privatization and divestiture of slated public enterprises.

32. **Private sector development is constrained by limited access to financial services.** Lack of financial development is evident in low credit to the private sector. Access to credit will be enhanced by strengthening information structure through establishing a credit reference bureau (*Structural Benchmark for December 2010*). To improve efficiency of transactions in the economy, the BSL is working towards strengthening the payments and settlement systems. In this context the AfDB is financing the automation of the payment system, which includes: (i) Real Time Gross Settlement; (ii) Automated Cheque Processing and Automated Clearing House; (iii) Scriptless Securities Settlement System; (iv) Core Banking Application; and (v) Infrastructure Upgrade. Contracts have been awarded to solution providers for all components and studies to gauge the scope have been conducted for most of them**.**

33. **To prevent opportunities for money laundering,** by the end of this year the government will submit to the parliament a new law on Anti-Money Laundering and Combating the Financing of Terrorism.

Other reforms

34. **The GoSL has committed to the principles of Extractive Industries Transparency Initiative (EITI).** The first EITI Report (covering mining for 2006–07) was published in March, and the final validation report was submitted on August 9, 2010. The validation report recommends a number of improvements to the governance and management of the process which are being considered. Furthermore, there are on-going efforts to disseminate the first Sierra Leone EITI report.

35. **There is a need to strengthen Sierra Leone's capacity to collect and disseminate economic statistics.** The GoSL is seeking technical assistance from the IMF to improve the reporting of national account and price statistics. There is a particular need to improve collection of data on agriculture output and to compute one single reliable consumer price index.

VII. Program Monitoring

36. The program will be monitored based on quantitative performance criteria for end–December 2010, end-June 2011 and end-December 2011 (Tables 1 and 3), and structural benchmarks for 2010 and 2011 (Tables 2 and 4).

Table 1. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2010 1/
(Cumulative change from beginning of calendar year to end of month indicated; Le billions, unless otherwise indicated)

	2009	2010					
		June					
	Actual Stock	*Prog.*	*Adj. Prog.*	*Act.*	*Status*	*Sept. 2/*	*Dec.*
Performance criteria							
Net domestic bank credit to the central government (ceiling)	647.3	191.5	240.4	206.5	Met	202.7	250.3
Unadjusted target (ceiling)			191.5				
Adjustment for the shortfall (excess) in external budget support			31.5				
Adjustment for the issuance of government securities to the nonbank private sector			17.3				
Net domestic assets of the central bank (ceiling)	-442.3	198.6	247.7	192.4	Met	235.5	235.1
Unadjusted target (ceiling)			198.6				
Adjustment for the shortfall (excess) in external budget support			31.5				
Adjustment for exchange rate depreciation (appreciation)			17.6				
Gross foreign exchange reserves of the central bank, US$ millions (floor)	336.4	-8.7	-24.3	-23.2	Met	-11.8	0.0
Unadjusted target (floor)			-8.7				
Adjustment for the shortfall (excess) in external budget support 3/			-7.9				
Adjustment for the shortfall in the US$ value of IMF disbursement			-7.2				
Adjustment for the increase (decrease) in BSL short-term foreign currency liabilities			-0.4				
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) 3/	…	0.0		0.0	Met	0.0	0.0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) 3/	0.0	0.0		0.0	Met	0.0	0.0
External payment arrears of the public sector (ceiling) 3/	…	0.0		…		0.0	0.0
Indicative target							
Total domestic government revenue (floor)	…	432.8		438.1	Met	676.8	987.9
Poverty-related expenditures (floor)	…	252.2		294.5	Met	337.9	417.0
Memorandum items:							
External budgetary assistance (US$ million) 4/	…	29.6		21.7		52.1	77.8
Net credit to government by nonbank sector 5/	…	44.0		26.7		45.4	18.4
ECF disbursements (SDR millions)		11.4		7.0		11.4	15.9
Exchange rate (Leones/US$)	…	3,990		3,906		3,990	3,990

1/ The performance criteria and indicative targets are defined in the Technical Memorandum of Understanding (TMU).
2/ Indicative targets.
3/ These apply on a continuous basis.
4/ Including grants and loans.
5/ Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the nonfinancial private sector.

Table 2. Sierra Leone: Structural Benchmarks for 2010

Measures	Timing	Macro Rationale	Status
• Adopt a domestic fuel pricing formula that reflects full pass-through of international oil prices.	End– June	To enhance transparency and eliminate risks for the budget in case of external shocks.	Met with delay. Implemented in October 2010.
• Adoption by the BSL of new off-site surveillance guidelines for banks.	End– June	To enhance the supervisory role of the BSL for financial sector development.	Met with delay. Implemented in November 2010.
• Establish a Domestic Tax Department (DTD) as the vehicle for achieving integration of domestic tax collection and make it functional, including recruiting Commissioner and Deputy Commissioner.	End-September	To improve efficiency of revenue collection efforts.	Not met. Following interviews held in October 2010, the NRA Board has appointed a Commissioner and a Deputy Commissioner for the Domestic Tax Department.
• Submit to parliament amendments of the Government Budgeting and Accountability Act (2005) and Financial Management Regulation to ensure that only viable capital projects enter into the budget.	End–September	To improve efficiency of public investments and achieve the program growth targets.	Met with delay. Implemented in October 2010.
• Establish reverse repo rate as the benchmark interest rate and announce the rate after every Monetary Policy Committee meeting.	Continuous from end-September	To increase the effectiveness of monetary policy and help develop a yield curve.	Not met. Expected to be met in November 2010.
• Establish a credit reference bureau.	End-December	To improve informational infrastructural and promote credit access for credit-worthy customers.	The Credit Reference Bill was gazette on September 9, 2010. This bill has been sent to parliament and a pre-legislative hearing is scheduled for the third week in November.
• Integrate the Goods and Services Tax (GST) administration within the Large Taxpayer Office (LTO).	End-December	To ensure full and efficient implementation of the GST to achieve domestic revenue target.	An action plan has been developed and sent to the Board. NRA Management intends to execute the establishment of the LTD and to integrate the GST administration within the same framework but at different dates of end September and end December, respectively. The next step is to seek approval by the NRA Board.

Table 3. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2011 1/

(Cumulative change from beginning of calendar year to end of month indicated; Le billions, unless otherwise indicated)

	Dec. 2010	2011			
	Stock	*Mar. 2/*	*Jun.*	*Sept. 2/*	*Dec.*
Performance criteria					
Net domestic bank credit to the central government (ceiling)	897.6	64.6	106.6	137.6	152.1
Net domestic assets of the central bank (ceiling)	-207.5	63.7	112.8	146.6	159.5
Gross foreign exchange reserves of the central bank, US$ millions (floor)	336.4	-22.7	-14.8	-24.7	-9.9
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) 3/	…	0.0	0.0	0.0	0.0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) 3/	…	0.0	0.0	0.0	0.0
External payment arrears of the public sector (ceiling) 3/	…	0.0	0.0	0.0	0.0
Indicative target					
Total domestic government revenue (floor)	…	260.0	549.7	831.8	1,156.6
Poverty-related expenditures (floor)	…	134.6	271.0	382.5	514.2
Memorandum items:					
External budgetary assistance (US$ million) 4/	…	16.7	31.3	42.5	53.5
Net credit to government by nonbank sector 5/	…	12.4	18.2	25.9	43.2
ECF disbursements (SDR millions)			4.4	4.4	8.9
Program exchange rate (Leones/US$)	3,990	3,990	3,990	3,990	3,990

1/ The performance criteria and indicative targets are defined in the Technical Memorandum of Understanding (TMU).
2/ Indicative targets.
3/ These apply on a continuous basis.
4/ Including grants and loans.
5/ Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the non financial private sector.

Table 4. Sierra Leone: Proposed Structural Benchmarks for 2011

Measures	Timing	Macro Rationale
• Submit amendments to the BSL and Banking Acts.	End–June	To increase operational independence of the BSL and improve regulation and supervision of the financial sector.
• Develop and start implementing a pay reform for public servants.	End-June	To improve the quality of civil services by providing competitive wages.
• Transfer all eligible taxpayers to the Medium Taxpayer Office (MTO) and integrate GST administration with MTO.	End-September	To improve efficiency of revenue collection efforts.
• Implement new small taxpayer regime.	End–December	To improve voluntary compliance and raise tax revenue.
• Strengthen the medium-term expenditure framework by completing a three-year public investment plan, fully integrated with the budget process, to be submitted with 2012 budget.	End-December	To improve efficiency of public investments and achieve medium-term growth targets

ATTACHMENT II. SIERRA LEONE: TECHNICAL MEMORANDUM OF UNDERSTANDING

November 17, 2010

I. INTRODUCTION

1. This memorandum sets out the understandings between the Sierra Leonean authorities and the International Monetary Fund (IMF) regarding the definitions of the quantitative performance criteria (PCs) and structural benchmarks (SBs) for the program supported by the Extended Credit facility (ECF) arrangement, as well as the related reporting requirements. Unless otherwise specified, all quantitative PCs and indicative targets will be evaluated in terms of cumulative flows from the beginning of the period, as specified in Table 3 of the Memorandum of Economic and Financial Policies (MEFP).

2. **Program exchange rates.** For the purpose of the program, foreign currency denominated values in 2010 and 2011 will be converted from their U.S. dollar denominated value into Sierra Leonean currency (leones) using a program exchange rate of Le 3,990/US$.

II. QUANTITATIVE PERFORMANCE CRITERIA

A. Gross Foreign Exchange Reserves of the Bank of Sierra Leone (BSL)

3. **Definition**. Unless otherwise noted, gross foreign exchange reserves of the Bank of Sierra Leone (BSL) are defined as reserve assets of the BSL. Reserve assets are defined in the IMF's *Balance of Payments Manual* (5th ed.) and elaborated in the reserve template of the Fund's *International Reserves and Foreign Currency Liquidity: Guidelines for a Data Template*. They exclude foreign assets not readily available to, or controlled by, the monetary authorities.

Adjustment clauses

4. The floor on the change in gross foreign exchange reserves will be adjusted (a) downward (upward) by the amount in U.S. dollars of the shortfall (excess) in programmed external budgetary assistance[1]—the downward adjustment will be capped at the equivalent of US$20 million; (b) downward (upward) for any shortfall (excess) in the U.S. dollar value of disbursements from the IMF under the ECF arrangement; and (c) upward (downward) for any increase (decrease) in BSL short-term (one year or less in original maturity) foreign currency-denominated liabilities (to residents and nonresidents).

[1] External budgetary assistance is defined as program grants and program loans, excluding HIPC assistance.

B. Net Domestic Assets of the BSL

5. **Definition.** Net domestic assets (NDA) of the BSL are defined as the end-period stock of the reserve money less the end-period stock of net foreign assets calculated at the program exchange rates. Reserve money includes currency issued (equal to currency outside banks plus cash in vaults), deposits of commercial banks with the BSL and the BSL liabilities to other private sector. Net foreign assets of the BSL are defined as gross foreign exchange reserves (defined above) minus foreign liabilities. Foreign liabilities are defined as foreign currency-denominated liabilities of the BSL to nonresidents and the outstanding use of Fund credit. For program purposes, foreign liabilities exclude SDR allocation.

6. **Adjustment clauses.** The ceiling on changes in NDA of the BSL will be adjusted upward (downward) by the leone value of the shortfall (excess) in the external budgetary assistance at the test dates—the upward adjustment will be capped at the equivalent of US$20 million.

C. Net Domestic Bank Credit to the Central Government (NCG)

7. **Definition.** NCG refers to the net banking system's claims on the central government as calculated by the BSL. It is defined as follows:

- the net position of the government with commercial banks, including: (a) treasury bills; (b) treasury bearer bonds; and (c) loan and advances of commercial banks to the government; less government deposits in commercial banks;

- the net position of the government with the BSL, including: (a) treasury bills; (b) treasury bearer bonds, excluding holdings of special bonds provided by government to cover the BSL losses; (c) the stock of non-interest bearing non-marketable securities (NIBNMS); (d) the difference between converted NIBNMS into treasury bills and proceeds from their sales; and (e) ways and means; less (a) central government deposits; and (b) HIPC and MDRI relief deposits.

8. **Adjustment clauses.** The ceiling on changes in NCG will be adjusted (a) upward (downward) by up to the leone value of the shortfall (excess) in external budgetary assistance—the upward adjustment will be capped at the equivalent of US$20 million; (b) downward (upward) by the excess (shortfall) in the leone value of net issues of government securities to the nonbank private sector vis-à-vis the program assumption (as specified in the memorandum items in Table 3 of the MEFP).

9. **Data source**. The data source for the above will be the series "Claims on government (net)", submitted to the IMF staff and reconciled with the monthly monetary survey prepared by the BSL.

10. **Definition of Central government.** Central government is defined for the purposes of this memorandum to comprise the central government and those special accounts that are classified as central government in the BSL statement of accounts. The National Social Security and Insurance Trust and public enterprises are excluded from this definition of central government.

D. External Payment Arrears of the Public Sector

11. **Definition.** External payment arrears of the public sector are defined as the stock of new external overdue debt-service payments by the public sector. For the purposes of this PC, the public sector comprises the central government, regional government, all public enterprises and the BSL. The nonaccumulation of external arrears is a performance criterion during the program period. Excluded from this PC are those debts subject to rescheduling. This PC will apply on a continuous basis.

E. New Nonconcessional External Debt Contracted or Guaranteed by the Public Sector with an Original Maturity of One Year or More

12. **Definition**. Those are defined as all forms of new debt with original maturity of one year or more contracted or guaranteed by the public sector (see paragraph 11 for definition of public sector) based on the residency criterion. This PC applies not only to debt as defined in the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274 (00/85), August 24, 2000, Point 9, as revised on August 31, 2009, (Decision No. 14416-(09/91)) but also to commitments contracted or guaranteed for which value has not been received. Excluded from this PC are disbursements from the IMF and those debts subject to rescheduling. For the purposes of this PC, the "public sector" is as defined in ¶11 above. This PC will apply on a continuous basis.

13. Any external debt of which the net present value, calculated with the reference interest rates mentioned hereafter, is greater than 65 percent of the nominal value (grant element of less than 35 percent) is considered nonconcessional, with the exception of IMF lending. For debt with a maturity of more than 15 years, the average of the ten-year commercial interest reference rates (CIRRs) published by the OECD is used to calculate the grant element. The average of the six-month CIRRs is used for debt with shorter maturities. For loans in foreign currencies for which the OECD does not calculate a CIRR, calculation of the grant element should be based on the CIRR in SDRs. The Government will report any new external borrowing and its terms to Fund staff as soon as external debt is contracted or guaranteed by the government.

F. External Short-Term Debt Contracted or Guaranteed by the Public Sector

14. **Definition**. External short-term debt is defined as external debt stock with a maturity of less than one year contracted or guaranteed by the public sector (see paragraph 11 for definition of public sector). Debt is defined in Annex I of this TMU. For this purpose,

short-term debt will exclude normal trade credit for imports. For the purposes of this PC, the public sector is as defined in ¶11 above. This PC will apply on a continuous basis.

III. Quantitative Indicative target

A. Domestic Revenue of Central Government

15. **Definition**. The floor on total domestic central government revenue is defined as total central government revenue, as presented in the central government financial operations table, excluding external grants.

B. Poverty-Related Expenditures

16. **Definition**. Poverty-related expenditures refer to those expenditures in the areas identified in Table 2 of the Sierra Leone HIPC Decision Point Document.

IV. Program Monitoring

17. The Sierra Leonean authorities shall maintain a program-monitoring committee composed of senior officials from the MoFED, the BSL, and other relevant agencies. The committee shall be responsible for monitoring performance under the program, recommending policy responses, informing the IMF regularly about the progress of the program, and transmitting the supporting materials necessary for the evaluation of PCs and benchmarks. The committee will provide monthly reports to the IMF on progress in implementing the program's quantitative targets and structural benchmarks.

ANNEX 1: IMPLEMENTATION OF THE REVISED GUIDELINES ON PERFORMANCE CRITERIA WITH RESPECT TO FOREIGN DEBT

The term "debt" has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000, which reads as follows: "(a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property. (b) Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt". (c) Excluded from this performance criterion are normal import-related credits, disbursements from the IMF, and those debts subject to rescheduling arrangements."

Sierra Leone: Summary of Data to be Reported to IMF Staff

Type of Data	Tables	Frequency	Reporting Deadline
Real sector	National accounts	Annual	End of year + 9 months
	Revisions of national accounts	Variable	End of revision + 2 months
	Disaggregated consumer price index	Monthly	End of month + 2 weeks
Public finance	Net government position and details of nonbank financing, including the stock of the float, treasury bills, and bonds, as well as privatization receipts	Monthly	End of month + 6 weeks
	Government flow-of-funds table (Government Financial Operations Table) with supporting documentation (final) and presented on commitment and cash bases	Monthly	End of month + 6 weeks
	Petroleum product prices and tax receipts by categories of petroleum products	Monthly	End of month + 6 weeks
	Stock of outstanding payment commitments with a breakdown between current and capital expenditures	Monthly	End of month + 6 weeks
	Import duty exemptions by end-users and tariff regimes and estimates of corresponding revenue losses	Quarterly	End of quarter + 6 weeks
Monetary and financial data	Monetary survey	Monthly	End of month + 6 weeks
	Balance sheet of the BSL	Monthly	End of month + 6 weeks
	Consolidated balance sheets of commercial banks	Monthly	End of month + 6 weeks
	BSL monitoring sheet of net financing of the financial sector to the government	Monthly	End of month + 6 weeks
	BSL monitoring sheet of treasury bills and bonds holdings	Monthly	End of month + 6 weeks
	Borrowing and lending interest rates	Monthly	End of month + 6 weeks
	Results of foreign exchange and Treasury Bills auctions	Weekly	End of week + 3 days
	Stocks of government securities	Monthly	End of month + 6 weeks
	Banking supervision ratios	Quarterly	End of quarter + 8 weeks

Sierra Leone: Summary of Data to be Reported to IMF Staff (concluded)

Type of Data	Tables	Frequency	Reporting Deadline
Monetary and financial data			
	Gross official foreign reserves	Weekly	End of week + 1 week
	Foreign exchange cashflow table	Monthly	End of quarter + 4 weeks
	Revised balance of payments data	Monthly	When revisions occur
	Exports and imports of goods (including the volume of key minerals and fuels)	Monthly	End of month + 3 months
External debt	Outstanding external arrears and repayments (if applicable)	Monthly	End of month + 4 weeks
	Details of all new external borrowing and guarantees provided by government on new borrowing, including the associated concessionality calculation (percentage) for each new loan.	Monthly	End of month + 4 weeks
	External debt service payments (separately on principal and interest payment) to each creditor, including and excluding new disbursements in the debt recording system. Also, including and excluding HIPC relief.	Monthly	End of month + 4 weeks
HIPC initiative and MDRI monitoring	Statement of special account at the BSL, that receives resources generated by the HIPC Initiative and tracks their use	Monthly	End of month + 4 weeks
	Statement of special MDRI account at the BSL and the corresponding poverty-reducing spending financed	Monthly	End of month + 4 weeks
	Minutes of the meeting of the Monetary Policy Committee	Monthly	Date of meeting + 2 weeks

INTERNATIONAL MONETARY FUND AND
INTERNATIONAL DEVELOPMENT ASSOCIATION

SIERRA LEONE

Joint IMF/World Bank Debt Sustainability Analysis 2010

Prepared by the staffs of the International Monetary Fund and the International Development Association

Approved by Doris C. Ross and Dominique Desruelle (IMF) and Sudarshan Gooptu and Jan Walliser (World Bank)

November 18, 2010

Based on the low-income country (LIC) debt sustainability analysis (DSA), staff's assessment is that Sierra Leone's risk of debt distress remains moderate. Under baseline projections, all external debt indicators are below their indicative thresholds throughout the projection period (2010-30). Under the most extreme shock scenarios, however, the PV of debt to exports breaches its threshold significantly, the PV of debt to revenue breaches its threshold marginally, and the PV of debt to GDP ratio touches its threshold temporarily. Public sector debt dynamics remain on a stable path under the baseline scenario, but stress tests suggest that threats to debt sustainability remain. The analysis highlights the continued need for improved domestic revenue mobilization, the containment of low priority current expenditures, as well as growth and export-enhancing policies. Sierra Leone should continue to contract new external financing only in the form of grants and highly concessional loans and promote the development of a domestic debt market. The authorities agree with staff's assessment, highlighting the need for continued borrowing on highly concessional terms to meet the countries' large infrastructure investment needs, while stressing the importance of not unduly increasing the risk of debt distress.

I. Background

1. **This debt sustainability analysis (DSA) updates the DSA presented in December 2009 (IMF Country Report, No. 10/15)**. It was jointly conducted by the Fund and World Bank staffs in collaboration with the authorities.

2. **Sierra Leone reached the completion point under the enhanced HIPC Initiative and qualified for debt relief under the MDRI on December 15, 2006**. In January 2007, Paris Club creditors agreed to cancel outstanding claims.[1] Debt relief from the international

[1] Sierra Leone has received debt relief under HIPC and MDRI Initiatives from the IMF, IDA, AfDB, EIB, IFAD, BADEA, IDB, and OPEC Fund. Bilateral agreements have been signed with all Paris Club creditors. Agreements on the delivery of the HIPC relief are still pending with China, Kuwait, and Saudi Arabia.

community helped decrease Sierra Leone's public sector nominal external debt from about 142 percent of GDP at end-2005 to about 32 percent of GDP at end-2007.

3. **At end-2009, Sierra Leone's nominal public and publicly guaranteed external debt, including arrears, was estimated at US$692.6 million.**[2] About 57 percent of this debt is multilateral, 8 percent bilateral, and 35 percent commercial. The largest multilateral creditors are the World Bank Group (US$124 million), the African Development Bank (US$60 million) the Islamic Development Bank (US$47 million), and the IMF (US$72 million). Debt to commercial creditors consists of arrears accumulated before and during the civil war, which ended in 2002. The Sierra Leone government is making goodwill payments to some commercial creditors to avoid litigation. With World Bank assistance, the authorities are preparing for a debt-buy-back operation of eligible commercial debt by end-2011.

4. **Domestic debt amounted to 20 percent of GDP at end-2009**. Around 80 percent of outstanding domestic debt is in the form of treasury instruments. Commercial banks and other financial institutions accounted for about one half and the Bank of Sierra Leone one quarter of the holdings.

Comparison with the 2009 DSA
(averages in percent of current GDP unless indicated)

	2009	2010-14		2015-19		2020-24		2025-29	
	Actual	DSA09	DSA10	DSA09	DSA10	DSA09	DSA10	DSA09	DSA10
Stock of external debt (eop. US$ million)	692.6	778.4	835.0	1042.5	1114.2	1405.1	1495.2	1854.1	2020.5
Stock of external debt (eop.)	40.8	29.0	31.1	27.5	29.4	26.5	28.2	25.0	27.2
Debt service on external debt	1.4	2.1	2.3	3.6	4.1	4.3	4.7	6.5	6.4
Exports of goods and nonfactor services	17.5	19.1	21.9	20.9	24.1	24.1	26.3	26.9	29.0
Current account deficit	8.4	7.4	9.4	5.5	8.6	4.7	7.5	4.5	6.9
Domestic government revenue	11.7	12.0	13.8	12.4	16.4	12.2	19.4	11.5	21.3
Domestic debt	19.7	12.1	18.0	9.0	16.0	7.4	16.1	5.9	16.1
Real GDP growth (percent)	3.2	5.6	5.5	5.1	5.5	5.0	5.5	5.0	5.5

II. Underlying DSA Assumptions

5. **While Sierra Leone was negatively affected by the global economic downturn, the medium-term outlook remains relatively favorable.** Economic activity continued to decline in the first half of 2009 due to falling global demand and declining foreign inflows. Despite a pickup in exports of diamonds and agricultural products in the second half of 2009 and an increase in domestic food production, real GDP growth for the year as a whole slowed to 3.2 percent in 2009 compared with 5.5 percent in 2008. The external current account deficit is estimated to have declined to 8.4 percent of GDP in 2009 from 11.5 percent of GDP

[2] Public sector refers to central government and the nonfinancial public sector. This includes USD$240 million of unreconciled commercial debt for which a debt-buy-back operation is pending.

Box 1. Baseline Macroeconomic Assumptions Underlying the DSA

- Economic activity is projected to recover gradually with real GDP reaching 6 percent by 2012 and declining thereafter towards a steady state of 5.5 percent by 2018. Medium- to long-term growth is predicated on the government's ongoing policies to consolidate macroeconomic stabilization, expand basic public infrastructure, and improve the business environment for private sector development.
- Monetary and exchange rate policies will aim to bring 12-month (end of period CPI) inflation down to 8 percent at end-2012, from a projected inflation of 16 percent at end-2010, and to a steady state of 5.4 percent by 2016. The projection reflects the WEO assumptions on the prices of the main commodities, as well as the authorities' commitment to refrain from central bank financing and to strengthen central bank capacity in conducting monetary policy.
- Exports are expected to benefit from a projected increase in commodity prices, expansion in mining capacity, and increased investment in agriculture. Exports of goods and services are projected to gradually increase from about 18 percent of GDP in 2009 to 31 percent by 2030. Imports of goods and services are projected to gradually increase from about 31 percent of GDP in 2009 to 40 percent in 2030.
- The new GST together with ongoing strengthening and modernization of customs and tax administration is expected to gradually broaden the tax base, raising domestic revenue from 11.8 percent of GDP in 2009 to 14.5 percent by 2012 and gradually to 22.5 percent by 2030. Current expenditures are projected to gradually increase from 15 percent to 19.5 percent of GDP by 2030, while public capital expenditures are expected to gradually increase from 7 percent of GDP in 2009 to 12 percent by 2030 in order to address the substantial infrastructure needs of the country. The overall fiscal deficit, including grants, is projected to slightly increase from 3.2 percent of GDP in 2009 to 3.5 percent by 2030.
- Total donor assistance, including grants and concessional loans, is expected to decline from the current level of 10 percent of GDP to 8 percent of GDP in the medium term. Budget support is projected to decline gradually from 5.2 percent of GDP in 2009 to 0.6 percent by 2030.
- It is assumed that about US$240 million of unreconciled commercial debt would be eligible for the World Bank assisted debt buy-back operation in 2011.
- Domestic debt is expected to decline gradually from 19 percent of GDP in 2009 to 16 percent in 2030, as the government refrains from central bank borrowing and limits issuance of new securities. In the outer years, domestic debt in percent of GDP is projected to be significantly higher than envisaged under the 2009 DSA because of higher annual fiscal deficits reflecting investment in infrastructure and social services. Domestic debt includes treasury bills, treasury bearer bonds, non-interest bearing bonds, recapitalization bond, ways and means advances, and domestic arrears.

in 2008, reflecting an increase in official transfers and weak imports. After a long period of stability, the leone depreciated against the US dollar by about 25 percent in 2009, mostly reflecting weaker inflows from exports. The medium-term outlook is, however, favorable for Sierra Leone. Economic growth will benefit from the recent completion of the Bumbuna power station, investment in basic infrastructure, initiatives to improve the business climate and raise agricultural productivity, and continued macroeconomic stability. This should support a recovery of real GDP growth to 4.5 percent in 2011 and to 6 percent in 2012. An expected recovery in export demand for minerals and cash crops should contribute to exchange rate stability. Monetary and exchange rate policies will aim to bring 12-month CPI inflation down to 8 percent at end-2012 from a projected inflation of 16 percent at end-2010. The baseline macroeconomic assumptions underlying this DSA are summarized in Box 1.[3]

III. External Debt Sustainability

A. Baseline

6. **Under the baseline scenario, the debt indicators are projected to remain below the corresponding thresholds throughout the projection period**. The PV of debt-to-GDP ratio would remain in the range of 19-22 percent throughout.[4] The PV of external debt to exports is projected to decline from 108 percent in 2009 to 95 percent in 2015, 79 percent by 2020, and 63 percent in 2030. The PV of debt-to-revenue ratio declines from a peak of 159 in 2009 to 87 by 2030, below its 200 percent threshold. The ratios of debt-service-to exports and debt-service-to-revenue remains well below their thresholds throughout the projection period (Table 1).[5]

B. Alternative Scenarios and Stress Tests

7. **The alternative scenarios highlight the need for maintaining prudent external debt management and refraining from non-concessional borrowing**. Under an alternative scenario that assumes less favorable borrowing terms, the PV of debt-to-exports ratio breached the indicative thresholds (A2, Table 2a). It would therefore be important to pursue a prudent external debt management policy, relying mostly on grants and highly concessional loans. The government has expressed interest in technical assistance from the Bank and the Fund on developing a Medium Term Debt Management Strategy (MTDS).

8. **Under the standard stress tests, public debt ratios are sensitive to an export shock and a one-time real depreciation of 30 percent in 2011**. These highlight the vulnerability of the economy to adverse external developments. Notably the analysis shows

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[3] The impact of two new iron ore projects is not reflected in the baseline because of limited information.

[4] Sierra Leone remains rated as a weak performer with regard to its policies and institutions with an average 2007–09 Country Policy and Institutional Assessment (CPIA) rating of 3.14. As a poor performer, the debt and debt service thresholds under the joint IMF-WB DSA framework for LICs applied to Sierra Leone are: (i) 100 percent for Present Value (PV) of debt-to-exports; (ii) 30 percent for PV of debt-to-GDP; and (iii) 200 percent for PV of debt-to-revenue. The relevant debt service thresholds are (i) 15 percent of exports; and (ii) 25 percent of revenues.

[5] While the nominal value of public debt includes USD$240 million of unreconciled commercial debt for which a debt-buy-back operation is pending in 2011, the present value calculation includes 10 percent of this nominal debt stock, reflecting the expected payments in the debt-buy-back. It should be noted, however, that all the external debt thresholds would be breached temporarily in 2010 in the case of treating the full amount at face value in the present value calculation prior to the debt buy-back in 2011.

that the debt-to-exports ratio is particularly sensitive to export shocks. Under the most extreme bound test of a one standard deviation export shock (B2), the PV of debt-to-exports-ratio would reach 159 percent of exports in 2012, gradually declining to 89 percent in 2030.[6] A combination shock (B5), which reduces growth in exports, real GDP, net FDI inflows, and the GDP deflator in U.S. dollar terms by half a standard deviation, would also breach the threshold, but to a lesser degree. The most extreme stress test for the debt-to-GDP and debt-to-revenue indicators represents a one-time 30 percent real exchange rate depreciation relative to the baseline in 2011. This results in a temporary breach of the indicative threshold of the debt to revenue indicator, while the threshold is touched but not breached in the case of the debt-to-GDP ratio. Finally, none of the stress tests for the liquidity indicators breach their corresponding thresholds. Overall, however, the tests underscore the importance of strengthening the environment for economic growth and export oriented policies, including continuing infrastructure investment and financial deepening.

IV. Fiscal Debt Sustainability

A. Baseline

9. **Under the baseline, Sierra Leone's total public debt burden (including domestic debt) is expected to stabilize over the projection period**.[7] The baseline macroeconomic scenario assumes a marginal and gradual reduction in domestic financing relative to GDP. With moderate domestic financing, domestic debt is expected to decline from 19 percent of GDP in 2009 to 16 percent by 2030. This trend helps offset the increase in external debt, so that the public debt-to-GDP ratio would decline from 60 percent of GDP in 2009 to 44 percent by 2030. While a lower relative accumulation of domestic debt is a positive development, there is a need to develop a more competitive domestic debt market that could result in lower nominal and real interest rates and longer maturities (Table 3).

B. Alternative Scenarios and Stress Tests

10. **In order to avoid unfavorable developments in public debt dynamics, the primary fiscal deficit needs to be contained going forward.** Under an alternative scenario assuming an unchanged primary balance from 2010, the PV of debt-to-GDP ratio would moderately increase after 2020, compared to the baseline during the projection period. This underscores the importance of improving domestic revenue mobilization and containing non-priority current expenditures (Table 4). Under bound tests, a one standard deviation growth shock in 2011-12, and a one-time 30 percent depreciation, would moderately increase the corresponding PV of debt ratios.

[6] Due to large fluctuations in the economic data following the end of the civil war in 2002, stress tests and alternative scenarios have been calibrated to use a 5-year historical period.

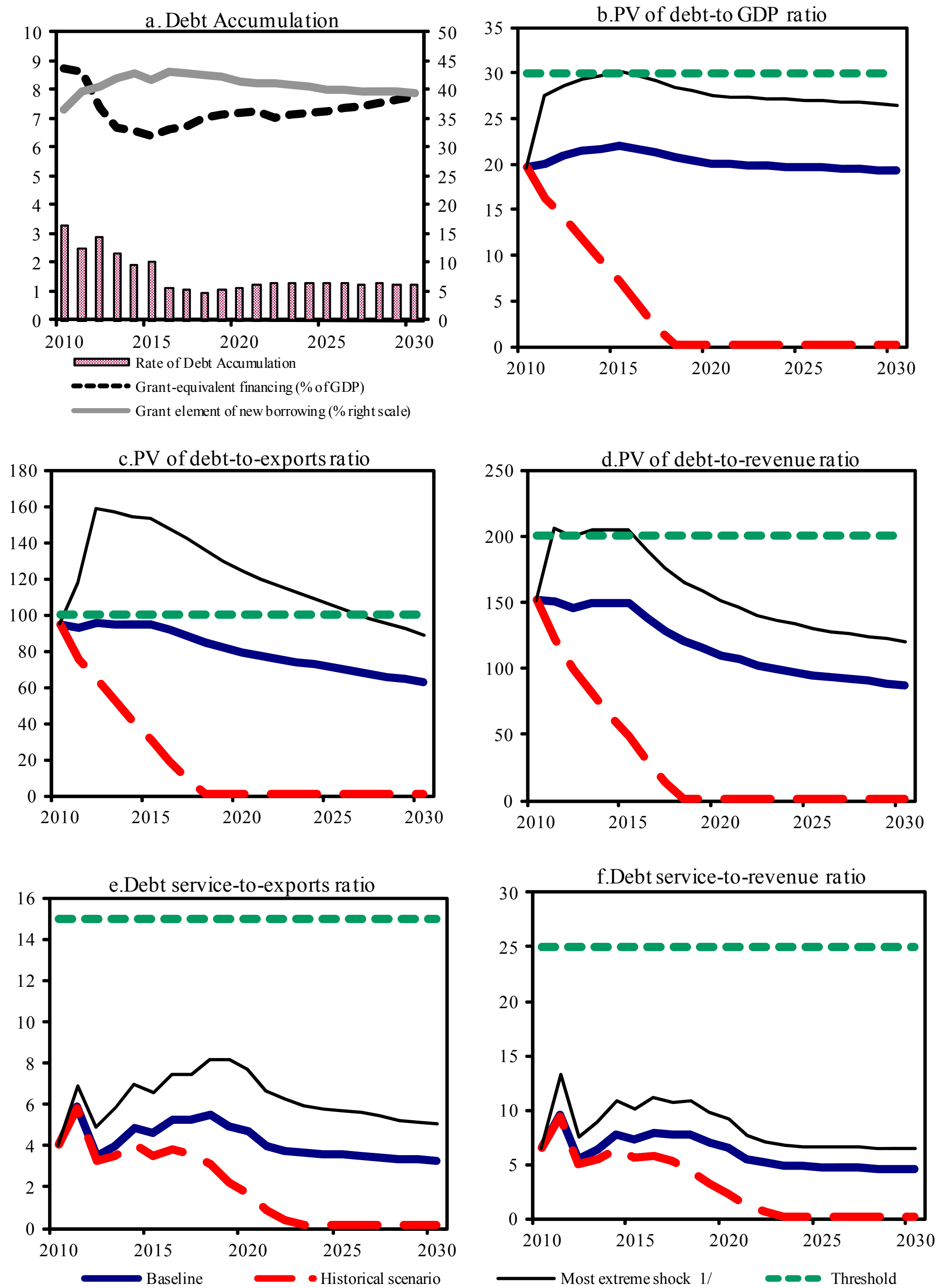
[7] Public debt reflects current and committed government obligations.

V. DEBT DISTRESS CLASSIFICATION AND CONCLUSIONS

11. **Based on the LIC-DSA framework, Sierra Leone remains at moderate risk of external debt distress.** Under the baseline scenario, debt indicators are below the indicative, country-specific policy dependent thresholds. Stress tests reveal that Sierra Leone's external debt trajectory is still vulnerable to shocks affecting its external sector. The evolution of external debt critically hinges on policies aimed at boosting growth and diversifying the export base, while continuing to access grants and highly concessional loans.

12. **Although domestic debt is projected to decline significantly over time relative to GDP, it does not affect the overall assessment.** A slowdown in domestic debt accumulation does, however, lessen liquidity and rollover risks associated with its short maturities. Stress tests underline the importance of improving domestic revenue mobilization and containing non-priority expenditures. Policies should aim at developing the domestic debt market.

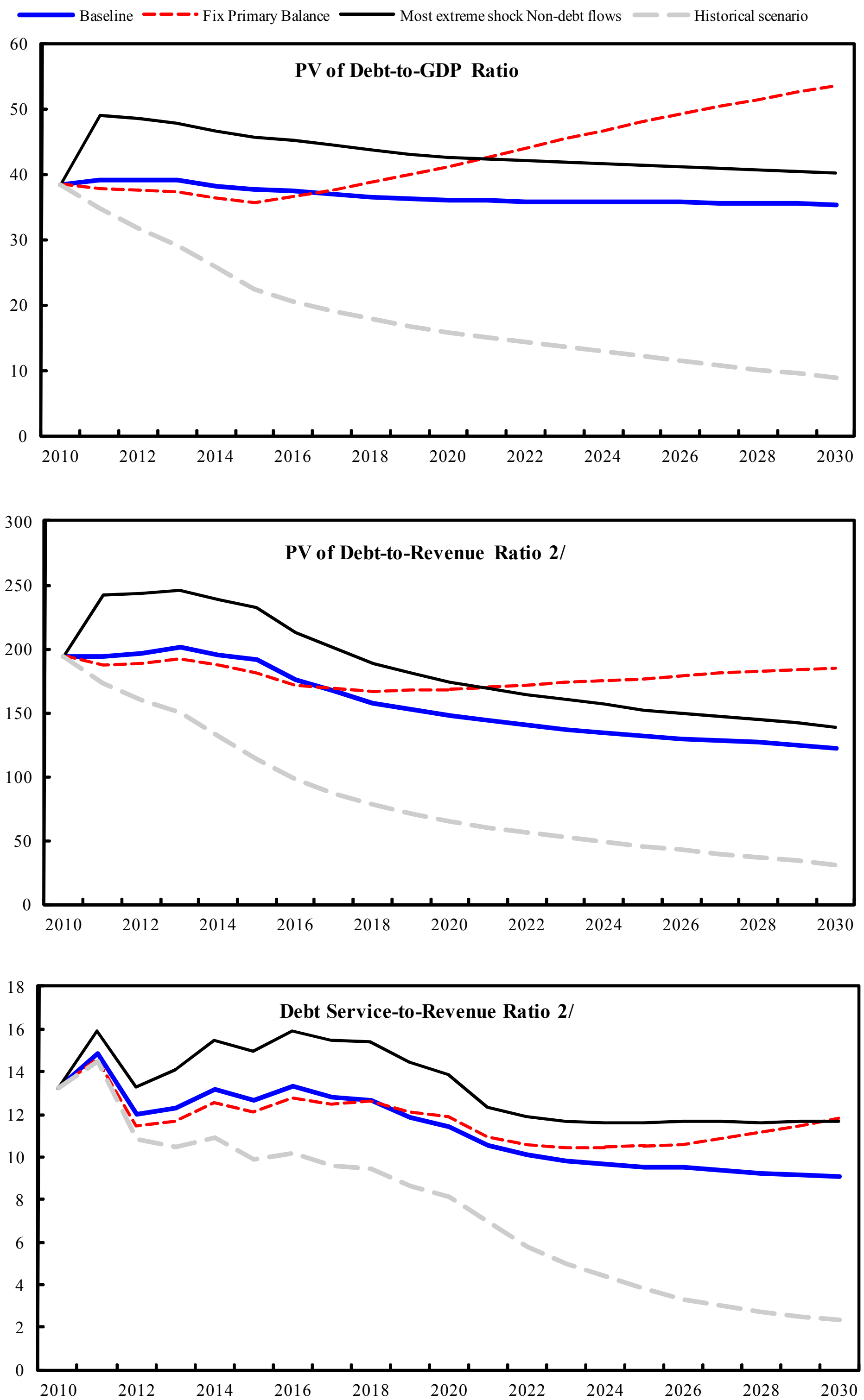
Figure 1. Sierra Leone: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2010-2030 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2020. In figure b. it corresponds to a One-time depreciation shock; in c. to a Exports shock; in d. to a One-time depreciation shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

Figure 2.Sierra Leone: Indicators of Public Debt Under Alternative Scenarios, 2010-2030 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2020.
2/ Revenues are defined inclusive of grants.

Table 1.: External Debt Sustainability Framework, Baseline Scenario, 2007-2030 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average	Standard Deviation	Projections									
	2007	2008	2009			2010	2011	2012	2013	2014	2015	2010-15 Average	2020	2030	2016-30 Average
External debt (nominal) 1/	**31.7**	**31.8**	**40.8**			**40.4**	**29.6**	**30.9**	**31.8**	**32.3**	**33.0**		**30.3**	**28.0**	
o/w public and publicly guaranteed (PPG)	31.7	31.8	40.8			40.4	29.6	30.9	31.8	32.3	33.0		30.3	28.0	
Change in external debt	-78.6	0.0	9.0			-0.4	-10.8	1.3	0.9	0.5	0.7		-0.5	-0.3	
Identified net debt-creating flows	-16.2	4.0	6.1			5.5	5.4	5.3	5.0	4.8	4.9		3.8	2.5	
Non-interest current account deficit	**5.1**	**11.3**	**8.2**	**4.9**	**3.6**	**9.3**	**9.3**	**9.3**	**9.0**	**8.9**	**8.8**		**7.7**	**6.3**	7.3
Deficit in balance of goods and services	9.0	13.3	13.5			13.9	12.5	12.2	11.9	11.6	11.4		9.9	9.0	
Exports	19.7	17.2	17.5			20.7	21.5	22.0	22.5	22.9	23.3		25.3	30.8	
Imports	28.7	30.5	30.9			34.6	34.0	34.2	34.4	34.5	34.7		35.3	39.7	
Net current transfers (negative = inflow)	-5.7	-5.7	-7.0	-10.4	4.7	-5.9	-4.6	-4.3	-4.1	-4.0	-3.8		-3.5	-3.0	-3.3
o/w official	-3.5	-4.0	-4.5			-3.4	-2.1	-1.8	-1.6	-1.5	-1.3		-1.0	-0.5	
Other current account flows (negative = net inflow)	1.8	3.6	1.7			1.4	1.4	1.3	1.3	1.3	1.3		1.2	0.3	
Net FDI (negative = inflow)	**-5.8**	**-3.0**	**-4.0**	**-4.0**	**2.3**	**-2.4**	**-2.3**	**-2.6**	**-2.6**	**-2.6**	**-2.6**		**-2.6**	**-2.6**	-2.6
Endogenous debt dynamics 2/	**-15.6**	**-4.3**	**1.9**			**-1.5**	**-1.6**	**-1.4**	**-1.5**	**-1.5**	**-1.4**		**-1.4**	**-1.2**	
Contribution from nominal interest rate	0.4	0.4	0.3			0.3	0.3	0.2	0.2	0.2	0.2		0.2	0.2	
Contribution from real GDP growth	-6.1	-1.5	-1.1			-1.8	-1.9	-1.6	-1.7	-1.8	-1.7		-1.6	-1.5	
Contribution from price and exchange rate changes	-9.9	-3.2	2.7			…	…	…	…	…	…		…	…	
Residual (3-4) 3/	**-62.4**	**-3.9**	**2.9**			**-5.8**	**-16.2**	**-4.0**	**-4.1**	**-4.4**	**-4.1**		**-4.3**	**-2.8**	
o/w exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	18.7			19.7	20.0	20.9	21.4	21.6	22.0		20.1	19.2	
In percent of exports	...	...	107.4			94.8	93.1	95.0	95.0	94.3	94.6		79.2	62.6	
PV of PPG external debt	**...**	**...**	**18.7**			**19.7**	**20.0**	**20.9**	**21.4**	**21.6**	**22.0**		**20.1**	**19.2**	
In percent of exports	**...**	**...**	**107.4**			**94.8**	**93.1**	**95.0**	**95.0**	**94.3**	**94.6**		**79.2**	**62.6**	
In percent of government revenues	**...**	**...**	**158.4**			**151.3**	**150.1**	**145.9**	**149.1**	**148.8**	**148.6**		**109.8**	**87.3**	
Debt service-to-exports ratio (in percent)	**8.3**	**3.2**	**4.3**			**4.0**	**5.9**	**3.5**	**4.0**	**4.9**	**4.6**		**4.7**	**3.3**	
PPG debt service-to-exports ratio (in percent)	**8.3**	**3.2**	**4.3**			**4.0**	**5.9**	**3.5**	**4.0**	**4.9**	**4.6**		**4.7**	**3.3**	
PPG debt service-to-revenue ratio (in percent)	**15.0**	**4.7**	**6.4**			**6.4**	**9.5**	**5.4**	**6.3**	**7.7**	**7.2**		**6.5**	**4.6**	
Total gross financing need (Billions of U.S. dollars)	0.3	0.4	0.3			0.4	0.4	0.2	0.2	0.2	0.2		0.3	0.4	
Non-interest current account deficit that stabilizes debt ratio	83.7	11.2	-0.8			9.7	20.2	7.9	8.1	8.5	8.1		8.2	6.6	
Key macroeconomic assumptions															
Real GDP growth (in percent)	6.4	5.5	3.2	6.6	1.9	4.5	5.2	6.0	6.0	6.0	5.5	5.5	5.5	5.5	5.5
GDP deflator in US dollar terms (change in percent)	9.8	11.2	-7.8	3.7	7.4	-1.7	5.3	4.2	2.2	2.1	1.5	2.3	1.4	1.4	1.4
Effective interest rate (percent) 5/	0.4	1.3	0.9	1.2	0.7	0.8	0.7	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Growth of exports of G&S (US dollar terms, in percent)	3.4	2.3	-3.4	10.9	14.5	22.0	14.8	12.9	11.3	9.9	8.8	13.3	8.9	9.2	9.0
Growth of imports of G&S (US dollar terms, in percent)	5.0	24.5	-3.6	8.7	13.9	14.9	9.0	11.0	9.0	8.5	7.5	10.0	7.4	8.5	8.0
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	36.7	39.6	40.4	42.0	42.9	41.8	40.6	41.4	39.5	41.0
Government revenues (excluding grants, in percent of GDP)	10.9	11.5	11.8			13.0	13.3	14.3	14.4	14.5	14.8		18.3	22.0	19.5
Aid flows (in Billions of US dollars) 7/	0.1	0.1	0.2			0.2	0.2	0.2	0.2	0.2	0.3		0.4	0.7	
o/w Grants	0.1	0.1	0.1			0.1	0.1	0.1	0.1	0.1	0.1		0.3	0.6	
o/w Concessional loans	0.0	0.1	0.1			0.1	0.1	0.1	0.1	0.1	0.1		0.1	0.2	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			8.8	8.6	7.4	6.7	6.6	6.4		7.2	7.8	7.2
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			72.1	75.6	73.4	74.5	75.5	74.7		83.0	84.4	83.2
Memorandum items:															
Nominal GDP (Billions of US dollars)	1.7	2.0	1.9			1.9	2.1	2.3	2.5	2.7	2.9		4.1	8.1	
Nominal dollar GDP growth	16.9	17.3	-4.9			2.7	10.8	10.5	8.3	8.2	7.1	7.9	7.0	7.0	7.0
PV of PPG external debt (in Billions of US dollars)			0.3			0.4	0.4	0.5	0.5	0.6	0.6		0.8	1.5	
(PVt-PVt-1)/GDPt-1 (in percent)						3.3	2.5	2.9	2.3	1.9	2.0	2.5	1.1	1.2	1.2
Gross remittances (Billions of US dollars)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.1	0.1	
PV of PPG external debt (in percent of GDP + remittances)	...	...	18.4			19.3	19.7	20.5	21.1	21.2	21.7		19.7	18.9	
PV of PPG external debt (in percent of exports + remittances)	...	...	98.0			87.7	86.4	88.3	88.4	87.9	88.3		74.3	59.4	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	4.0			3.7	5.5	3.3	3.7	4.6	4.3		4.4	3.1	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes project grants (3 and 4 percent of GDP annually), exceptional financing (changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exch. rate changes. The large residual in 2007 includes HIPC relief and in 2011 the pending debt buyback.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are derived over the past 5 years due to large fluctuations in the post-conflict economic data.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2a.Sierra Leone: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010-2030
(In percent)

	Projections							
	2010	2011	2012	2013	2014	2015	**2020**	2030
PV of debt-to GDP ratio								
Baseline	20	20	21	21	22	22	**20**	19
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	20	16	14	12	9	7	**-2**	-3
A2. New public sector loans on less favorable terms in 2010-2030 2	20	21	23	24	25	27	**27**	29
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	20	20	21	22	22	22	**20**	19
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	20	22	26	26	26	26	**23**	20
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	20	21	23	24	24	25	**23**	22
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	20	19	19	19	20	20	**19**	19
B5. Combination of B1-B4 using one-half standard deviation shocks	20	20	22	23	23	24	**21**	20
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	20	27	29	29	30	30	**28**	26
PV of debt-to-exports ratio								
Baseline	95	93	95	95	94	95	**79**	63
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	95	76	65	52	41	31	**-10**	-10
A2. New public sector loans on less favorable terms in 2010-2030 2	95	97	103	107	110	114	**107**	95
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	95	91	93	93	92	93	**78**	62
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	95	118	159	157	154	154	**124**	89
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	95	91	93	93	92	93	**78**	62
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	95	87	85	86	86	87	**74**	60
B5. Combination of B1-B4 using one-half standard deviation shocks	95	101	120	119	119	119	**99**	78
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	95	91	93	93	92	93	**78**	62
PV of debt-to-revenue ratio								
Baseline	151	150	146	149	149	149	**110**	87
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2010-2030 1/	151	122	99	82	65	49	**-13**	-15
A2. New public sector loans on less favorable terms in 2010-2030 2	151	156	158	168	174	179	**149**	133
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	151	149	146	150	150	150	**111**	88
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	151	162	179	181	179	177	**127**	91
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	151	159	163	167	167	167	**124**	98
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	151	141	131	135	135	136	**102**	84
B5. Combination of B1-B4 using one-half standard deviation shocks	151	149	157	160	160	160	**118**	92
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	151	206	200	204	204	204	**151**	120

Table 2b.Sierra Leone: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2010-2030 (continued)
(In percent)

	2010	2011	2012	2013	2014	2015	2020	2030
Debt service-to-exports ratio								
Baseline	4	6	4	4	5	5	**5**	3
A. Alternative Scenarios								
A2. New public sector loans on less favorable terms in 2010-2030 2	4	6	4	5	6	6	**6**	6
A3. Alternative Scenario :[Costumize, enter title]	4	6	4	4	5	5	**4**	0
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	4	6	4	4	5	5	**5**	3
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	4	7	5	6	7	7	**8**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	4	6	4	4	5	5	**5**	3
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	4	6	3	4	5	5	**4**	3
B5. Combination of B1-B4 using one-half standard deviation shocks	4	7	4	5	6	6	**6**	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	4	6	4	4	5	5	**5**	3
Debt service-to-revenue ratio								
Baseline	6	9	5	6	8	7	**7**	5
A. Alternative Scenarios								
A2. New public sector loans on less favorable terms in 2010-2030 2	6	9	6	7	9	9	**8**	8
A3. Alternative Scenario :[Costumize, enter title]	6	10	6	7	8	8	**5**	0
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2011-2012	6	10	6	6	8	7	**7**	5
B2. Export value growth at historical average minus one standard deviation in 2011-2012 3/	6	9	6	7	8	8	**8**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2011-2012	6	10	6	7	9	8	**7**	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2011-2012 4/	6	9	5	6	8	7	**6**	4
B5. Combination of B1-B4 using one-half standard deviation shocks	6	10	6	7	8	8	**7**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2011 5/	6	13	8	9	11	10	**9**	6
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	40	40	40	40	40	40	**40**	40

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 3.Sierra Leone: Public Sector Debt Sustainability Framework, Baseline Scenario, 2007-2030
(In percent of GDP, unless otherwise indicated)

	Actual			Average	Standard Deviation	Estimate					Projections				
	2007	2008	2009			2010	2011	2012	2013	2014	2015	2010-15 Average	2020	2030	2016-30 Average
Public sector debt 1/	55.2	53.7	60.4			59.2	48.5	49.2	49.4	48.9	48.7		46.2	44.1	
o/w foreign-currency denominated	31.7	32.9	41.6			40.9	29.9	31.0	31.8	32.3	33.0		30.3	28.0	
Change in public sector debt	-81.5	-1.5	6.7			-1.3	-10.6	0.6	0.2	-0.5	-0.2		-0.4	-0.2	
Identified debt-creating flows	-19.6	-3.3	6.6			-4.0	-1.3	-0.2	0.0	0.0	0.8		-0.6	-0.4	
Primary deficit	-0.4	2.6	1.6	0.1	2.2	2.7	3.8	3.2	2.7	2.7	3.0	3.0	1.0	1.1	1.1
Revenue and grants	15.7	16.0	19.7			19.8	20.1	19.9	19.4	19.5	19.6		24.4	28.9	
of which: grants	4.8	4.5	7.9			6.8	6.8	5.6	5.0	5.0	4.8		6.1	6.8	
Primary (noninterest) expenditure	15.3	18.7	21.4			22.5	23.9	23.0	22.1	22.2	22.6		25.5	30.0	
Automatic debt dynamics	-18.2	-5.3	5.5			-6.3	-4.2	-3.1	-2.7	-2.7	-2.2		-1.7	-1.5	
Contribution from interest rate/growth differential	-11.3	-3.5	-1.3			-3.2	-2.7	-2.5	-2.5	-2.5	-2.2		-1.8	-1.6	
of which: contribution from average real interest rate	-3.0	-0.6	0.4			-0.6	0.2	0.3	0.3	0.3	0.3		0.6	0.7	
of which: contribution from real GDP growth	-8.3	-2.9	-1.7			-2.6	-2.9	-2.7	-2.8	-2.8	-2.5		-2.4	-2.3	
Contribution from real exchange rate depreciation	-6.9	-1.8	6.8			-3.1	-1.5	-0.6	-0.2	-0.2	0.0		...	...	
Other identified debt-creating flows	-1.0	-0.6	-0.5			-0.4	-0.8	-0.2	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	-0.1	-0.1	-0.2			-0.1	-0.6	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	-0.9	-0.5	-0.4			-0.3	-0.2	-0.2	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-61.9	1.8	0.1			2.7	-9.3	0.8	0.2	-0.6	-1.0		0.2	0.2	
Other Sustainability Indicators															
PV of public sector debt	23.5	22.0	38.4			38.4	39.0	39.1	39.0	38.2	37.7		35.9	35.3	
o/w foreign-currency denominated	0.0	1.2	19.6			20.2	20.3	20.9	21.4	21.6	22.0		20.1	19.2	
o/w external	...	...	18.7			19.7	20.0	20.9	21.4	21.6	22.0		20.1	19.2	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	17.5	17.1	17.0			16.8	17.1	5.6	5.1	5.3	5.5		3.8	3.7	
PV of public sector debt-to-revenue and grants ratio (in percent)	149.2	137.0	194.5			194.0	193.5	196.8	200.7	195.7	191.9		147.1	122.4	
PV of public sector debt-to-revenue ratio (in percent)	215.0	191.1	324.4			295.6	292.4	273.5	271.2	262.9	254.6		196.6	160.4	
o/w external 3/	…	…	158.4			151.3	150.1	145.9	149.1	148.8	148.6		109.8	87.3	
Debt service-to-revenue and grants ratio (in percent) 4/	22.8	15.0	10.9			13.2	14.9	12.0	12.3	13.2	12.7		11.4	9.1	
Debt service-to-revenue ratio (in percent) 4/	32.8	21.0	18.3			20.1	22.5	16.7	16.7	17.7	16.8		15.2	11.9	
Primary deficit that stabilizes the debt-to-GDP ratio	81.1	4.1	-5.1			4.0	14.4	2.5	2.5	3.3	3.1		1.5	1.4	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	6.4	5.5	3.2	6.6	1.9	4.5	5.2	6.0	6.0	6.0	5.5	5.5	5.5	5.5	5.5
Average nominal interest rate on forex debt (in percent)	0.4	1.3	0.8	1.2	0.7	0.7	0.7	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Average real interest rate on domestic debt (in percent)	-1.8	-1.6	1.9	-2.1	2.3	-3.1	2.2	2.4	2.8	3.2	4.2	1.9	6.3	6.3	6.3
Real exchange rate depreciation (in percent, + indicates depreciation)	-6.8	-6.1	21.5	0.7	11.1	-7.9	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	10.6	11.1	5.3	10.9	3.5	15.0	8.5	7.3	6.3	6.0	5.1	8.0	4.5	4.5	4.5
Growth of real primary spending (deflated by GDP deflator, in percer	-0.1	0.3	0.2	0.1	0.1	0.1	0.1	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Grant element of new external borrowing (in percent)	...	...	...	…	…	36.7	39.6	40.4	42.0	42.9	41.8	40.6	41.4	39.5	...

Sources: Country authorities; and staff estimates and projections.
1/ Public sector refers to central government and nonfinancial public sector.
2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
3/ Revenues excluding grants.
4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.
5/ Historical averages and standard deviations are derived over the past 5 years due to large fluctuations in the post-conflict economic data.

Table 4.Sierra Leone: Sensitivity Analysis for Key Indicators of Public Debt 2010-2030

	Projections							
	2010	2011	2012	2013	2014	2015	2020	2030
PV of Debt-to-GDP Ratio								
Baseline	38	39	39	39	38	38	36	35
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	38	35	32	29	26	22	16	9
A2. Primary balance is unchanged from 2010	38	38	37	37	36	36	41	54
A3. Permanently lower GDP growth 1/	38	39	39	39	39	39	39	50
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	38	39	40	40	40	40	40	43
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	38	37	36	36	35	35	33	33
B3. Combination of B1-B2 using one half standard deviation shocks	38	36	34	35	34	34	33	35
B4. One-time 30 percent real depreciation in 2011	38	51	49	48	46	45	41	40
B5. 10 percent of GDP increase in other debt-creating flows in 2011	38	49	48	48	46	46	43	40
PV of Debt-to-Revenue Ratio 2/								
Baseline	194	194	197	201	196	192	147	122
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	194	173	160	149	132	114	65	31
A2. Primary balance is unchanged from 2010	194	188	188	192	187	182	168	185
A3. Permanently lower GDP growth 1/	194	194	197	202	198	196	160	170
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	194	195	202	207	203	201	161	148
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	194	185	183	186	181	178	136	114
B3. Combination of B1-B2 using one half standard deviation shocks	194	179	173	177	174	171	135	120
B4. One-time 30 percent real depreciation in 2011	194	254	249	247	236	227	168	138
B5. 10 percent of GDP increase in other debt-creating flows in 2011	194	242	243	246	238	233	174	139
Debt Service-to-Revenue Ratio 2/								
Baseline	13	15	12	12	13	13	11	9
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	13	15	11	10	11	10	8	2
A2. Primary balance is unchanged from 2010	13	15	11	12	13	12	12	12
A3. Permanently lower GDP growth 1/	13	15	12	12	13	13	12	11
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2011-2012	13	15	12	12	13	13	12	10
B2. Primary balance is at historical average minus one standard deviations in 2011-2012	13	15	11	11	12	12	11	8
B3. Combination of B1-B2 using one half standard deviation shocks	13	15	11	11	12	12	11	8
B4. One-time 30 percent real depreciation in 2011	13	16	13	14	16	15	14	12
B5. 10 percent of GDP increase in other debt-creating flows in 2011	13	15	13	14	15	14	12	11

Sources: Country authorities; and staff estimates and projections.
1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.
2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND

SIERRA LEONE

Staff Report for the 2010 Article IV Consultation, First Review Under the Three-Year Arrangement Under the Extended Credit Facility, Request for Modification of Performance Criterion, and Financing Assurances Review—Informational Annex

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

November 18, 2010

Contents Page

Appendix I. Relations with the Fund
(As of September 30, 2010)

I. Membership Status: Joined 9/10/62; Article VIII

II. General Resources Account:	**SDR Million**	**% Quota**
Quota	103.70	100.00
Fund holdings of currency	103.69	99.99
Reserve position	0.02	0.02

III. SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	99.51	100.00
Holdings	120.97	121.57

IV. Outstanding Purchases and Loans:	**SDR Million**	**% Quota**
ECF Arrangements	70.32	67.81

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF	Jul 01, 2010	Jun 30, 2013	31.11	4.44
ECF	May 10, 2006	Jun 22, 2010	51.88	51.88
ECF	Sep 26, 2001	Jun 25, 2005	130.84	130.84

VI. Projected Payments to Fund[1]
(SDR million; based on current use of resources and present holdings of SDRs):

	Forthcoming				
	2010	2011	2012	2013	2014
Principal	1.40	3.27	4.62	4.62	8.12
Charges/interest		0.00	0.16	0.15	0.14
Total	1.40	3.27	4.78	4.77	8.26

VII. Implementation of HIPC Initiative

	Enhanced Framework
Commitment of HIPC Initiative assistance	
Decision point date	March 2002
Assistance committed (NPV terms)	

[1] When a member has overdue financial obligations outstanding for more than three months, the amount will be shown in this section.

By all creditors (US$ million)[2]	675.20
Of which: IMF assistance (US$ million)	125.21
(SDR equivalent in millions)	100.00
Completion point date	December 2006

Disbursement of IMF assistance (SDR million)	
Amount disbursed	100.00
Interim assistance	66.03
Completion point balance	33.97
Additional disbursement of interest income [3]	6.58
Total disbursements	106.58

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

I. MDRI-eligible debt (SDR Million) [4]	117.34
Financed by: MDRI Trust	76.75
Remaining HIPC resources	40.59

II. Debt Relief by facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGT**	**Total**
December 2006	N/A	117.34	117.34

IX. Safeguards Assessment

Pursuant to IMF policy, the Bank of Sierra Leone was subject to a safeguards assessment with respect to the ECF arrangement approved on May 10, 2006. The assessment, which was completed on June 12, 2006, proposed recommendations to address new and continuing vulnerabilities in financial reporting, internal audits, and internal controls. Updates of the 2006 safeguards assessment report were completed in October 09 and November 2010. The most recent update finds that the BSL maintains important elements of the safeguards framework; financial statements are prepared and audited in accordance with international standards and are published in a timely manner. However, financial safeguards need to be

[2] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

[3] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim.

[4] 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 2004 that remains outstanding at the time the member qualifies for debt relief.

improved in other areas. External auditors need to be selected and appointed in a timely manner, based on well-established criteria, and should be appointed for a multi-year term instead of the current practice of annual appointments. The audit committee should monitor timely implementation of recommendations arising from external and internal audits and safeguards assessments.

X. Exchange Rate Arrangement

For customs valuation purposes and for official transactions, the Bank of Sierra Leone (BSL) calculates an official exchange rate every Friday morning as the weighted average of the auction rate, the commercial bank mid-rate, and the bureau mid-rate in the previous week. Commercial banks may buy foreign exchange from and sell it to individual customers and may trade among themselves or with the BSL on a freely negotiable basis. As of October 14, 2010, the BSL mid-rate was Le 4,109.30=US$1.

Sierra Leone's *de jure* exchange rate regime is classified as floating, with the value of the leone determined by the market. Furthermore, effective November 1, 2008, the *de facto* exchange rate arrangement has been reclassified to 'floating' from a 'stabilized arrangement'.

Effective February 2, 2009, the *de facto* exchange rate arrangement was reclassified from a conventional pegged arrangement to a "stabilized arrangement" retroactively to April 30, 2008, due to a revision of the classification methodology. In March 2008, the exchange rate regime was reclassified as "a conventional peg" to reflect the nominal stability of exchange rate developments under *de facto* management through the auction by the BSL as the only seller of foreign exchange.

With effect December 14, 1995, Sierra Leone has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions. Sierra Leone maintains one multiple currency practice subject to Fund jurisdiction arising from the applied multiple-price Dutch auction system, as there is no formal mechanism in place to prevent spreads of effective rates between winning bids from exceeding 2%.

XI. Article IV Consultation

The Executive Board concluded the 2008 Article IV consultation on December 22, 2008. The next Article IV consultation will be held in accordance with the 2010 decision on consultation cycles.

XII. Technical Assistance

Department	Purpose	Date
FAD	Reform Progress update	September 2010
	Review of petroleum pricing mechanism	February 2010
	Tax administration	January 2010
	Evaluation of progress in PFM reforms	March 2009
	Assistance in designing a simplified regime for small taxpayers	January 2009

Department	Purpose	Date
	Evaluation of progress on tax administration reform and VAT preparation	September 2008
	Evaluation of progress on PFM reforms	July 2008
	Implementation of public financial management reforms	March 2008
	Tax administration reforms for successful VAT implementation	February 2008
MCM	Banking Supervision and Banking Regulation	April 2010
	Needs assessment and monetary operations and foreign exchange auction system	March 2010
	Follow-up assessment on TA needs	June 2009
	Follow-up assessment of banking supervision processes at BSL	March 2009
	Follow-up assessment on progress in strengthening central bank internal auditing	March 2009
	BSL: Internal audit and management of the central bank	October 2008
	Monetary policy, banking supervision, and recapitalization of the BSL	April/May 2008
	Recapitalization of the BSL	February 2008
STA	Standardized Report Form Data Development for Other Financial Corporations	October 2010
	Producer Price Index Mission	October 2010
	Assist the authorities in implementing the international standards recommended in the *Monetary and Financial Statistics Manual*	April 2009
	National accounts statistics mission	March 2009
	National accounts statistics mission	September/October 2008
	National accounts statistics mission	January 2008

XII. Resident Representative

Mr. Francis Kumah will assume responsibility for the Fund office in Freetown in November 2010 as a new resident representative.

Appendix II. Sierra Leone Joint World Bank-IMF Work Program, 2010–11

Title	Activities	Provisional Timing of Mission	Expected Delivery Date
	A. Mutual Information on Relevant Work Programs		
World Bank work program	Public Expenditure Review	February 2009	November 2010
	Supplement to Third Governance Reform and Growth Credit (GRGC 3)	May 2010	June 2010
	Fourth Governance Reform and Growth Credit (GRGC 4)	Multiple 2010	December 2010
	Decentralized Service Delivery Spn.	Multiple 2010	N/A
	Financial Sector TA Credit	Sep., Dec. 2010	March 2011
	Mining Sector TA Credit	Nov-Dec. 2010	May 2011
	IRCBP Supervision	June & Dec. 2010, May 2011	N/A
	IPFMRP (PFM Project) Supervision	Feb-Mar., June, Nov. 2010, May 2011	N/A
	Public Expenditure & Financial Accountability Assessment (joint with other donors)	August 2010	January 2011
	Technical Assistance		
	FPDFI:		
	• AML/CFT	May 2010	N/A
	AFRPS:		
	• Pay Reform	June 2010	N/A
IMF work program	2010 Article IV consultation and first ECF review	September 2010	December 2010
	Second ECF review	March 2011	June 2011
	Technical Assistance		
	FAD:		
	• Tax administration reform	N/A	N/A

Appendix II. Sierra Leone Joint World Bank-IMF Work Program, 2010–11 (continued)

Title	Activities	Provisional Timing of Mission	Expected Delivery Date
	MCM		
	• Needs Assessment and Multi-Topic	May 2010	June 2010
	• Banking Legislation	June 2010	July 2010
	• Open Market Operations/FOREX Management	October 2010	August 2010
	• Open Market Operations and Foreign Exchange Market	Dec 2010	March 2011
	• Open Market Operations and Foreign Exchange Market	Feb 2011	May 2011
	STA		
	• Monetary and Banking Statistics	October 2010	January 2011
	• Price Statistics	October 2010	January 2011
	• National Accounts	March 2011	June 2011
B. Agreement on Joint Products and Missions			
Joint products in 2010	DSA	September 2010	December 2010
	Assisting the authorities with the implementation of their financial sector reform strategy		Continuous

Appendix III. Statistical Issues

A. Assessment of Data Adequacy for Surveillance

General: Data provision has serious shortcomings that significantly hamper surveillance. The prolonged civil war resulted in a virtual collapse of statistical systems in the late 1990s. Serious deficiencies still affect balance of payments statistics, national accounts, government finance statistics, and social indicators. A major and sustained improvement in the coverage and timeliness of economic data will require greater interagency coordination and restructuring the institutional framework.

Real sector statistics: Improvements have been made in the compilation of construction, estimation of informal sector activity, measurement of government services, agricultural production, household final consumption, and constant price gross domestic product (GDP). Remaining issues concern rebasing the accounts, developing better data sources for agricultural production, and generally continuing the improvement of informal sector measurement. In addition, for constant price GDP, there is a need to supplement the consumer price index (CPI) with alternative price measures, such as the producer price index or industry-specific measures such as a construction cost index. Work in this area will continue under a new DFID-funded project.

Efforts to reconstruct the national accounts estimates commenced during 2003/04, with the main effort being to prepare new estimates for the period starting in 2001. Because resource constraints significantly hindered the production of final estimates, only preliminary data for 2001–04 were made available. Efforts are underway to prepare revised national accounts based on a 2005 benchmark and using 2005 prices to compile constant price estimates. However, shortages of resources and staff continue to pose major constraints to the statistical development undertaken by Statistics Sierra Leone (SSL).

The SSL compiles the CPI monthly and publishes it with a lag of about three weeks. It has been rebased to 2007 using the 2007 Sierra Leone integrated household survey and continues to cover the capital city and three main districts. While a national CPI is being compiled, the authorities continue to publish the old CPI (1992=100). To avoid confusion, the authorities have requested TA to validate the work done in order to adopt a common series.

A technical assistance mission visited Freetown in October 2010 to review the CPI and to advice on the development of a producer price index (PPI). The authorities are working to improve the index calculation methods for the CPI and procedures to aggregate regional CPIs to obtain the national index.

Preliminary PPI weighting structures have been developed in some areas to support compilation of indices by industry and product, and the sample of establishments to be surveyed has been selected. Work will continue on obtaining further weighting data, and on selecting products and transactions for sampling. It is expected that the first PPI, with indices calculated for May to August 2011, will be published in November 2011.

Government finance statistics: The budget reporting system was established with assistance from the Fund/UNDP technical assistance project. Monthly cash flow data on budgetary central government revenue, current expenditure, and financing are provided. The transaction coverage of the budgetary central government cash flow is incomplete. There is an urgent need for more timely and accurate data on foreign-financed development projects. Reports on implementation of the development budget and its financing are currently not produced in a format that is suitable for budget analysis because the necessary data are not available. There is also need for quality control of the final data.

The authorities are currently considering introduction of a flash reporting system for government expenditure in general and for foreign aid-financed projects. As part of the GDDS regional project for Anglophone African countries, work has been undertaken to reconcile fiscal and monetary data and to improve the coverage and classification of the two data sets. With the current drive towards decentralization and the growing role of local government, there is an urgent need to compile and monitor the operations (and financial balance sheet data) for the whole of consolidated general government.

Monetary and financial statistics: The main components of the central bank balance sheet are available daily and weekly; this system provides an early warning system on key financial targets. The full monetary survey is compiled by the Bank of Sierra Leone (BSL) with a lag of about six weeks; it has comprehensive coverage of commercial banks.

There has been some progress in the compilation of data in line with the 2000 Monetary and Financial Statistics Manual. The BSL, with assistance from STA, has completed the preparation of a standardized report form (SRF) for the central bank. There is a need to expand coverage of other deposit corporations, improve data collection for other financial corporations and develop the financial corporations survey.

Reconciliation of fiscal and monetary statistics remains a challenge. In the past, compilation of fiscal data solely on a cash basis and differences in the coverage of the central government explained most of the discrepancies between the datasets. In 2007, a TA mission found limited progress on previous recommendations on the fiscal reporting system for extra budgetary agencies and projects. The coverage of reporting agencies had improved, but there were many obvious errors and omissions in the data and in the BSL database. However, in June 2008 the authorities notified the IMF that the fiscal data have been reconciled with the expanded BSL monetary data.

Balance of payments: The BSL is responsible for compiling balance of payments (BOP) statistics. It obtains source data from the SSL, government ministries, the Customs and Excise Department (Customs), and the "Financial Survey of Major Limited Companies," for data on foreign direct investment. Imports and exports of goods estimates are based on data compiled by Customs and are adjusted for coverage, valuation, and timing to accord with BOP definitions. The BSL does not adjust BOP data using supplementary information to take account of unreported data.

External transactions are characterized by a large volume of activity in the informal sector, principally diamond smuggling. A considerable portion of imports is financed by these unrecorded exports. As a result, official BOP statistics tend to substantially understate transactions. Staff has been addressing this problem through the use of third-country (principally EU member) import data. STA has been providing technical assistance on BOP issues to help the authorities implement the *Balance of Payments Manual*, Fifth Edition (*BPM5*).

Data problems also exist for trade in services, income statistics, current transfers, and the capital and financial accounts. Regarding the last, there are substantial difficulties in tracking financial transactions of the public and private sectors that are routed through commercial banks. While the authorities are producing data on the international investment position, improvements are required in coverage and in valuation adjustments. These difficulties are manifested in reconciling flow data in the BOP and stocks in the international investment position. Estimates of smuggled imports and exports, in particular diamonds, are also not available.

Information on official grant and loan receipts is relatively good and is prepared by AFR on the basis of contact with the authorities and donor agencies, but data on private capital flows are very poor. Some information on private banking flows can be derived from the monetary survey. Other private flows, especially those linked to the informal diamond trade, are implicitly included in "errors and omissions."

B. Data Standards and Quality

Sierra Leone commenced its participation in the General Data Dissemination System (GDDS) in 2003. Metadata need to be updated.

C. Reporting to STA

Fiscal data are reported to AFR, but it is not disseminated in the *International Financial Statistics*. Plans are underway to resume reporting annual data for publication in the GFS Yearbook (the most recent data refer to 2004).

The BSL started reporting monetary data in the SRF-format to the IMF in April 2010.

Sierra Leone: Table of Common Indicators Required for Surveillance
October 2010

	Date of latest observation	Date received	Frequency of Data 1/	Frequency of Reporting 1/	Frequency of publication 1/
Exchange Rates	10/14/10	10/22/10	W	W	W
International Reserve Assets and Reserve Liabilities of the Monetary Authorities 2/	08/10	10/07/10	M	M	M
Reserve/Base Money	08/10	10/07/10	M	M	M
Broad Money	08/10	10/07/10	M	M	M
Central Bank Balance Sheet	08/10	10/07/10	M	M	M
Consolidated Balance Sheet of the Banking System	08/10	10/07/10	M	M	M
Interest Rates 3/	09/10	10/22/10	M	M	M
Consumer Price Index	08/10	09/17/10	M	M	M
Revenue, Expenditure, Balance and Composition of Financing – Central Government	06/10	08/13/10	M	M	N/A
Stocks of Central Government and Central Government-Guaranteed Debt	12/09	09/08/10	Q	Q	N/A
External Current Account Balance	12/09	09/08/10	A	A	A
Exports and Imports of Goods and Services	06/10	09/08/10	A	A	A
GDP/GNP	12/09	09/15/10	A	A	A
Gross External Debt	06/10	09/08/10	A	A	A
International Investment Position 4/	06/09	08/31/09	A	A	A

1/ Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).
2/ Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
3/ Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
4/ Includes external gross financial asset and liability positions vis-à-vis nonresidents.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 10/156
FOR IMMEDIATE RELEASE
December 10, 2010

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2010 Article IV Consultation with Sierra Leone

On December 6, 2010, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Sierra Leone.[1]

Background

Sierra Leone continued to make progress in its post-conflict transition towards creating an enabling environment for sustained economic growth. Although living conditions have started to improve, per capita income remains low and poverty is widespread. Sierra Leone's growth prospects hinge on rebuilding basic infrastructure and developing broad access to financial services.

Real GDP growth decelerated to 3.2 percent in 2009 owing to weak external demand associated with the global economic recession. However, economic activity is projected to increase to 4.5 percent in 2010, reflecting marked growth in the services sector, buoyant agricultural production, and a rebound in exports. While lower fuel and domestic food prices eased inflationary pressures during most of 2009, inflation is projected to increase to 16 percent in 2010, mainly because of a jump in the price level in the first two months of the year due to the introduction of the goods and services tax.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm

Exports have picked up in 2010 because of higher diamond export volumes and prices and gross international reserves are expected to remain at comfortable levels.

In June 2010, the Executive Board approved a new 3-year Extended Credit Facility (ECF) arrangement in support of Sierra Leone's economic program, which aims to raise economic growth in the medium-term by accelerating investments in infrastructure and social development. The program is designed to create fiscal space for these spending priorities by further strengthening tax performance and improving the public financial management system. Private sector growth is envisaged to be supported by a deepening of the financial sector.

Fiscal policy aims at improving infrastructure and social services in 2011. Capital spending is envisaged to further expand to 10.2 percent of GDP, most of which will be externally financed. Nonpriority expenditures are expected to remain constrained. Domestic revenues are projected to continue to increase to 13.3 percent of GDP in 2011, reflecting efficiency gains from tax reforms and the implementation of higher royalties on diamonds.

Monetary policy aims at bringing inflation down to single digits in 2011. With the establishment of a benchmark policy rate, the transmission mechanism is likely to improve. A flexible exchange rate will be maintained to facilitate adjustment to external shocks.

Structural reforms focus on: (i) improving the tax administration and broadening the tax base; (ii) strengthening public financial management by enhancing the planning, monitoring and evaluation process for capital projects and building a high-caliber workforce by implementing a multi-year pay reform; and (iii) deepening the financial sector by adopting the new surveillance guidelines for banks and establishing a credit reference bureau.

Executive Board Assessment

Against the backdrop of a challenging domestic and global environment, Directors underscored the need to maintain macroeconomic stability, address infrastructure bottlenecks, and reduce poverty. Given the large development needs and the importance of maintaining debt sustainability, Directors welcomed the authorities' determination to safeguard capital and social spending while minimizing the use of domestic financing.

Directors stressed the importance of fiscal prudence in balancing the need to mobilize resources for the ambitious infrastructure and social spending plans while maintaining debt sustainability. They expressed concern about the recent acceleration in fiscal spending and the continued use of central bank financing for budget expenditures. Directors noted the authorities' commitment to improve revenue collection from the goods and services tax, higher diamond royalties, and other critical tax administration reforms, and welcomed the implementation of an automatic fuel pricing formula. Directors also stressed the importance of implementing a comprehensive public sector pay reform, eliminating discretionary tax exemptions, and carefully prioritizing infrastructure projects. Directors strongly urged the authorities to apply the fiscal regime in the Mines and Minerals Act to all future mining agreements.

Directors noted the staff assessment that the leone remains broadly aligned with its fundamentals. They encouraged the authorities to press ahead with structural reforms to improve the business climate and boost competitiveness over the medium term.

Directors commended the Bank of Sierra Leone’s commitment to maintain a tight monetary policy to reduce inflationary pressures, particularly in the face of the significant increase in direct credit to the government. They considered that establishing a benchmark policy interest rate will help improve the transmission mechanism. Directors highlighted the need to enhance central bank independence and strengthen bank regulation and supervision.

Directors concurred that strong progress in implementing structural reforms is key to achieving high and sustainable growth. They agreed that reforms should focus on improving tax administration, strengthening public financial management, and developing the financial sector to boost private sector investment and activity.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Sierra Leone: Selected Economic Indicators

	2008	2009	2010 Proj.	2011 Proj.	2012 Proj.
	(Annual percentage change, unless otherwise indicated)				
National account and prices					
GDP at constant prices	5.5	3.2	4.5	5.2	6.0
GDP deflator	11.1	5.3	15.0	8.5	7.3
GDP at market prices	5,826	6,330	7,605	8,678	9,874
(in billions of local currency)					
Consumer prices (end-of-period)	12.2	10.8	16.0	9.5	8.0
Consumer prices (average)	14.8	9.2	17.6	9.1	8.7
External sector					
Terms of trade (deterioration -)	-2.3	-10.5	3.6	3.2	2.0
Exports of goods (US$)	-3.0	-1.0	25.7	15.4	13.2
Imports of goods (US$)	24.8	-2.6	18.0	8.6	11.1
Average exchange rate	2,985	3,410	…	…	…
(local currency per U.S. dollar)					
Nominal exchange rate change (depreciation -)	-2.2	-26.7	…	…	…
Real effective exchange rate (depreciation -)	-11.6	-3.2	…	…	…
Gross international reserves, months of imports	4.4	6.1	5.6	4.9	4.6
Money and credit					
Domestic credit to the private sector	56.8	45.4	26.1	31.4	18.3
Base money	9.6	19.3	8.0	14.4	15.8
M2	30.4	28.1	11.8	20.5	17.7
91-day treasury bill rate (in percent) [1]	9.1	14.0	18.1	...	...
	(Percentage of GDP, unless otherwise indicated)				
National accounts					
Gross capital formation	14.8	14.9	16.3	18.9	19.4
Government	6.2	7.1	8.4	10.2	10.2
Private	8.6	7.8	7.9	8.7	9.2
National savings	3.3	6.6	6.8	9.4	9.9
External sector					
Current account balance					
(including official grants)	-11.5	-8.4	-9.5	-9.5	-9.5
(excluding official grants)	-15.4	-12.8	-12.9	-11.6	-11.3
External public debt (including IMF)	31.2	36.1	39.8	28.1	29.2
Central government budget					
Overall balance	-4.7	-3.2	-4.7	-5.7	-5.0
(excluding grants)	-9.2	-11.1	-11.5	-12.5	-10.6
Revenue	11.5	11.8	13.0	13.3	14.3
Grants	4.5	7.9	6.8	6.8	5.6
Total expenditure and net lending	20.7	22.9	24.5	25.8	24.9

Sources: Sierra Leonean authorities; and the IMF staff estimates and projections.
1/ For 2010 data is for September.

INTERNATIONAL MONETARY FUND
EXTERNAL RELATIONS DEPARTMENT

Press Release No. 10/474
FOR IMMEDIATE RELEASE
December 6, 2010

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes First Review Under ECF Arrangement with Sierra Leone and Approves US$6.83 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the first review of Sierra Leone's economic performance under a program supported by an Extended Credit Facility (ECF) arrangement. The completion of the review enables the immediate disbursement of an amount equivalent to SDR 4.44 million (about US$6.83 million), bringing total disbursements under the arrangement to SDR 8.88 million (about US$13.67 million).

In completing the review, the Executive Board also approved the modification of a performance criterion related to the target on net domestic bank credit to the government. The three year ECF arrangement for Sierra Leone was approved with effect from July 1, 2010 for an amount of SDR 31.11 million (about US$47.88 million; see Press Release No. 10/228). The Executive Board also completed the financing assurances review.

Following the Executive Board's discussion of Sierra Leone, Mr. Naoyuki Shinohara, Deputy Managing Director and Acting Chair, made the following statement:

"After the economic slowdown in 2009, the outlook this year for Sierra Leone is more favorable. Growth has picked up due to buoyant output in the service and agriculture sectors and a rebound in exports. However, inflation will remain in double digits this year owing to the one time jump in prices from the introduction of the goods and services tax and higher domestic fuel prices. Gross international reserves remain at comfortable levels.

"The government's *Agenda for Change* envisages raising growth by removing infrastructure bottlenecks, while developing access to financial services. In the medium term, fiscal space for higher capital and social spending will be created by broadening the tax base, containing nonpriority spending, and raising public sector efficiency, especially in project selection and implementation.

"Fiscal spending, including on infrastructure, is projected to be higher than envisaged in 2010, resulting in higher domestic budget financing. Going forward, there is a need to strengthen budget discipline, increase revenue collection, contain nonpriority expenditures, and limit the use of direct credit to the government from the central bank. While the introduction of the goods and services tax has improved revenue collections, there is a need to adhere to the Mines and Minerals Act and continue to strengthen tax administration. The recent establishment of an automatic pricing framework for domestic fuel prices will eliminate fuel subsidies.

"Fiscal policy for 2011 appropriately focuses on scaling up investment in infrastructure and improving basic healthcare, while limiting domestic financing. To ensure fiscal sustainability, continued efforts to improve domestic revenue collection and to implement public sector pay reform will be important.

"Monetary policy will seek to bring inflation to single digits by next year. Exchange rate flexibility will be maintained to facilitate adjustment to external shocks," Mr. Shinohara added.

Statement by Moeketsi Majoro, Executive Director for Sierra Leone
December 6, 2010

Introduction

My Sierra Leonean authorities value highly the support from staff, Management, and Executive Directors in their efforts to foster socio-economic development, while maintaining macroeconomic stability. They appreciate the constructive dialogue with staff in addressing the policy challenges to sustaining economic growth and reducing poverty. My authorities have embarked on the structural transformation of the economy through increased investment in infrastructure and the social sectors. Accordingly, efforts at enhancing domestic revenue mobilization have been enhanced in the face of accelerated development spending. Implementation of their development agenda is however severely challenged by dwindling external financing, which remains crucial in creating the required fiscal space. My authorities broadly share the thrust of the staff report as it presents a balanced assessment of recent macroeconomic developments, policy opportunities and challenges going forward.

Program performance

In spite of the daunting challenges, my authorities continue to demonstrate a steadfast commitment to pursuing prudent macroeconomic and structural policies within the context of the Fund program. This is reflected in the strong performance in respect of the end-June 2010 program targets, as all quantitative performance criteria were met. However, while domestic revenue collection has risen, the enhanced development spending has warranted a resort to additional domestic bank financing. As staff pointed out, part of the additional spending has been required to finance the free health care program, higher interest payments, and outstanding arrears to oil marketing companies. On the structural front, the Bank of Sierra Leone (BSL) strengthened its oversight of the banking system by adopting new guidelines for off-site surveillance. In addition, the authorities took the bold and socially-sensitive step to implement an automatic fuel pricing mechanism, with a commitment to effect monthly increases until domestic fuel prices are fully reflective of international petroleum market developments. Further efforts continue to be directed at strengthening revenue administration and enhancing public financial management. My authorities' commitment to judiciously implement the program, going forward, remains unwavering. It is against this backdrop that they request completion of the first review under the ECF arrangement and modification to the program target on net domestic bank financing.

Recent economic developments

The economy continues to exhibit signs of an incipient recovery, manifested by the strong growth in mineral exports, rebound in domestic manufacturing and services sectors, and buoyancy in agricultural productivity. Against the backdrop of these developments, real GDP growth is well on course to revert to its upward trajectory, accelerating to 4.5 percent in 2010 from 3.2 percent in 2009. In spite of the increased importation of machinery, transport equipment and petroleum products to support the recovery process, the more than proportionate expansion in exports culminated in the narrowing of the trade deficit. The exchange rate has been relatively stable in 2010 following a marked depreciation the previous year, prompting the BSL to gradually reduce the size of the foreign exchange auctions. Gross foreign reserves are expected to remain at comfortable levels, well above 5 months of imports coverage, by end-December 2010. Furthermore, my authorities seize this opportunity to re-emphasize that the corrective measures to eliminate the separate windows in the foreign exchange auction that gave rise to multiple currency practices (MCP) have long been instituted. They continue to await the provision of technical assistance by the Fund in putting in place appropriate safeguards in the auction system to prevent re-introduction of MCPs.

Fiscal performance in 2010 has been challenging, given the authorities' determination to pursue their infrastructural and social development programs outlined under the 'Agenda for Change'. With improving but inadequate domestic revenue mobilization and delays in the disbursement of programmed external budgetary support, my authorities resorted to direct central bank financing as a stop-gap measure to keep implementation of critical development projects on course. Notwithstanding, they remain committed to maintaining fiscal discipline and minimizing utilization of ways and means advances at the Central Bank, and have thus instituted appropriate policy measures to improve the fiscal outlook. In addition to the upward revision of the domestic revenue target, the increase in diamond royalties to 6.5 percent initially scheduled to take effect in 2011 has been frontloaded to November 2010, while a new automatic petroleum pricing mechanism has commenced operation with a view to eliminating subsidies. Furthermore, the accumulated overdrafts from the Central Bank are gradually being rolled back and the authorities are in the process of effecting legislative amendment to the BSL Act to limit direct Central Bank credit to the government.

Monetary policy has responded appropriately to the fiscal developments and price pressures from the introduction of the goods and services tax (GST) in January this year. Supported by the relatively stable exchange rate, proactive monetary policy by the BSL has succeeded in containing inflationary pressures and in keeping monetary aggregates within program parameters. Inflation, which peaked at 17.8 percent in April 2010, is expected to drop to below 16 percent by end-December 2010. Credit to the private sector has expanded significantly to support a strong recovery of the economy. My authorities, however, remain committed to improving the efficiency of monetary operations to be better positioned to contain any resurging inflationary pressures.

Though in broad agreement with staff's assessment of recent macroeconomic and social developments, my authorities, however, wish to stress that the report fails to appropriately capture the tremendous progress that has been accomplished in recent years in addressing pervasive poverty and improving social development. While Sierra Leone had ranked at the bottom of the United Nation's Human Development Index (HDI) emerging from a decade-long civil conflict, the 2010 United Nation's HDI moves the country up an impressive 11 places from the preceding year to 158 position, reflecting recent progress in socio-economic developments.

Medium-term outlook and policies

With recovery from the global financial and economic crisis firming up, my authorities' policy focus has shifted to returning the economy to a high and sustainable growth trajectory, albeit within a stable macroeconomic environment. Continued scaling up of investment in infrastructure and enhanced delivery of basic social services, in line with the authorities' 'Agenda for Change' which forms the basis of the second generation Poverty Reduction Strategy Paper (PRSP II), will be pursued over the medium term. Against this backdrop, my authorities are in agreement with staff on the growth path of GDP to 6 percent and the improving outlook for inflation to single digits by 2012. With the reduced exchange rate pressures, the gross foreign exchange reserves position is expected to cover over 5 months of imports over the medium term.

Fiscal policy

My authorities remain committed to pursuing prudent fiscal management with a view to maintaining medium- to long-term fiscal sustainability. Mindful of the challenges in scaling-up resources to effectively implement the 'Agenda for Change', the authorities are determined to institute far-reaching policy measures to ensure mobilization of substantial domestic revenues to complement external budgetary and project support. To this end, the fiscal regimes stipulated in the Mines and Minerals Act (MMA) 2009 and the existing tax and customs legislations will be judiciously applied. The Revenue Management Bill, which is to be submitted soon for legislative approval, will minimize the issuance of discretionary tax exemptions.

On the expenditure front, my authorities will seek to switch expenditures towards their strategic priority of scaling up investments in infrastructure and other key areas such as education, health, and agriculture, consistent with attainment of the MDGs. Accordingly, non-statutory recurrent expenditures will be appropriately contained to create the needed fiscal space. Furthermore, public financial management will continue to be strengthened in order to improve budget credibility and enhance the efficiency of public spending. To this end, the integrated financial management information system (IFMIS) will continue to be rolled out to the remaining government ministries, departments and agencies (MDAs), while at the local council level a financial management information system will be implemented to promote transparency and accountability in the use of their resources. Additionally, a three-year public investment plan will be fully integrated into the budget process over the medium term.

While we agree with staff on the exclusion of the anticipated proceeds from large mining operations from the medium-term macroeconomic framework, my authorities are confident that the medium- to long-term fiscal outlook will be drastically improved as proceeds from these mining ventures are realized and prospects for commercial oil drilling off the coast of Sierra Leone materialize. On the latter, action is being taken to strengthen the regulatory and institutional framework for the upstream petroleum sector, including the formulation of a new petroleum sector policy that sets out the fiscal principles for a modern petroleum fiscal regime.

Monetary and exchange rate policies

My authorities are committed to returning inflation to single digits over the medium term, following the hike at the start of the year on account of the introduction of the GST and the pass-through effects of the exchange rate. To this end, the monetary policy framework will be strengthened, including through the introduction of a benchmark policy rate to help signal the stance of monetary policy to the market. Monetary operations will be further deepened by enhancing the effectiveness of the monetary instruments in sterilizing excess liquidity.

The current flexible exchange rate regime will be maintained to help facilitate smooth adjustments to external shocks. The foreign exchange auction will continue to complement monetary operations in absorbing excess liquidity. Also, the BSL will seek to enhance its foreign exchange management strategy by promoting inter-bank foreign exchange market transactions and migrating to a wholesale foreign exchange auction system.

Debt sustainability and management

My authorities concur with the staffs' assessment that the country remains at a moderate risk of debt distress, with all external debt indicators below their indicative thresholds under the baseline scenario. They are, nonetheless, cognizant of the threats to debt sustainability in the event of an external shock. As a result, they are committed to refraining from non-concessional external borrowing, while strengthening their public debt management capacity. In this regard, a comprehensive national debt law and procedures manual, consistent with international best practices, will soon be submitted for parliamentary approval. Plans are also underway to electronically link the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) with IFMIS, and technical assistance is being sought from the Fund and the World Bank to develop a comprehensive medium-term debt management strategy (MTDS). Finally, as staff pointed out, progress is being made in finalizing arrangements for the implementation of the commercial debt buyback operation, under the auspices of the World Bank that will significantly reduce the country's stock of outstanding external debt.

Other structural reforms

In addition to strengthening the debt management capacity, my authorities' structural reform agenda will include instituting policy measures aimed at developing the financial sector and improving the business climate.

My authorities will continue to pursue reform of the financial sector aimed at promoting financial intermediation, while maintaining financial stability. To this end, a credit reference bureau is to be fully operational to help address the information asymmetry in the banking sector, thereby mitigating the risk of loan default. Further strengthening of the supervisory framework of the banking system will be undertaken through the adoption of risk-based supervision including consolidated supervision of banks and other financial institutions, while the automation of the payments system will be completed over the medium term.

Finally, the process of revising key banking legislations, in line with international regulatory standards, will be swiftly concluded.

Finally, the business environment will be further improved, including through the implementation of the Private Sector Development Strategy. Progress is already being made in strengthening the business regulatory framework and minimizing the barriers to investment, as manifested in the recent legislative approval of the Public-Private Partnership law that encourages private participation in the delivery of public services. The continued progress accomplished in creating a conducive business environment is reflected in the country's steady upward movement in the rankings of the World Bank's 'Ease of Doing Business' index.

Conclusion

My authorities continue to demonstrate a firm commitment to implementing the ECF program as reflected in the strong program performance. Their commitment to judiciously implement the program, going forward, remains unwavering.

My authorities consider the Fund's and other development partners' policy advice and financial assistance critical to successfully implementing their development agenda and attaining the MDGs. It is against this backdrop that they solicit the Executive Board's support in completing the first review under the ECF arrangement.