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Djibouti: Sixth Review Under the Extended Credit Facility Arrangement and Request for Waivers of Nonobservance of Performance Criteria—Staff Report; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Djibouti.

In the context of the sixth review under the extended credit facility arrangement and request for waivers of nonobservance of performance criteria, the following documents have been released and are included in this package:

- The staff report for the sixth review under the extended credit facility arrangement and request for waivers of nonobservance of performance criteria, prepared by a staff team of the IMF, following discussions that ended on March 19, 2012 with the officials of Djibouti on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 9, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive

- A Press Release summarizing the views of the Executive Board as expressed during its May 23, 2012 discussion of the staff report that completed the request and/or review.

- A statement by the Executive Director for Djibouti.

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

Letter of Intent sent to the IMF by the authorities of Djibouti*
Memorandum of Economic and Financial Policies by the authorities of Djibouti*

*Also included in Staff Report

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

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DJIBOUTI

Sixth Review Under the Extended Credit Facility Arrangement and Request for Waivers of Nonobservance of Performance Criteria

Prepared by the Middle East and Central Asia Department
(In consultation with other departments)

Approved by Adnan Mazarei and Dhaneshwar Ghura

May 9, 2012

- **Mission:** Discussions on the sixth review of the Extended Credit Facility (ECF) were held in Djibouti during March 6–19, 2012. The staff team consisted of Messrs. Sdralevich (head) and Davies, and Ms. Gicquel (all MCD), and Mr. Million (SPR). The mission met with the governor of the Central Bank of Djibouti (CBD), the minister of finance, senior government officials, representatives of public enterprises, the private sector, and the donor community. World Bank staff attended some of the meetings. Mr. Thiam (resident representative) assisted the mission. Mr. Bah (OED) participated in key policy meetings.
- **Fund relations:** The ECF arrangement (September 2008–June 2012) was approved in September 2008 in the amount of SDR 12.72 million (80 percent of quota). The program performance was broadly on track, and the authorities are requesting three waivers of nonobservance of end-December 2011 performance criteria. Djibouti's outstanding loans from the Fund were SDR 16.92 million (106.43 percent of quota) as of March 31, 2012.
- **Augmentation:** At the completion of the fifth review, the Executive Board approved an augmentation of SDR 9.54 million (60 percent of quota) to meet the additional external financing needs created by the international price shock and the drought. The second, equal tranche of the augmentation will be disbursed at completion of the sixth review.
- **Exchange rate regime:** The CBD operates a currency board arrangement pegged to the U.S. dollar at the rate of Djibouti Franc 177.721 per U.S. dollar. Djibouti has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current international transactions.
- **Safeguards assessment:** A mission took place in June–July 2008; an update assessment mission took place in November 2011.
- **Financial Sector Assessment Program:** The report was discussed by the Board on June 17, 2009.

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Executive Summary

The ECF which began in 2008 is nearing its conclusion. Despite mixed program implementation, the ECF helped Djibouti maintain macroeconomic stability in a period that saw a transformation of the Djiboutian economy, when massive FDI expanded port capacity, transit trade to Ethiopia soared, the banking system boomed, and the country played an increasingly important geopolitical role. The Fund also supported the country in dealing with the Horn of Africa drought and the 2008 and 2011 commodity price hikes.

Economic activity is expected to be strong in 2012, and inflation is projected to decline. Port activity, trade with Ethiopia, construction, and FDI are expected to contribute to a 4.8 percent GDP growth this year compared to 4.5 percent in 2011. Inflation is projected to decline to 4.3 percent mostly thanks to the stabilization of world food prices. Still high world commodity prices and food import to help households affected by the drought are expected to keep the current account deficit above 12 percent of GDP.

The ECF program was broadly on track at the end of 2011. The authorities improved fiscal performance and achieved a fiscal deficit of 0.7 percent of GDP, in line with the program targets. However, bank financing to the government was higher than programmed because of the larger repayment of domestic arrears, and the government missed by a very small margin the ceiling on the accumulation on domestic arrears. The structural benchmarks for 2011-12 have been met, save two.

The authorities are committed to keeping sound macroeconomic policies in 2012 by:

- Targeting a surplus of 0.5 percent of GDP in 2012 and pursuing fiscal reforms;
- Improving debt sustainability by relying on concessional borrowing and avoiding accumulation of domestic and external arrears; and
- Continuing strengthening bank supervision and central bank governance.

Staff supports the authorities' request for the completion of the sixth review and the waivers for the nonobservance of performance criteria. Executive Directors endorsed the revised targets agreed with the authorities during the fifth review mission, but because of the delay in issuing the fifth review report to the Board, the end-2011 performance criteria could not be modified accordingly. Therefore, the authorities request waivers for nonobservance of performance criteria on the budget balance (for which the revised target was met) and net credit to the government (for which the revised target was missed by a small margin), and of the continuous performance criterion on the non-accumulation of domestic arrears.

The authorities have expressed interest for a successor program. Staff is ready to assist the authorities in drawing lessons after the completion of the program and help define the objectives of a new ECF arrangement.

I. Background and Recent Economic Developments

1. **The sixth review concludes the ECF**:

- **The program coincided with the still-ongoing transformation of the Djiboutian economy.** Massive FDI expanded port capacity, transit trade to Ethiopia soared, and the country played an increasingly important geopolitical role—not least because of the threat of piracy in the Indian Ocean. Reflecting Djibouti's rising pivotal role in the region, the number of banks increased, and deposits and credit to the private sector grew at double-digit rates. At the same time, the economy was hit by exogenous shocks, chiefly the Horn of Africa drought and the 2008 and 2011 commodity price hikes.

- **The ECF helped the authorities to maintain sustained growth and broad economic stability.** Fiscal policy focused on social and investment spending. The CBD's policies centered on maintaining coverage of the currency board and strengthening bank supervision. Despite the imported price shocks, inflation remained relatively contained.

- **Program implementation was however mixed**. After the 2009 fiscal slippage, partly driven by extra-budgetary spending, the completion of the second and third reviews required building a track record period. Moreover, external arrears were accumulated to several bilateral and multilateral creditors. And, structural reform advanced less than expected, undermining the effectiveness of fiscal policy and holding back improvements in the economy's competitiveness.

2. **The ruling coalition was unexpectedly defeated at the February local elections.** Civil society associations won key municipal positions, including the mayor of Djibouti, thus giving rise to the first-ever electoral loss on the ruling coalition. President Ismaël Omar Guelleh is still solidly in power at the national level, but public discontent—fueled by widespread poverty and unemployment particularly among the youth—is rising and will likely affect the next legislative elections in January 2013. Security risks are increasing with the government's military involvement in Somalia.

3. **Economic activity is expected to be strong this year**. GDP growth is projected to rise from 4.4 percent last year to 4.8 percent in 2012 because of improved port activity, trade with Ethiopia, construction and FDI. Inflation is expected to decline from about 5 percent in 2011 to about 4 percent this year owing to the stabilization of international food prices, a likely larger supply of subsidized food from the state-owned farms abroad, and the reduction of electricity tariffs. Broad money and bank deposits, which had fallen in 2011 because of exceptional factors, are expected to resume growth this year. In parallel, private-sector credit growth is projected to rise, driven by construction and trade.

4. **The current account deficit will remain high**. The deficit rose sharply to 12.6 percent of GDP last year mainly because of the impact of last year's Horn of Africa drought and high commodity prices. As these effects will persist to some degree in 2012 while FDI is expected to increase, the deficit is projected to decline only to about 12 percent of GDP. International reserves will increase from about $230 million in 2011 to $245 million in 2012 and continue to ensure currency board coverage. In line with the decline of the U.S. dollar, the real effective exchange rate depreciated by about 4 percent in 2011.

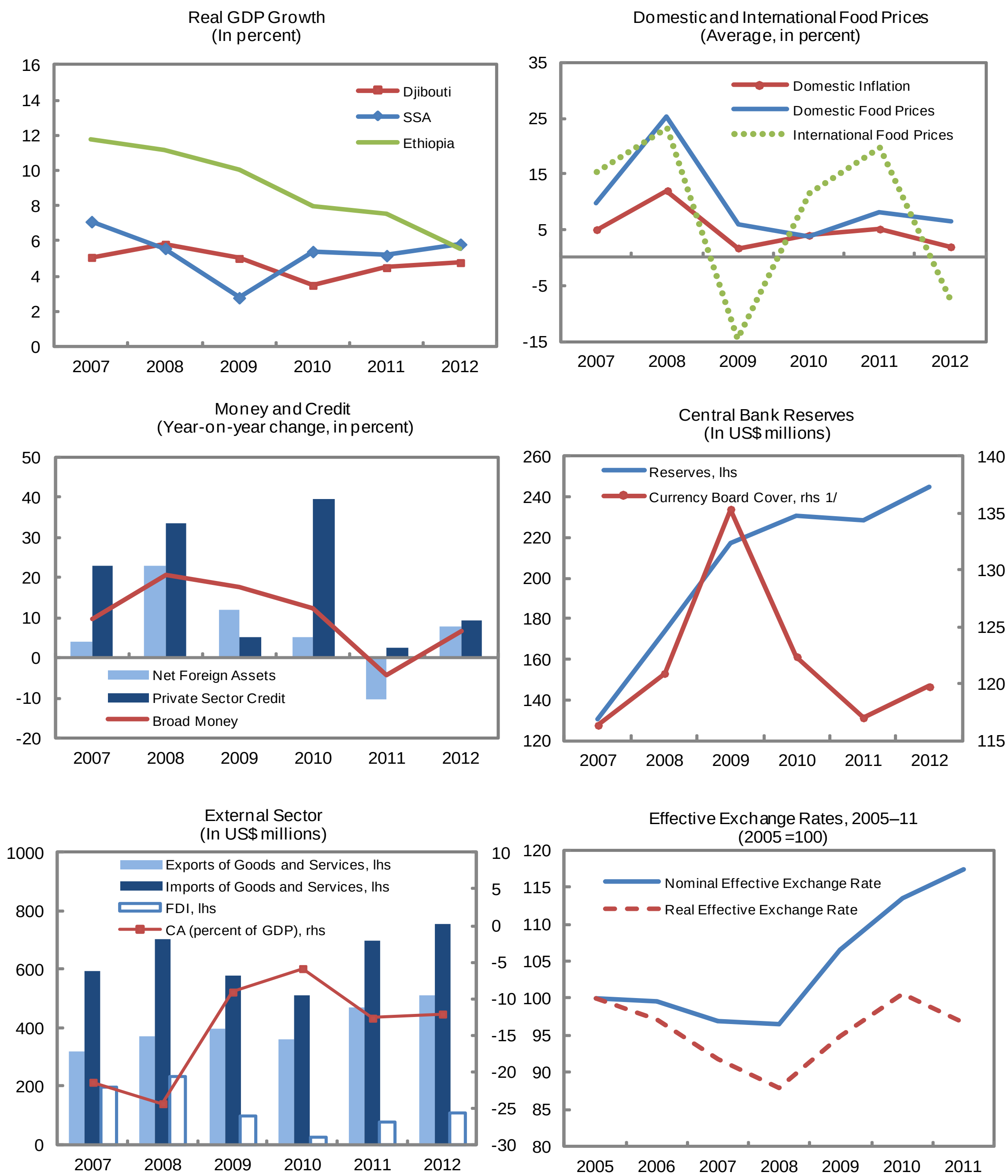
Text Table 1. Djibouti: Main Macroeconomic Indicators, 2008–12

	2008	2009	2010	2011 Prel. Est.	2012 Proj.
Real GDP growth	5.8	5.0	3.5	4.5	4.8
Inflation (average)	12.0	1.7	4.0	5.1	4.3
Current account balance (percent of GDP)	-24.3	-9.1	-5.8	-12.6	-12.1
Gross official reserves 1/	3.6	5.1	4.0	3.6	3.6
Memorandum Item:					
Ethiopia: Real GDP growth	11.2	10.0	8.0	7.5	5.5

Sources: Djibouti authorities; and IMF staff estimates.
1/ In months of following year's imports.

5. **The negative effects of the drought will continue to affect Djibouti in 2012.** The UN has declared the end of the famine in Somalia, the country worst hit by the drought. However, its effects will persist in Djibouti, as the total affected population, mainly rural inhabitants and refugees, is expected by the UN to rise from about 140,000 in 2011 to over 200,000 this year, including a refugee population numbering about 22,000 (up from 15,000 before the summer) which puts continued pressure on government and donor services. Development partners have already disbursed part of the pledged $65 million, mostly in the form of food aid through the World Food Program (WFP).

Figure 1. Djibouti: Selected Economic Indicators, 2007-12



Sources: IMF *World Economic Outlook*, September 2011; IMF *Information Notice System;* Djibouti Authorities; and IMF staff projections.

1/ Gross foreign assets of the CBD in percent of monetary liabilities (reserve money and government deposits).

II. PROGRAM PERFORMANCE

6. **The end-2011 program outcome is being formally evaluated based on the performance criteria set at the time of the fourth review.** Owing to the issuance of the fifth review staff report to the Board after the end of 2011, Executive Directors could not modify the end-December performance criteria on the budget balance and net credit to the government in line with the authorities' revised fiscal objectives for the year agreed during the fifth review mission, which envisages a budget deficit target of 0.4 percent of GDP. Consequently, the end-2011 performance criteria set in CR/12/169 still reflect the more ambitious target of a fiscal surplus of 0.4 percent of GDP (Text Table 2). At the Board meeting for the completion of the fifth review, Directors supported the principle that the program would be achieving its broader goals if the end-December 2011 outcome is in line with the revised targets (CR/12/197).

Text Table 2: End-December 2011 Quantitative Performance Criteria and Preliminary Estimates

(In millions of Djibouti francs; unless otherwise indicated)

		End-2011	
		CR/12/169 PC	Revised Targets
Performance criteria			
	Ceiling on net credit to government from the banking system	-2,600	-779
	Floor on government budget balance (*ordonnancement*)	883	-938
	in percent of GDP	0.4	-0.4
Indicative target			
	Floor on social spending	14,451	12,829
Memorandum items 1/ :			
Adjuster No.1	Projected French, U.S., and Japan military base payments	12,736	10,554
Adjuster No.2	External budgetary grants and loans	3,228	2,709
Adjuster No.3	Externally financed public investment loans (PIP)	6,815	5,948

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ See the Technical Memorandum of Understanding for definitions and adjustor calculations.

7. **According to these metrics, the program is broadly on track.** The authorities achieved a budget deficit of 0.7 percent of GDP (compared with the targeted deficit of 0.4 percent of GDP). This allowed them to meet the target for the budget balance adjusted for the shortfalls in the French military base payment (net of taxes)[1] and external assistance. However, the target on net credit to government from the banking system was missed by 0.2 percent of GDP because of the much-larger-than-planned repayment of domestic arrears at the end of the year. The criterion on accumulation of new domestic arrears was missed by less than 0.01 percent of GDP in December 2011, by about 0.05 percent of GDP in January 2012, and by about 0.09 percent in February 2012 because of delays in social security payments.

[1] The revenues from the French military base were lower than expected because the taxes paid by French personnel, and deducted from the lease, were higher than previously estimated by the authorities.

8. **The structural benchmarks for 2011-12 have now been met, save two.** Because of the lack of systematic information on tax-exempt companies (gathering which turned out to be administratively and politically more challenging than expected), the authorities have not been able to prepare a list of beneficiary companies defaulting on the requirement to file tax returns (*structural benchmark for end-March 2012*). Moreover, the software for the introduction of the new budget classification consistent with the GFS standard was not acquired because of delays in donor financing (*structural benchmark for end-December 2011*).

III. POLICY DISCUSSIONS

9. **Discussions focused on the economic situation, program performance, and policies for 2012 on the backdrop of the forthcoming program conclusion.** In the real sector, the authorities' continued concern is how to reduce unemployment through high rates of growth. In the fiscal sector, the challenges are maintaining fiscal discipline through strong tax collection and spending controls. In this connection, public debt issues center on preventing the accumulation of new external arrears and gradually repaying domestic arrears, especially with public utilities. In the monetary and financial sector, the emphasis is on strengthening bank supervision and implementing the 2011 banking law.

A. Real Sector

10. **Unemployment remains the crucial social and economic challenge for Djibouti.** During the mission, staff presented the results of cross-country comparisons and medium-term unemployment projections and sensitivity analysis. The sobering message of these simulations is that Djibouti's high unemployment rate, currently estimated at 60 percent of the labor force, will persist for several years even under very optimistic assumptions.

11. **Growth will be helped by the interconnection with the Ethiopian electricity grid, which is fully operational.** This has made possible a 30 percent tariff reduction for about 60 percent of consumers, and reduced fuel imports by the state-owned power company *Electricité de Djibouti* (EDD). At the same time, a World Bank-funded study to evaluate options for the domestic production of electricity will be launched this year. The World Bank is also financing the exploration of Djibouti's geothermal potential. A recently launched solar-energy project financed by Japan could open the way to wider exploitation of solar power.

12. **Long-delayed poverty and household budget consumption surveys were launched in the first half of the year**. The results will be used to update the National Initiative for Social Development (INDS), the government's poverty reduction initiative, and prepare the ground for the donor conference. The oft-postponed donor conference is tentatively planned for the second half of 2012 when the outcome of the poverty and household expenditure review will be available.

B. Fiscal Issues

13. **In 2011, the authorities succeeded in maintaining broad fiscal discipline.** The budget deficit reached 0.7 percent of GDP as the authorities caught up most of the shortfall in tax collection that was due to the government transition and the drought in the first half of the year. A shortfall in revenues from the lease on the French military base net of taxes and in external assistance was partly compensated by cuts in current and investment spending.

14. **A higher-than-planned repayment of domestic arrears led to an increase in net bank credit to the government.** Last year, the authorities concluded the reconciliation of cross-debt with Djibouti Telecom, the water company ONEAD, and EDD (*structural benchmark for end-September 2011*), which confirmed that the stock of domestic arrears accumulated in the 1990s (netting out taxes due the public enterprises) amounted to about 4 percent of GDP. These arrears made it more difficult for public enterprises to attract donor financing, and the authorities decided at the end of last year to clean the public enterprises' balance sheet by doubling the scheduled annual arrears payment of 1 percent of GDP. The needed additional financing came from an advance on dividends of the CBI, the largest commercial bank in which the government has a stake, and the draw-down of government deposits at the CBD. This led net credit to government to overshoot its ceiling by 0.2 percent of GDP.

15. **The authorities committed to a budget surplus of 0.5 percent of GDP in 2012.** The National Assembly approved a balanced budget for 2012, with the objective of improving debt sustainability, strengthening the financial position with the banking system, and repaying domestic arrears. However, the authorities agreed that the improvement in the government financial position vis-à-vis the banking sector and the repayment of domestic arrears require a more ambitious outcome:

- **Revenues:** The authorities project broadly unchanged tax revenues compared with the budget. The expected shortfall deriving from the downward revision of the French contribution net of taxes (based on the lower outcome in 2011) will be compensated by the additional $8 million per year recently agreed with the U.S. as fixed annual payment in lieu of taxes on fuel consumed by the U.S. military.

- **Expenditures:** The authorities aim to maintain tight control on current spending, including the freeze on public-sector hiring (excluding health and education) and public-sector wages. The increase in the lowest salary level as an anti-poverty measure amounts to an additional budgeted cost of about 0.1 percent of GDP. To achieve the targeted budget surplus, the authorities made a commitment to postpone investment and reduce lower-priority transfer spending by a total of about 0.5 percent of GDP.

Fiscal sector reforms

16. **The authorities renewed their commitment to fiscal reform:**

- **Exemptions**: The reform of the tax exemption system remains a priority. Enforcing the suspension of exemptions for companies that have not yet filed tax returns for 2010 (*structural benchmark for end-March 2012)* proved to be too ambitious administratively and politically. However, tax returns are essential to calculate fiscal expenditures and build momentum for reform of the discretionary and non-transparent exemptions system, which would allow rationalizing the tax system and strengthening government revenues. Therefore, the authorities committed to compiling and publishing a list of tax-exempt companies, which is a necessary step toward collecting tax returns.

- **Tax policy**: The ministry of finance intends to conduct in the coming months a wide-ranging review of the tax framework in consultation with the private sector. The review would constitute the first step in a medium-term reform of the tax system that supports business, especially small-and-medium-sized enterprises, and boosts Djibouti's role as services and transport platform in the region.

- **Public financial management**: Financing from the EU, which had been secured to purchase the software for the reclassification of the budget according to GFS standards, may materialize much later than planned. The authorities are therefore considering possible back-up financing options, including budget resources.

- **Fuel and food subsidies**: In early 2011, the authorities fixed the prices of diesel and gasoline with the objective of alleviating the impact of the oil price shock on the poorest segments of the population. In light of its cost, estimated at 1.5 percent of GDP in 2011 and limited effectiveness, the authorities committed to a reform of the diesel subsidy (Box 1); the timing of the reform is uncertain, however, in light of the weak poverty data and the needed involvement of development partners. With regard to the food subsidy system, the authorities estimate its overall cost as relatively small (0.1 percent of GDP for the farm system, and 0.5 percent in indirect tax exemptions on basic food items), and do not plan to reform it in the immediate future.

Box 1. Diesel Subsidies

Diesel prices are set on the basis of a mechanism which allows domestic prices to follow international oil price movements. The mechanism adds several taxes, distribution costs and margins to the reference CFI (cost, freight, and insurance) price, and is applied monthly. A discretionary adjustment component is designed to smooth the transmission from world prices (Table), but in recent years has been used to maintain retail diesel prices consistently below full pass-through levels. In March 2012, the adjustment component was set at 50 DF, keeping the pump price around 20 percent below the 256.5 DF full pass-through level.

Fuel Price Structure for Retail Sale, March 2012

	Diesel (in DF)	In % of price incl. full pass-through
CIF price	157.5	61.4
FOB price	146.9	57.3
Exporter's premium and margins, and port fees	10.6	4.1
Taxes	15.2	5.9
Tax on domestic consumption (26% of CIF price)	41.0	16.0
Excise	6.0	2.3
Royalty	18.2	7.1
Adjustment	**-50.0**	**-19.5**
Distribution and margins	10.9	4.2
VAT (7% of CIF price, taxes, and distribution and margins)	12.8	5.0
Transport	1.8	0.7
Retailer margins	4.9	1.9
Pump price	203.0	79.1
Price including full pass-through	256.5	100.0

Source: National authorities

The diesel subsidy entails a shortfall in tax revenues, rather than an explicit subsidy. In 2011, reflecting rising international oil prices, the shortfall in revenue on diesel products amounted to 1.7 percent of GDP.

The diesel subsidy is inefficient. The diesel pricing mechanism was intended to protect the most vulnerable segments of the population. However, recent IMF technical assistance shows that 70 percent of direct fuel subsidies benefited the wealthiest quintile of the population.

The diesel subsidy should be substituted by better-targeted social safety nets and increased social spending. The gradual increase in diesel prices reduce the tax revenue loss should be accompanied by better targeting of social safety net spending. The government could support the neediest households, for example those below the extreme poverty line, through "workfare" cash-transfer programs, and the poor who are affected by higher transportation costs, through subsidized transportation for students. Geographical targeting can help to focus these interventions, since in Djibouti City, 90 percent of the population in the two lowest income quintiles lives in the northern neighborhoods of the city, mostly in Balbala. The World Bank is already active on these fronts in the context of its crisis response program, and availability of poverty statistics from the forthcoming household expenditure survey will help further improve targeting. Later on, the resources freed by subsidy reform could be used to promote spending on items that highly benefit the poor, such as water, health care, and education, which represent the largest expenditure shares in poor households' budgets.

C. Public Debt

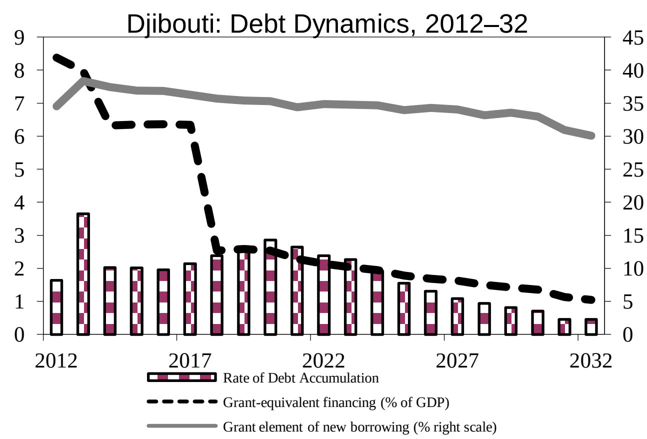
17. **During 2011, external public debt remained broadly stable at about 55 percent of GDP**. Djibouti remains at high risk of debt distress, and staff alerted the authorities of the risks that could derive from the ambitious investment plan which underpins "Djibouti 2035," a long-term vision for the country's economic development. For these projects, the authorities intend to rely on concessional financing and public-private partnerships. However, the scale of the envisaged projects could heighten debt vulnerabilities due to insufficient concessionality of financing and contingent fiscal costs related to the public-private partnerships. These vulnerabilities may be exacerbated by Djibouti's weak administrative capacity.

Box 2. Debt Sustainability Analysis

The updated DSA confirms that Djibouti remains at a high risk of debt distress. Under the baseline, the present value (PV) of the debt-to-GDP ratio is projected to decrease from 46 percent in 2012 to 27 percent in 2032, but remains above the threshold of 30 percent up to 2029. The PV of the debt-to-exports ratio also breaches its indicative threshold of 100 percent until 2020. However, the PV of the debt-to-revenue ratio and both debt service ratios are below their indicative thresholds.

Stress tests show that external debt sustainability is most vulnerable to a devaluation of the currency. The PVs of the debt-to-GDP ratio and debt -to-revenues ratio are most vulnerable to a one-time devaluation of the currency (Djibouti operates a currency board arrangement pegged to the U.S. dollar). The debt service-to-export ratio and the debt-to-export ratio are most vulnerable to an export shock, highlighting the vulnerability of debt sustainability to port services.

The macroeconomic assumptions for 2012–31 remain broadly the same as in the last DSA. The real GDP growth rate in the long run is projected at 5.8 percent, while inflation is expected to remain at 2.5 percent. The current account deficit is expected to stabilize at about 12 percent of GDP in the next few years, mostly due to large assumed FDI inflows, and then gradually decrease to about 5 percent of GDP in the long run.



The results of the public-sector DSA mirror those of the external DSA. In the baseline scenario, public debt indicators are projected to improve in the medium term. The PV of the debt-to-GDP ratio is projected to decrease from 51 percent in 2012 to 27 percent in 2032. The PV of debt-to-revenue ratio would also decrease from 143 percent to 89 percent in 2032, reflecting Djibouti's relatively high and stable government revenues.

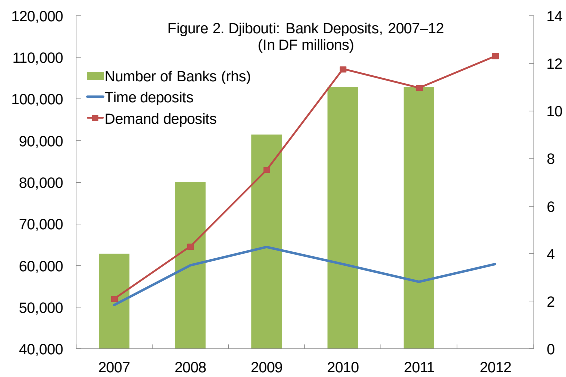
18. **The authorities are implementing the corrective measures introduced after the accumulation of external arrears in 2011.** All external arrears were cleared before the fifth review. The authorities are following more rigorously the external debt service schedule and have improved regular reporting to staff. However, despite the availability of UNDP financing, the debt office staff has not yet been strengthened, as finding an international debt expert has proved difficult. The authorities have also requested Fund technical assistance to strengthen debt sustainability analysis and debt management.

19. **Debt rescheduling efforts are continuing with the remaining official bilateral creditors.** To comply with the comparability of treatment requirement in their Paris Club agreement, the authorities are seeking similar terms from non-Paris Club creditors. They have already signed agreements with Saudi Arabia and are in negotiation with Kuwait and the United Arab Emirates.

20. **A successor arrangement with the Fund could open the way to a debt stock reduction by Paris Club creditors.** According to the goodwill clause in the 2008 agreement, creditors may agree to re-evaluate the sustainability of Djibouti's external debt situation and consider a debt stock reduction, provided that the current ECF is completed successfully and a successor arrangement is approved.

D. Financial Sector Issues

21. **Overall, the banking sector seems healthy, but there are concerns about credit quality.** According to end-2011 indicators, the banking sector remains profitable and highly liquid, with liquid assets accounting for over 60 percent of total assets. However, the ratio of nonperforming loans to gross loans rose from 8.3 percent at end-2010 to 9.4 percent at end-2011.[2]



Sources: Djibouti authorities; and Fund staff estimates and projections.

22. **Risks remain significant**. Rapid credit growth and the strong increase in number of banks in recent years, together with rising exposure to the real estate sector, raise concerns about a possible further deterioration in credit quality. The increase in the minimum capital requirement has already led some banks to strengthen their capital, but is putting many of the smaller banks under severe pressure to find funding. Moreover, continued dominance of the two leading banks, which account for more than 80 percent of total deposits and place a significant portion of their assets abroad

[2] The authorities revised some financial soundness indicators, including on non-performing loans, which are now estimated to be higher.

(traditionally Europe, but now also increasingly African countries) remains a potential source of instability, in light of the risks arising from the concentration of their bank loan portfolios, the exposure to interest rate risk abroad, and the tail risk of a European financial crisis, which might cause siphoning of liquidity out of the country.

23. **These vulnerabilities may be exacerbated by possible governance problems in the banking sector**. Despite significant improvement, there are still weaknesses in the prudential and regulatory framework, the size of the banking sector is relatively large compared with the small Djiboutian economy, and most banks are small and recently established. As a result, credit concentration remains excessive (in 2011, seven banks exceeded the single-borrower limit of 25 percent of net capital), connected lending is believed to be pervasive, and internal governance structures are often weak, especially in the smaller banks.

24. **The authorities continue their efforts to strengthen bank supervision.** With the support of Fund technical assistance, the CBD is introducing regulation that puts into effect the 2011 banking law. The CBD now also requires banks to submit prudential ratios and income statements on a quarterly basis, which will allow the CBD to compile financial soundness indicators more frequently. The CBD has conducted onsite inspection of five banks and one micro-finance institution in 2011, and, in 2012, intends to conduct onsite inspection of five banks, five foreign-exchange bureaus (of which three have already been inspected), and two micro-finance institutions.

25. **Central bank governance has improved, but the recent update safeguards assessment underlined persisting weaknesses**. In particular, the update safeguards assessment pointed to a limited oversight by the board of directors, continued lack of an internal audit function, and statutory noncompliance. Nevertheless, the CBD has implemented some of the key 2009 safeguards assessment recommendations, including the adoption of the official timetable for quarterly meetings (*structural benchmark for end-June 2011*) and the full publication of the 2010 audited financial statements of the CBD (*structural benchmark for end-December 2011*), which was completed in April 2012.

IV. PROGRAM ISSUES AND RISKS

26. **The authorities are requesting waivers on the basis of the performance criteria set up during the fourth review of the program (CR/12/169, 6/24/2011).** Since the end-December performance criteria could not be modified to include the revised targets discussed during the fifth review mission, the authorities request waivers for nonobservance of end-December 2011 performance criteria for the government balance (the performance criterion set in CR/12/169 was missed by about 0.4 percent of GDP), net credit to the government (the performance criterion set in CR/12/169 was missed by 1.1 percent of GDP), and non-accumulation of domestic arrears (missed by less than 0.01 percent of GDP in December 2011, by 0.05 percent in January 2012, and by 0.09 percent in February 2012). The waiver on the government balance is justified by the corrective actions (commitment to

a budget surplus in 2012 guided by quarterly targets beyond program end, agreed with staff). The waiver on net credit to the government is justified by the temporary nature of the deviation, which was caused by the one-off increase in the annual domestic arrears repayment, and the remedial actions (commitment to a budget surplus which would lead to the strengthening the government's position vis-à-vis the banking system). The waiver on domestic arrears is justified by the minor deviation from program objectives.

27. **The authorities confirmed their strong interest in a successor program.** During the mission, the authorities and staff held preliminary discussions on the objectives and timing of a possible successor arrangement. Staff underlined the importance of pursuing sound policies after the end of the ECF, and to this end, proposed quarterly quantitative indicative targets to end-2012, which the authorities agreed to follow.

28. **The program is fully financed.** Over the remaining program period, the authorities are expected to mobilize sufficient exceptional financing from multilateral and bilateral creditors on concessional terms. Donors will continue to support Djibouti mainly through grant and loan project financing, while expected budget support is relatively limited. However, given the high current account deficit and the possible delays in the donor meeting, financing needs may arise in the second half of 2012.

29. **The program and policy implementation beyond the ECF expiration in June are vulnerable to a number of risks:**

- *Wavering political commitment*, resulting from vested interests or a flare-up of domestic social unrest, among other causes;
- *Administrative capacity constraints*, combined with shortfalls in technical assistance from donors, which could possibly affect the authorities' ability to implement reform;
- *Slowdown in growth* driven by a fall in activity in Ethiopia or a worldwide growth slump, given Djibouti's economic reliance on traffic through the Suez Canal;
- *Diversion of shipping to other ports in the region,* in particular Aden following the improvement of security in Yemen; and
- *Fall in international reserves to unsustainable levels*—threatening currency board coverage—in case capital inflows and official financing are insufficient to finance the high current account deficit.

V. STAFF APPRAISAL

30. **The program is broadly on track**. Despite the impact of the commodity price shock and the drought—which keeps affecting Djibouti—the authorities have maintained spending discipline, made sufficient progress on their structural reform program, and committed to

strong policies for 2012. The 2011 program outcome deviated from the end-December 2011 performance criteria for the budget balance and net credit to the government set in CR/12/169 (6/24/11). However, staff considers that the broad objectives of the program continue to be met given that the 2011 outcome is in line with the revised framework agreed with the authorities and endorsed by Directors at the approval of the fifth review.

31. **Staff therefore supports the authorities' requests for the completion of the sixth review and the waivers of nonobservance of performance criteria.** Staff supports the waivers for the nonobservance of the end-December performance criteria on the budget balance and net credit to the government, and of the continuous performance criterion on the non-accumulation of domestic arrears, in light of the minor deviations from the program objectives and the corrective actions undertaken by the authorities.

32. **Under the currency board regime, which has served the country well, macroeconomic stability hinges on sound fiscal policy.** Staff welcomes the authorities' commitment to a budget surplus of 0.5 percent of GDP for 2012, which will depend on continued efforts to raise tax collection and resist spending pressures. The higher-than-programmed repayment of domestic arrears in 2011 will help restore the public enterprises' balance sheets, but financing from the budget rather than the banking sector would have been preferable. The lack of consultation with staff before taking this major decision is disappointing.

33. **Reform of the fiscal sector is essential.** Given the importance of exemptions reform, it is unfortunate that the obligation for tax-exempted companies to submit tax returns could not be enforced, even though the publication of the list of these enterprises has to be welcome as a step toward the calculation of tax expenditures. The plans for reform of the fuel subsidy will help to contain budget spending and better target the needs of the poor. However, the authorities should also improve transparency of the opaque food subsidy system.

34. **The CBD should continue focusing on the implementation of the banking law and the possible governance issues in the banking sector.** The financial system appears sound, but, in light of high credit growth and the increase in the number of banks in recent years, the authorities should carefully monitor banking sector developments and be vigilant toward the increase in risks and possible governance issues in the banking sector. They should also be alert to a possible reversal in the positive money and credit trends, which may be heralded by last year's contraction in broad money.

35. **Staff is ready to discuss a possible successor program.** The completion of the review presents an important opportunity for the authorities to take stock of the implementation of the ECF and reflect on the objectives for a successor program. In the period before a new arrangement, the implementation of sound policies, particularly in the fiscal area, the continued reliance on concessional financing, and the completion of the outstanding structural benchmarks will be critical.

Table 1. Djibouti: Selected Economic and Financial Indicators, 2009–17

(Quota: SDR 15.9 million)
(Population: 0.818 million; 2009)
(Per capita nominal GDP: $1,383; 2010)
(Poverty rate: 42 percent; 2002)

	2009	2010	2011	2012	2013	2014	2015	2016	2017
	Act.	Act.	Prel. Est.	Proj.					
	(Annual percent change, unless otherwise indicated)								
National accounts									
Real GDP (annual change in percent)	5.0	3.5	4.5	4.8	5.0	5.0	5.5	5.8	5.8
Consumer prices (annual average)	1.7	4.0	5.1	4.3	2.5	2.5	2.5	2.5	2.5
Consumer prices (end of period)	2.2	2.8	7.6	2.0	1.3	2.3	2.3	2.3	2.3
	(In percent of GDP)								
Investment and saving									
Total fixed capital investment	35.5	20.8	24.6	27.2	32.4	32.7	33.2	35.0	35.2
Private	18.3	9.0	13.5	15.5	19.8	19.6	19.8	21.0	20.0
Public	17.2	11.7	11.1	11.7	12.6	13.1	13.4	14.0	15.2
Gross national savings	26.4	14.9	12.0	15.1	20.5	21.8	23.4	24.8	25.9
Savings/investment balance	-9.1	-5.8	-12.6	-12.1	-11.9	-10.9	-9.8	-10.2	-9.4
Public finances									
Total revenue and grants	37.0	35.5	34.5	35.8	35.9	36.0	36.0	36.0	36.1
Of which: Tax revenue	20.1	20.2	20.3	20.9	21.9	22.7	23.0	23.4	23.7
Expenditure and net lending 1/	41.6	36.0	35.2	35.4	35.0	35.2	35.3	35.5	36.1
Of which: Current expenditure	36.1	24.3	24.1	23.7	22.4	22.1	21.9	21.5	20.9
Investment expenditure	5.5	11.7	11.1	11.7	12.6	13.1	13.4	14.1	15.2
Overall balance (commitment basis, incl. grants) 1/	-4.6	-0.5	-0.7	0.5	0.9	0.8	0.7	0.5	0.0
Domestic financing	-0.2	0.1	0.9	-1.1	-1.7	-1.3	-1.7	-2.1	-2.0
External financing	5.9	1.3	1.7	1.4	1.7	1.3	1.7	2.1	2.0
Change in domestic arrears (decrease -) 2/	-1.2	-0.8	-2.0	-0.7	-0.9	-0.8	-0.7	-0.5	0.0
	(Annual percent change, unless otherwise indicated)								
Monetary sector									
Net foreign assets	12.1	5.1	-10.5	7.6	5.5	6.0	6.0	6.1	6.2
Net domestic assets	43.2	38.4	12.5	4.1	12.3	11.2	12.6	13.0	12.5
Claims on the private sector	26.6	21.4	2.5	9.3	15.0	15.0	15.0	15.0	15.0
Broad money	17.5	12.2	-4.5	6.5	7.5	7.6	8.1	8.4	8.4
Velocity of broad money (ratio)	1.1	1.1	1.2	1.3	1.3	1.3	1.3	1.3	1.3
Average commercial lending interest rate (in percent)	11.7	10.1	…	…	…	…	…	…	…
	(In millions of U.S. dollars, unless otherwise indicated)								
External sector									
Exports of goods and services	399	359	471	511	560	600	648	719	805
Imports of goods and services	-578	-509	-697	-753	-807	-823	-830	-905	-970
Current account balance (in percent of GDP)	-9.1	-5.8	-12.6	-12.1	-11.9	-10.9	-9.8	-10.2	-9.4
FDI in percent of GDP	9.5	2.4	6.3	8.1	12.4	12.1	12.4	12.5	11.6
Stock of external public and publicly guaranteed debt (in percent of GDP)	59.8	56.1	52.3	51.3	53.5	53.0	52.3	51.6	49.2
Gross official reserves 3/	218	231	228	245	272	305	341	382	428
(in months of next year's imports of goods and services)	5.1	4.0	3.6	3.6	4.0	4.4	4.5	4.7	4.6
Memorandum items:									
Nominal GDP (in millions of Djibouti francs)	186,447	200,578	220,222	240,567	258,719	278,386	300,988	326,318	353,830
Currency board cover (in percent) 4/	135.4	122.4	117.0	119.9	118.7	121.8	118.8	113.7	110.4
Exchange rate (DF/US$) end-of-period	177.7	177.7	177.7	…	…	…	…	…	…
Real effective exchange rate (yearly average, 2005=100)	94.9	100.6	96.8	…	…	…	…	…	…
(Change in percent; depreciation -)	8.0	6.0	-3.8	…	…	…	…	…	…

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ In 2009 includes externally financed projects of public enterprises guaranteed by the government, amounting to 3.7 percent of GDP.

2/ Does not include repayment of arrears to public enterprises accumulated in 2009. Repayment of these arrears is included in current expenditure in 2010–12 .

3/ In 2009, includes special and general allocation of SDR 14 million.

4/ Gross foreign assets of the CBD in percent of monetary liabilities (reserve money and government deposits at CBD).

Table 2. Djibouti: Central Government Fiscal Operations, 2009–12

(In millions of Djibouti francs)

	2009	2010	2011				2012
	Act.	Act.	Prel. Est.	CR/12/169	Rev. Target	Prel. Est.	Proj.
			Q2	Q4			
Revenues and grants	68,953	71,124	33,329	81,299	77,295	75,992	86,142
Tax revenue	37,449	40,582	19,840	46,001	45,392	44,630	50,339
Direct taxes 1/	17,229	18,726	9,485	20,603	20,258	20,477	22,407
Indirect and other taxes	20,220	21,857	10,355	25,398	25,134	24,153	27,932
Indirect taxes	18,330	19,828	9,223	22,947	22,683	21,911	24,906
Other taxes	1,890	2,029	1,132	2,451	2,451	2,242	3,026
Nontax domestic revenues	9,010	8,872	4,054	9,621	6,117	6,981	9,618
Nontax external revenues 2/	10,546	10,965	6,373	12,736	12,736	10,554	10,268
Grants	11,948	10,705	3,062	12,941	13,050	13,315	15,918
Development projects	9,798	9,831	2,646	9,713	9,713	10,606	12,446
Budget support for current expenditures	2,150	874	416	3,228	3,337	2,709	3,472
Total expenditure 3/	77,483	72,140	33,707	80,416	78,233	77,515	85,059
Current expenditure	45,362	48,649	24,682	53,864	53,705	53,096	56,968
Wages and related expenditure	24,058	25,464	13,584	27,231	27,231	27,281	29,009
Wages and contributions	21,634	22,911	12,239	24,555	24,555	24,584	26,178
Housing subsidies	2,424	2,553	1,345	2,676	2,676	2,697	2,831
Goods and services	13,122	14,359	6,439	15,684	15,384	16,007	16,148
Of which: repayment of arrears to public enterprises 4/	0	500	0	1,300	1,300	1,300	1,000
Civil expenditure	10,700	11,349	5,896	12,657	12,657	13,347	13,416
Of which: extrabudgetary spending	0	0	0	0	0	0	0
Military expenditure 5/	2,422	3,010	543	3,027	2,727	2,660	2,732
Maintenance	650	1,152	258	1,354	1,354	1,081	1,474
Transfers 6/	803	745	385	7,139	7,139	946	1,085
Interest	803	745	385	1,005	1,037	946	1,085
Foreign-financed current spending	1,201	874	416	1,451	1,560	932	1,695
Investment expenditure	32,121	23,491	9,025	26,552	24,528	24,419	28,091
Domestically financed	10,181	10,068	3,375	10,024	8,000	7,865	8,962
Of which: extrabudgetary spending	0	0	0	0	0	0	0
Foreign-financed	21,940	13,423	5,650	16,528	16,528	16,554	19,129
Grants	9,798	9,831	2,646	9,713	9,713	10,606	12,446
Loans	12,142	3,592	3,004	6,815	6,815	5,948	6,683
Overall balance (commitment basis, incl. grants) 3/	-8,530	-1,016	-378	883	-938	-1,523	1,083
Overall balance (commitment basis, excl. grants)	-20,478	-11,721	-3,440	-12,058	-13,988	-14,838	-14,835
Change in arrears (cash payments = -)	-2,154	-1,626	-734	-2,800	-2,800	-4,318	-1,700
Repayment of domestic arrears 7/	-2,174	-1,603	-733	-2,800	-2,800	-4,342	-1,700
External arrears (interest)	-47	-23	-1	0	0	-15	0
Debt relief on interest payments	67	0	0	0	0	39	0
Overall balance (cash basis, incl. grants)	-10,684	-2,642	-1,112	-1,917	-3,738	-5,841	-617
Financing	10,666	2,698	1,269	1,917	3,738	5,910	617
Domestic financing (net)	-424	158	-597	-2,696	-875	2,091	-2,712
Bank financing	-328	254	-549	-2,600	-779	2,187	-2,616
Central bank	-1,594	842	305	-1,600	75	1,101	-1,116
Commercial banks	1,266	-588	-854	-1,000	-854	1,086	-1,500
Nonbank financing	-96	-96	-48	-96	-96	-96	-96
External financing (net)	11,090	2,540	1,866	4,613	4,613	3,819	3,329
Disbursements	12,142	3,592	3,004	6,815	6,815	5,948	6,683
Amortization payments	-1,052	-1,052	-1,138	-2,202	-2,202	-2,129	-3,354
Discrepancy	-18	56	157	0	0	-1	0
Memorandum items:							
Current expenditure for social purposes 7/	25,864	13,161	6,541	14,451	12,829	13,474	15,574
Base fiscal balance 8/	-7,883	-8,389	-3,747	-5,515	-7,336	-7,118	-2,978
Domestic revenue	46,459	49,454	23,894	55,622	51,509	51,611	59,957
Domestically financed expenditure	54,342	57,843	27,641	61,137	58,845	58,729	62,935

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ Includes €7.5 million of ITS personal income taxes from the French millitary, as per leasing agreement.

2/ Annual leasing fees from French (€30 million) and US (US$30 million) military bases, which include the payment of TIC. on behalf of French soldiers. From Q3 2010, includes US$3 million from Japanese military base.

3/ In 2009, includes externally financed projects of public enterprises guaranteed by the government, amounting to 3.7 percent of GDP.

4/ In 2010–12 includes the repayment of arrears to public enterprises accumulated in 2009.

5/ Includes €5 million (out of a total of €30 million) of foreign-financed current spending from French military as per leasing agreement. The budget classifies this amount as domestic investment spending.

6/ Excludes housing subsidies.

7/ Revised from 2010 to exclude salaries. In 2011 includes only social spending as defined in TMU.

8/ Defined as domestic revenue minus expenditure financed from domestic sources.

Table 3. Djibouti: Central Government Fiscal Operations, 2009–12

(In percent of GDP)

	2009	2010	2011				2012
	Act.	Act.	Prel. Est.	CR/12/169	Rev. Target	Prel. Est.	Proj.
			Q2		Q4		
Revenues and grants	37.0	35.5	15.1	35.6	35.1	34.5	35.8
Tax revenue	20.1	20.2	9.0	20.2	20.6	20.3	20.9
Direct taxes 1/	9.2	9.3	4.3	9.0	9.2	9.3	9.3
Indirect and other taxes	10.8	10.9	4.7	11.1	11.4	11.0	11.6
Indirect taxes	9.8	9.9	4.2	10.1	10.3	9.9	10.4
Other taxes	1.0	1.0	0.5	1.1	1.1	1.0	1.3
Nontax domestic revenues	4.8	4.4	1.8	4.2	2.8	3.2	4.0
Nontax external revenues 2/	5.7	5.5	2.9	5.6	5.8	4.8	4.3
Grants	6.4	5.3	1.4	5.7	5.9	6.0	6.6
Development projects	5.3	4.9	1.2	4.3	4.4	4.8	5.2
Budget support for current expenditures	1.2	0.4	0.2	1.4	1.5	1.2	1.4
Total expenditure	41.6	36.0	15.3	35.3	35.5	35.2	35.4
Current expenditure	24.3	24.3	11.2	23.6	24.4	24.1	23.7
Wages and related expenditure	12.9	12.7	6.2	11.9	12.4	12.4	12.1
Wages and contributions	11.6	11.4	5.6	10.8	11.1	11.2	10.9
Housing subsidies	1.3	1.3	0.6	1.2	1.2	1.2	1.2
Goods and services 3/	7.0	7.2	2.9	6.9	7.0	7.3	6.7
Of which: repayment of arrears to public enterprises 4/	0.0	0.2	0.0	0.6	0.6	0.6	0.4
Civil expenditure	5.7	5.7	2.7	5.5	5.7	6.1	5.6
Of which: extrabudgetary spending	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Military expenditure 5/	1.3	1.5	0.2	1.3	1.2	1.2	1.1
Maintenance	0.3	0.6	0.1	0.6	0.6	0.5	0.6
Transfers 6/	0.4	0.4	0.2	3.1	3.2	0.4	0.5
Interest	0.4	0.4	0.2	0.4	0.5	0.4	0.5
Foreign-financed current spending	0.6	0.4	0.2	0.6	0.7	0.4	0.7
Investment expenditure	17.2	11.7	4.1	11.6	11.1	11.1	11.7
Domestically financed 5/	5.5	5.0	1.5	4.4	3.6	3.6	3.7
Of which: extrabudgetary spending	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign-financed	11.8	6.7	2.6	7.2	7.5	7.5	8.0
Grants	5.3	4.9	1.2	4.3	4.4	4.8	5.2
Loans	6.5	1.8	1.4	3.0	3.1	2.7	2.8
Overall balance (commitment basis, incl. grants) 3/	-4.6	-0.5	-0.2	0.4	-0.4	-0.7	0.5
Overall balance (commitment basis, excl. grants) 3/	-11.0	-5.8	-1.6	-5.3	-6.3	-6.7	-6.2
Change in arrears (cash payments = -)	-1.2	-0.8	-0.3	-1.2	-1.3	-2.0	-0.7
Overall balance (cash basis)	-5.7	-1.3	-0.5	-0.8	-1.7	-2.7	-0.3
Financing	5.7	1.3	0.6	0.8	1.7	2.7	0.3
Domestic financing (net)	-0.2	0.1	-0.3	-1.2	-0.4	0.9	-1.1
Bank financing	-0.2	0.1	-0.2	-1.1	-0.4	1.0	-1.1
Central bank	-0.9	0.4	0.1	-0.7	0.0	0.5	-0.5
Commercial banks	0.7	-0.3	-0.4	-0.4	-0.4	0.5	-0.6
Nonbank financing	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
External financing (net)	5.9	1.3	0.8	2.0	2.1	1.7	1.4
Disbursements	6.5	1.8	1.4	3.0	3.1	2.7	2.8
Amortization payments	-0.6	-0.5	-0.5	-1.0	-1.0	-1.0	-1.4
Discrepancy	0.0	0.0	0.1	0.0	0.0	0.0	0.0
Memorandum items:							
GDP 7/	186,447	200,578	220,222	228,098	220,440	220,222	240,567
Base fiscal balance 8/	-4.2	-4.2	-1.7	-2.4	-3.3	-3.2	-1.2
Domestic revenue	24.9	24.7	10.8	24.4	23.4	23.4	24.9
Domestically financed expenditure	29.1	28.8	12.6	26.8	26.7	26.7	26.2

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ Includes €7.5 million of ITS personal income taxes from the French military, as per leasing agreement.

2/ Annual leasing fees from French (€30 million) and United States (US$30 million) military bases, which include the payment of TIC on behalf of French soldiers. From Q3 2010, includes US$3 million from Japanese military base.

3/ In 2009, includes externally financed projects of public enterprises guaranteed by the government amounting to 3.7 percent of GDP.

4/ In 2010–12 includes the repayment of arrears to public enterprises accumulated in 2009.

5/ Includes €5 million (out of a total of €30 million) of foreign-financed current spending from French military as per leasing agreement. The budget classifies this amount as domestic investment spending.

6/ Excludes housing subsidies.

7/ 2010 GDP was revised compared to program.

8/ Defined as domestic revenue minus expenditure financed from domestic sources.

Table 4. Djibouti: Balance of Payments, 2009–12
(In millions of U.S. dollars, unless otherwise indicated)

	2009	2010	2011			2012
	Act.	Act.	CR/12/169	Rev. Target	Prel. Est.	Proj.
Current account (including grants)	-95	-66	-133	-145	-156	-164
(In percent of GDP)	-9.1	-5.8	-10.4	-11.7	-12.6	-12.1
Credit	399	359	472	483	471	511
Exports of goods, f.o.b.	77	81	120	127	126	117
Exports of services	322	278	353	356	345	394
Of which: services to foreign military bases	180	187	218	216	193	206
maritime transportation	66	35	52	52	62	79
Debit	-578	-509	-679	-713	-697	-753
Imports of goods, f.o.b.	-451	-376	-520	-554	-536	-577
Of which: investment goods	-198	-75	-95	-94	-115	-136
crude oil and petroleum products	-86	-155	-161	-171	-182	-210
drought-related	…	…	…	17	19	27
Imports of services	-128	-134	-159	-159	-161	-175
Net income from abroad 1/	81	84	71	70	54	54
Of which: income related to the lease of military bases	59	62	72	72	59	58
Net current transfers from abroad	3	0	3	15	16	24
Private (net)	-8	-9	-9	-9	-9	-9
Official (net)	11	9	12	24	25	33
drought-related	…	…	…	12	16	19
Capital and financial account 2/ 3/	131	66	121	124	207	144
Net capital transfers	58	67	21	40	21	29
Foreign direct investment	100	27	92	72	78	110
Public sector (net)	30	-7	41	42	33	61
Disbursements	49	17	68	70	64	96
Repayments	-19	-24	-27	-27	-31	-35
Of which: Eligible for Paris Club rescheduling	-7	-5	-2	-2	-2	0
Commercial banks (- = increase in NFA)	-56	-21	-33	-30	75	-56
SDR allocation	21	…	…	…	…	…
Errors and omissions	-47	-15	0	0	-72	0
Overall balance (deficit -)	9	9	-11	-21	-21	-20
Financing	-9	-9	11	21	21	20
Central bank	-27	-17	-13	0	6	3
Assets	-44	-13	-12	1	2	-17
Liabilities	17	-4	-1	-1	4	19
Of which: SDR allocation	-21	…	…	…	…	…
Of which: ECF financing	2	0	9	7	7	19
Of which: ECF augmentation	…	…	…	0	0	15
Exceptional financing	13	8	14	14	14	10
Budget support from donors (grants and loans)	0	0	10	10	10	10
Change in overdue obligations (decrease-)	0	0	0	0	0	0
Expected debt relief	9	8	4	4	4	0
Paris Club	7	5	2	2	2	0
Non-Paris Club	3	3	2	2	2	0
Unidentified financing	… . .	… .	…	…	…	7
Memorandum items:						
Central bank gross foreign assets 3/	217.5	230.6	242.1	239.5	228.3	245
In months of next year's imports of goods and services	5.1	4.0	3.8	3.7	3.6	3.6
Currency board cover	135.4	122.4	115.6	125.8	117.0	119.9
FDI in percent of GDP	9.5	2.4	7.2	5.8	6.3	8.1
Drought-related external assistance	…	…	…	19.0	18.8	27.0
Official external debt (including public and publicly guaranteed debt)						
In millions of U.S. dollars	627	634	680	678	648	694
In percent of GDP	59.8	56.1	53.0	54.6	52.3	51.3
In percent of exports of goods and services	157	176	144	140	138	136
Debt service						
In millions of U.S. dollars	25	28	34	35	35	51
In percent of GDP	2.4	2.5	2.6	2.8	2.8	3.8
In percent of exports of goods and services	6.3	7.8	7.2	7.2	7.5	10.1

Sources: Djibouti authorities; and IMF staff estimates and projections.
1/ Includes the French and U.S. contributions for the military bases and outflows of interest due on Paris and non-Paris Club debt.
2/ Excludes exceptional financing.
3/ In 2009, includes special and general allocation of SDR 14 million.

Table 5. Djibouti: Monetary Survey and Banking Sector Indicators, 2008–12

(End-of-period, in millions of Djibouti francs, unless otherwise indicated)

	2008	2009	2010	2011			2012
	Act.	Act.	Act.	CR/12/169	Rev. Target	Prel. Est.	Proj.
Broad money	142,310	167,191	187,589	201,857	195,079	179,209	190,926
Currency in circulation	17,624	19,629	20,084	21,612	19,886	20,349	20,263
Deposits	124,686	147,562	167,505	180,245	175,194	158,860	170,663
Demand deposits	64,612	83,049	107,207	115,361	112,128	102,746	110,380
Djibouti francs	40,296	62,511	72,251	77,746	75,567	63,125	67,815
Foreign currency	24,316	20,538	34,956	37,615	36,560	39,621	42,565
Time deposits	60,074	64,513	60,298	64,884	63,066	56,114	60,283
Djibouti francs	38,238	23,497	18,657	20,076	19,513	17,784	19,105
Foreign currency	21,836	41,016	41,641	44,808	43,552	38,330	41,178
Net foreign assets	117,498	131,667	138,414	144,778	142,579	123,890	133,330
Central bank	27,093	31,286	34,322	34,893	33,089	33,171	32,709
Assets 1/	30,873	38,658	40,979	43,034	42,560	40,571	43,541
Liabilities 1/	3,780	7,371	6,657	8,141	9,471	7,400	10,832
Commercial banks	90,405	100,381	104,092	109,884	109,490	90,719	100,621
Assets	102,308	119,169	132,369	140,311	139,064	122,994	135,293
Liabilities	11,903	18,788	28,277	30,427	29,574	32,275	34,672
Net domestic assets	24,812	35,524	49,175	57,079	52,500	55,319	57,596
Claims on government (net)	3,236	2,908	3,161	561	2,382	5,348	2,732
Central bank	1,459	-135	706	-894	781	1,807	691
Commercial banks	1,777	3,043	2,455	1,455	1,601	3,541	2,041
Claims on nongovernment sector	44,730	57,342	69,058	77,294	72,297	70,407	76,738
Public enterprises	1,519	2,625	2,646	2,665	2,665	2,339	2,355
Private sector	43,211	54,717	66,412	74,629	69,633	68,068	74,382
Capital accounts	-9,786	-10,697	-11,187	-11,912	15,179	-14,935	-16,097
Other items (net)	-13,368	-14,029	-11,857	-8,864	-11,912	-5,501	-5,776
	Change from previous year; in percent of broad money						
Broad money	20.6	17.5	12.2	7.6	4.0	-4.5	6.5
Currency in circulation	1.8	1.4	0.3	0.8	-0.1	0.1	0.0
Net foreign assets	18.7	10.0	4.0	3.4	2.3	-7.7	5.3
Central bank	6.3	2.9	1.8	-1.7	-2.7	-0.6	-0.3
Commercial banks	12.3	7.0	2.2	3.1	2.9	-7.1	5.5
Net domestic assets	1.9	7.5	8.2	4.2	1.7	3.3	1.3
Of which: Claims on government (net)	-0.8	-0.2	0.2	-2.2	-0.4	1.2	-1.5
Claims on nongovernment sector	7.7	8.9	7.0	4.4	1.7	0.7	3.5
Memorandum items:							
Monetary authorities							
Net international reserves (in U.S. dollars million) 1/	30.0	34.9	20.6	32.7	49.2	11.7	19.2
Gross foreign assets (in U.S. dollars million) 1/	173.7	217.5	230.6	242.1	239.5	228.3	245.0
In percent of foreign currency deposits	66.9	62.8	53.5	52.2	53.1	52.0	52.0
In percent of total deposits	24.8	26.2	24.5	23.9	24.3	25.5	25.5
Banking system							
Credit to the private sector, 12-month percent change	27.3	26.6	21.4	12.4	4.8	2.5	9.3
Money velocity	1.2	1.1	1.1	1.1	1.1	1.2	1.3

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ In 2009, includes special and general allocation of SDR 14 million.

Table 6. Djibouti: Financial Soundness Indicators, 2000–11

(In percent, unless otherwise indicated)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Capital adequacy												
Tier I capital to risk-weighted assets	17.3	18.5	21.7	19.1	15.0	15.7	17.4	14.1	8.9	11.0	12.2	9.4
Regulatory capital to risk-weighted assets	2.3	2.6	2.5	2.7	2.1	2.0	4.2	14.1	8.9	11.0	12.2	9.4
Reported total capital to risk weighted assets (K1-1)	114.2	99.5	96.5	104.5	101.5	106.2	102.7	80.9	85.4	86.4	112.3	44
Asset quality 1/												
Nonperforming loans to gross loans	19.7	26.9	30.6	29.2	28.8	27.8	15.6	16.0	12.4	9.3	8.3	9.4
Nonperforming loans net of provisions to capital	49.6	50.4	59.0	60.5	67.0	73.7	23.5	22.6	20.8	18.0	15.9	17.3
Provisions to nonperforming loans	54.7	55.5	52.3	52.5	55.1	56.6	74.9	77.2	77.4	76.4	75.1	77
Banks exceeding maximum single borrower limit 2/	1	0	0	2	1	0	1	1	1	2	5	7
Earning and profitability												
Reported return on assets (ROA)	4.8	4.2	2.1	2.8	2.1	1.9	1.8	1.8	1.7	1.8	1.1	1
Reported return on equity (ROE) 3/	13.1	11.7	7.9	8.5	21.1	28.2	43.9	43.2	43.3	45.6	26.9	26.6
Interest margin to gross income	33.5	31.7	26.3	22.3	22.7	40.5	49.9	68.8	68.7	68.9	75.6	78.6
Noninterest expenditures to gross income	59.0	60.0	64.7	71.2	72.2	59.1	47.6	54.1	52.2	40.1	56.8	49.7
Salary expenditures to non-interest expenditures	60.9	62.9	61.8	60.7	54.0	56.6	56.4	47.6	46.6	59.9	59.7	56.6
Liquidity												
Liquid assets to total assets	47.5	58.5	64.9	70.5	74.3	76.6	75.4	72.4	69.5	65.8	65.1	61.2
Liquid assets to short-term liabilities	285.6	455.1	494.0	726.0	710.5	736.2	670.3	155.3	148.0	124.7	120.7	112.3
Liquid assets to demand and saving deposits	164.0	180.1	188.7	175.8	209.1	226.6	597.9	170.4	164.6	183.8	211.0	213.2
Liquid assets to total deposits	61.4	72.0	78.8	81.4	85.4	87.7	87.1	81.2	77.9	74.3	76.8	73.6

Source: Central Bank of Djibouti; and IMF staff estimates.

1/ Nonperforming loans include three loan classifications: watch, doubtful, and loss. Revised from 2006 to exlcude old NPLs of a liquidated bank.
2/ Maximum single borrower limit is defined as 25 percent of capital (K3-1).
3/ Based on minimum capital.

Table 7. Djibouti: Millennium Development Goals, 1990–2015

	1990	1995	2000	2005	2007	2008	2015 Goal
Goal 1: Eradicate extreme poverty and hunger							
Employment to population ratio, ages 15-24, total (percent)	..	..	..	..	..	..	..
Malnutrition prevalence, weight for age (percent of children under 5)	..	..	..	..	..	..	..
Pupulation below $2 per day (in percent)				43			28
Prevalence of undernourishment (percent of population)	53	..	..	24	..	..	..
Goal 2: Achieve universal primary education							
Literacy rate, youth female (percent of females ages 15-24)	..	..	..	..	..	..	..
Literacy rate, youth male (percent of males ages 15-24)	..	..	..	..	..	..	..
Persistence to last grade of primary, total (percent of cohort)	..	..	..	..	..	..	..
Primary completion rate, total (percent of relevant age group)	32	29	28	31	..	41	..
Total enrollment, primary (percent net)	..	..	27	35	42	..	..
Goal 3: Promote gender equality and empower women							
Proportion of seats held by women in national parliaments (percent)	0	..	0	11	11	14	
Ratio of female to male primary enrollment (percent)	73	77	73	82	86	88	..
Ratio of female to male secondary enrollment (percent)	..	..	66	66	69	70	100
Ratio of female to male tertiary enrollment (percent)	..	..	89	73	69	..	..
Primary completion rate, total (percent of relevant age group)	32		28		35		100
Share of women employed in the nonagricultural sector (percent of total nonagricultural employmen	..	..	..	..	..	..	..
Goal 4: Reduce child mortality							
Immunization, measles (percent of children ages 12-23 months)	85	41	50	65	74	73	..
Mortality rate, infant (per 1,000 live births)	95	89	84	79	77	76	..
Mortality rate, under-5 (per 1,000)	123	114	106	99	96	95	58
Goal 5: Improve maternal health							
Contraceptive prevalence (percent of women ages 15-49)	..	..	..	..	..	23	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	730	650	..	..	130
Goal 6: Combat HIV/AIDS, malaria, and other diseases							
Incidence of tuberculosis (per 100,000 people)	619	619	619	619	619	619	..
Prevalence of HIV, female (percent ages 15-24)	..	..	..	..	2	..	..
Prevalence of HIV, male (percent ages 15-24)	..	..	..	..	1	..	..
Prevalence of HIV, total (percent of population ages 15-49)	0	2	3	3	3	..	..
Tuberculosis case detection rate (all forms)	61	..	88	62	62	70	..
Goal 7: Ensure environmental sustainability							
CO2 emissions (kg per PPP $ of GDP)	0	0	0	0	..	..	..
CO2 emissions (metric tons per capita)	1	1	1	1	..	..	..
Forest area (percent of land area)	0	0	0	0	0	..	..
Improved sanitation facilities (percent of population with access)	..	..	65	..	..	..	..
Improved water source (percent of population with access)	76	78	83	..	..	..	..
Marine protected areas (percent of total surface area)	..	..	..	..	..	0	..
Goal 8: Develop a global partnership for development							
Debt service (PPG and IMF only, percent of exports, excluding workers' remittances)	..	5	6	5	7	6	..
Internet users (per 100 people)	0	0	0	1	2	2	..
Mobile cellular subscriptions (per 100 people)	0	0	0	5	8	13	..
Telephone lines (per 100 people)	1	1	1	1	2	2	..
Other							
Fertility rate, total (births per woman)	6	5	5	4	4	4	..
GNI per capita, Atlas method (current US$)	..	820	760	1,000	1,070	1,130	..
GNI, Atlas method (current US$)	..	1	1	1	1	1	..
Gross capital formation (percent of GDP)	14	8	9	19	39	..	..
Life expectancy at birth, total (years)	51	52	54	54	55	55	..
Literacy rate, adult total (percent of people ages 15 and above)	..	..	..	..	..	..	..
Population, total	560,279	623,798	729,561	804,940	834,291	849,245	..
Trade (percent of GDP)	132	90	85	92	139	..	..

Sources: World Development Indicators database, September 2010.

Table 8. Djibouti : Reviews and Disbursements, 2008–12

Date	Action/Status	Disbursement	In percent of Quota 1/
September 2008	Board Approval of ECF arrangement.	3.864 million SDR	24.00
June 2009	First review completed (June 2009) on end-December 2008 performance criteria.	1.476 million SDR	9.28
December 2010	Second and third reviews completed (January 2011) on end-June and end-December 2009 performance criteria.	2.952 million SDR	18.56
June 2011	Fourth review completed (July 2011) on end-December 2010 performance criteria.	1.476 million SDR	9.28
February 2012	Fifth review completed (February 2012) on end-June 2011 performance criteria.	6.246 million SDR 2/	39.28
May 2012	Completion of the sixth review on end-December 2011 performance criteria.	6.246 million SDR 2/	39.28
	Total	22.260 million SDR	140.00

Source: IMF staff estimates and projections.

1/ Djibouti's quota is SDR 15.9 million.
2/ Includes the ECF augmentation of SDR 9.54 million or 60 percent of quota.

Table 9. Djibouti: Indicators of Capacity to Repay the Fund, 2007–22

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
						Projections										
Fund obligations based on existing credit																
(in millions of SDRs)																
Principal	1.82	2.73	2.73	2.18	1.64	0.91	-	0.92	1.07	1.36	2.58	3.20	2.28	2.13	1.84	0.62
Charges and interest	0.09	0.08	0.06	0.01	-	0.01	0.01	0.05	0.05	0.04	0.04	0.03	0.02	0.02	0.01	0.01
Fund obligations based on existing and prospective credit																
(in millions of SDRs)																
Principal	1.82	2.73	2.73	2.18	1.64	0.91	-	0.92	1.07	1.36	3.20	4.45	3.53	3.38	3.09	1.25
Charges and interest	0.09	0.08	0.06	0.01	-	0.01	0.01	0.06	0.06	0.06	0.05	0.04	0.03	0.02	0.02	0.01
Total obligations based on existing and prospective credit																
In millions of SDRs	1.9	2.8	2.8	2.2	1.6	0.9	0.0	1.0	1.1	1.4	3.3	4.5	3.6	3.40	3.11	1.26
In billions of DF	0.5	0.7	0.8	0.6	0.4	0.2	0.0	0.3	0.3	0.4	0.9	1.3	1.0	1.0	0.9	0.4
In percent of government revenue	1.0	1.0	1.1	0.9	0.6	0.3	0.0	0.3	0.3	0.3	0.7	1.0	0.8	0.7	0.6	0.2
In percent of exports of goods and services	0.9	1.1	1.1	1.0	0.5	0.3	0.0	0.3	0.3	0.3	0.6	0.8	0.6	0.5	0.4	0.2
In percent of debt service 1/	10.4	12.8	12.2	9.7	6.4	2.9	0.0	3.1	3.5	4.3	10.3	11.5	10.0	9.6	8.7	3.9
In percent of GDP	0.3	0.4	0.4	0.3	0.2	0.1	0.0	0.1	0.1	0.1	0.3	0.3	0.2	0.2	0.2	0.1
In percent of quota	12.0	17.6	17.5	13.8	10.3	5.8	0.1	6.2	7.1	8.9	20.4	28.2	22.4	21.38	19.56	7.92
Outstanding Fund credit																
In millions of SDRs	10.18	11.32	10.07	7.88	10.68	22.26	22.26	21.34	20.27	18.91	15.71	11.25	7.72	4.34	1.25	0.00
In billions of DF	2.77	2.96	2.74	2.22	2.93	6.04	6.25	5.85	5.56	5.19	4.41	3.16	2.17	1.22	0.35	0.00
In percent of government revenue	5.22	4.05	3.97	3.11	3.85	7.01	6.73	5.85	5.13	4.41	3.45	2.61	1.67	0.88	0.24	0.00
In percent of exports of goods and services	4.85	4.51	3.86	3.47	3.50	6.65	6.28	5.49	4.83	4.06	3.09	2.04	1.30	0.66	0.17	0.00
In percent of debt service 1/	55.23	51.71	44.22	34.76	41.89	70.27	77.55	67.32	62.62	57.40	49.66	28.74	21.69	12.20	3.51	0.00
In percent of GDP	1.84	1.69	1.47	1.10	1.33	2.51	2.41	2.10	1.85	1.59	1.25	0.84	0.54	0.28	0.08	0.00
In percent of quota	64.01	71.16	63.30	49.59	67.15	140.00	140.00	134.21	127.48	118.93	98.81	70.75	48.55	27.30	7.86	0.00
Net use of Fund credit (millions of SDRs)	-1.82	1.14	-1.25	-2.18	2.79	11.58	0.00	-0.92	-1.07	-1.36	-3.20	-4.45	-3.53	-3.38	-3.09	-1.25
Disbursements	0.00	3.86	1.48	0.00	4.43	12.49	0.00	0.00	0.00	0.00	0.00	0.00	0.00	-	-	-
Repayments and Repurchases	1.82	2.73	2.73	2.18	1.64	0.91	0.00	0.92	1.07	1.36	3.20	4.45	3.53	3.38	3.09	1.25
Memorandum items:																
Nominal GDP (in billions of DF)	151	175	186	201	220	241	259	278	301	326	354	377	405	434	465	499
Exports of goods and services (in billions of DF)	57	66	71	64	84	91	100	107	115	128	143	155	167	185	204	225
Government revenue (in billions of DF)	53	73	69	71	76	86	93	100	108	118	128	121	130	138	148	159
Debt service (in billions of DF) 1/	5	6	6	6	7	9	8	9	9	9	9	11	10	10	10	9
DF/SDR (period average)	272	261	272	281	274	271	281	274	274	274	281	281	281	281	281	281

Source: IMF staff estimates and projections.

1/ Total debt service includes IMF repurchases and repayments.

Appendix I.
Letter of Intent
and Memorandum of Economic and Financial Policies

Djibouti, May 9, 2012

Madame Christine Lagarde
Managing Director
International Monetary Fund
Washington D.C. 20431

Madame Managing Director,

1. This Letter of Intent is to inform you of the progress made by Djibouti in 2011 and in the first months of 2012 in the context of the Extended Credit Facility (ECF). It also sets out the government's intentions in the area of economic policy and the planned reforms for the remainder of 2012.

2. The objectives of the ECF-supported program remain unchanged. These objectives are consistent with our goal of making Djibouti a hub of trade, logistics and related services, and financial services. The ECF-supported program will remain aligned with the National Social Development Initiative (INDS) and is based on our national economic development and poverty reduction strategy.

3. Program implementation suffered significant disruption in 2011 owing to the exceptional drought conditions. More than 12 million people (11 percent of the population) in the Horn of Africa were affected by one of the worst droughts in 60 years, resulting in the loss of harvests and cattle. Djibouti was among the worst affected countries, along with Ethiopia, Kenya, and Somalia. In 2012, the government of Djibouti and its partners still assist more than 106,000 people and the more than 22,000 refugees who have continued to arrive. This assistance includes general food distribution and targeted supplementary feeding programs aimed at reducing and stabilizing cases of acute malnutrition, particularly in the country's five rural districts, where the persistent drought conditions have continued to exacerbate an already acute food security situation. With support from its partners, actions have focused on the rehabilitation of assets lost during the drought (restocking of herds) and on new activities designed to strengthen resilience to future shocks, such as access roads, soil and water conservation and rehabilitation, fruit and vegetable farming, and tree planting. Nonetheless, according to UNICEF, the number of new cases of malnutrition among children aged 6 to 59 months has continued to rise, and some 14,000 primary school children in rural areas are enrolled in school feeding programs. Based on available data, around 33 percent of

Djiboutians still live in high-risk areas, and 35.3 percent of the economy is vulnerable to natural risks.

4. Against that backdrop, our partners have committed to providing us with aid amounting to a total of US$65 million to assist us in dealing with this emergency situation. We have set up an interministerial drought crisis committee chaired by the Minister of the Interior, assisted by the Ministry of Finance and the Solidarity Secretariat in coordination with donors, including the IMF. Some payments on these commitments were already made in 2011, and the remainder is expected in 2012 and 2013. Most of this aid is expected to take the form of in-kind donations channeled mainly through the World Food Program (WFP).

5. The adverse effects of the drought are in addition to the strong surge in international prices of petroleum products and, more particularly, food in 2011, which have hit hard the population. To meet the exceptional financing needs resulting from these shocks, we have requested and obtained from your institution an augmentation of access to ECF resources of 60 percent of quota (SDR 9.54 million).

6. Owing to delays in the finalization of preparations for the review, it was not possible to modify the quantitative criteria for end-2011 agreed with Fund staff in the context of discussions on the fifth review. Thus, end-of-year performance will have to be assessed on the basis of the targets outlined in the Letter of Intent of January 2011, which will require waivers for failure to meet the performance criteria for technical reasons, over and above the limited deviations from the targets described below.

7. In respect of the targets agreed with Fund staff, the program remains on track, with an actual budget deficit of 0.7 percent, which is in line with the target of 0.4 percent, taking into account the program adjustments. Rigorous expenditure control in 2011 made it possible to control overall fiscal performance, which had suffered from weak collection of tax and nontax revenues during the first half of the year. However, net credit to the government deviated from the adjusted target by about 0.2 percent of GDP as a result of the faster-than-expected pace of clearance of domestic arrears (Table 1). We also accumulated small amounts of domestic arrears due mainly to delays in social security payments. The other indicative quantitative performance criteria and targets for end-December 2011 were observed. Further, no nonconcessional debt has been contracted either in 2011 or over the course of 2012.

8. Most of the structural benchmarks for 2011 and 2012 have now been completed (Table 2), with the exception of: (i) the acquisition of a software program for budget reclassification (*structural benchmark for end-December 2011*), and (ii) preparation of the list of enterprises whose exemptions have been suspended for failing to file their tax returns (*structural benchmark for end-March 2012*).

9. To achieve the objectives of the ECF, our program for 2012 continues to hinge on: (i) the pursuit of prudent fiscal policy consistent with the safeguarding of social expenditure;

(ii) the strengthening of fiscal management; (iii) the maintenance of debt sustainability; (iv) the modernization of the financial sector; and (v) the enhancement of the competitiveness of the economy through the deepening of structural reforms.

I. Economic Developments in 2011 and Outlook for 2012

10. Djibouti's economy is estimated to have grown by 4.4 percent in 2011, compared to 3.5 percent in 2010, boosted by the resumption of transshipment activity, the stabilization of the situation in Ethiopia, and intensification of the services sector, particularly banking and telecommunications (mobile telephony and internet). In 2011, inflation reached 5.1 percent, owing to the significant rise in world food and fuel prices. Competitiveness, measured by the effective exchange rate, deteriorated from 2008 to 2010 as a result of the appreciation of the Djibouti franc against the euro. The trend was reversed in 2011 because of the decline in the US dollar and the positive differential between domestic inflation and inflation rates in Djibouti's main trading partner, Ethiopia.

11. The current account deficit is estimated at 12.6 percent of GDP in 2011, up from 5.8 percent of GDP in 2010, driven by the increase in imports stemming from the impact of the drought and by the surge in world food and fuel prices. As a result of this increase, weak fiscal performance, and a resumption of FDI less vigorous than expected, reserves remained broadly unchanged at $228 million in 2011, guaranteeing adequate coverage of the currency board and imports. The stock of external debt is estimated to have declined from 56 percent of GDP at end-2010 to 55 percent at end-2011. The strong trend in credit and deposit growth seen in recent years was reversed in 2011, owing in part to election-period uncertainty, and to the situation of one bank which was changing ownership. Credit to the private sector recorded a positive growth, but deposits fell, resulting in a 5 percent fall in the money supply.

12. Growth is expected to rise to 4.8 percent in 2012, owing mainly to expanding port, construction, and service activities as well as increased FDI. Inflation is projected to fall to 4.3 percent as world food prices stabilize and electricity rates decline. Imports will continue the upward trend we saw in 2011 as a result of the impact of the drought and the rise in FDI flows. Consequently, the current account deficit is set to stabilize at a high level of 12.1 percent of GDP. However, significant capital flows should drive reserves up to $245 million, while, buoyed by the rebound in activity, monetary variables are expected to accelerate.

II. Government Finance

A. Fiscal policy

13. Our fiscal policy remains focused on three key areas, namely: fiscal rebalancing to maintain debt sustainability and nonmonetary financing of fiscal deficits; the safeguarding of fiscal space for social expenditure; and the strengthening and modernization of fiscal management.

2011 Fiscal performance

14. Fiscal performance for 2011 remained close to the targets discussed during the mission for the fifth review of the ECF.

- Collection of direct and indirect taxes was slowed by the election period, installation of the new government, and reorganization of the fiscal administration. Revenues also suffered from the indirect impact of the drought on households, including through transfers to family members, often residing in neighboring countries such as Somalia, and the contribution of private operators to solidarity efforts. In addition, owing to the steep spike in international prices, we were obliged to post losses on the petroleum price adjustment factor (*redevances*) for diesel needed to offset the impact of higher oil prices on the most vulnerable sections of the population.

- Expenditures, more particularly transfers, have been strictly controlled, so as to limit the deficit. We maintained the freeze on hiring and wages in the public sector, except in the education and health sectors.

15. In the context of the repayment of domestic arrears accumulated before 2003, we finalized the reconciliation of cross debts. On this basis, we doubled the programmed amount of settled domestic arrears to facilitate the financial consolidation process in the state-owned enterprises ONEAD, Djibouti Telecom, and EDD. This early repayment was financed domestically through financing from the BCD and the BCI (in the form of advance dividends). In 2011, we did not carry out any extrabudgetary spending and are committed to avoid any such spending in the future. We accumulated small amount of domestic arrears (between 0.01 and 0.09 percent of GDP) in December 2011, and January and February 2012, mainly due to delays in social security payments.

Fiscal policy for 2012

16. The need to strengthen the government's financial position has compelled us to go beyond the target set in the 2012 Budget Law, which envisaged a balanced budget. We envisage now a surplus of 0.5 percent of GDP. This revised target, to be formalized in the revised budget, is designed both to facilitate reconstitution of government deposits at the BCD and BCI, which declined following the scheduled repayment of domestic arrears in 2011, and to continue the domestic arrears clearance. To the extent possible, the repayment of arrears could be accelerated in the event of more robust revenue performance.

- We expect revenues to exceed 2011 levels, thanks to reform of the VAT and of exemptions as well as to the stepping-up of our tax collection efforts through more effective onsite and offsite inspection. We have included in the 2012 budget the lowering of the VAT threshold from DF 80 million to DF 50 million (*structural benchmark for December 2011*). The 2012 budget law provides for a tax of DF 3 per kilowatt/hour imported from Ethiopia to offset forgone domestic consumption tax

(TIC) revenue as a result of fuel savings made possible by the interconnection. In addition, the U.S. armed forces that were exempt from the pump prices equalization mechanism in 2011 will now pay an annual lump sum of $8 million.

- We will seek to raise our investment spending in sectors with growth potential, while pursuing fiscal restraint. In this context, we will maintain the hiring freeze in the public service, with the exception of the social sectors, in particular, education and health. We also intend to maintain the public-sector wage freeze. At the same time, we have increased wages on the lowest levels of the public-service pay scale to fight poverty by catching up with the cumulative loss of purchasing power of the lowest-paid employees. We are committed to reduce spending, in particular on domestically-financed expenditures, in the event of an underperformance of revenues.

Subsidy policy

17. To address the rise in fuel and food prices, we put in place subsidies to mitigate the effects on the most vulnerable population groups.

- Regarding the energy sector, in 2012 we plan to pursue our policy of stabilizing the diesel price by reducing both the pump price adjustment (*redevances*) and the surcharge. Thus, the 2012 budget law projects a revenue shortfall of around DF 92 million compared to potential revenues, despite the gradual but steady rise in pump prices since October 2011, amounting to a total of DF 10. Mindful that, given its budgetary constraints, the government cannot afford to continue absorbing a loss of this magnitude, we have launched a study, with the assistance of the IMF, on the introduction of social safety nets for vulnerable sectors (such as public transportation, taxis, and bakeries). We have also set the price of kerosene at a level affordable by the most vulnerable segments of the population through a subsidy of around DF 60 million for 2011.

- Regarding the food security situation, under further pressure from the drought, we count on cereal production (of around 8,000 metric tons in 2010 and 7,500 metric tons in 2011) grown in Ethiopia and Sudan and managed by the Djiboutian Food Security Company. This production is sold on the local market at subsidized prices, with the objective of stabilizing local food prices, at a budgetary cost of around DF 100 million. In the interest of increased transparency of the subsidies, we plan to prepare a summary balance sheet for FY 2010 of the food security program by end-2011. We will disclose the operating accounts of the food security company to Fund staff.

18. One of the major challenges we are facing is unemployment, which affects a significant share of our active population, and in particular, young people. With a view to achieving greater alignment between training and employers' needs, the National Education

Ministry is currently preparing a training strategy that is more targeted towards mid-level technical training programs. We have also opened a logistics training center to promote training in the skills needed to fill high-technology jobs on the port and in the transport and energy sectors. To facilitate the employment of young graduates outside the public sector, we have established a youth employment promotion fund and, through the national budget, we are financing a loan initiative for business creation. Further, we have put in place a guarantee fund for loans granted within that framework. In addition, some foreign companies operating in the country have been offering selective skills training programs abroad, to meet their own operational needs.

B. Fiscal Reforms

19. In light of the reorganization of the Ministry of Finance with an expanded scope of activities and to ensure better coordination of the actions necessary for implementation of the ECF-supported program, under the authority of the Secretary General, we have established a macroeconomic unit that has taken on the functions of the committee for program coordination. The unit will be responsible for macroeconomic analysis, follow up, within the agreed timeframes, of the program reporting documents, monitoring of the targeted program variables, and preparation of a reference macroeconomic framework for the Ministry of Finance.

Direct and indirect taxes

20. To improve the management of direct and indirect taxes, we plan to (i) strengthen the coordination between the entities responsible for managing the VAT and direct taxes through the extension, already in effect, of the single taxpayer identification number (NIF) to include enterprises subject to the declaration of direct taxes as well as to other taxpayers; (ii) strengthen the functionality of the tax center opened in 2011 in the Balbala district consistent with the policy of equipping each major region of the country with similar centers (the two regional treasuries in Ali Sabieh and Tadjourah will soon come on stream) in the context of decentralization. We have completed the full rollout of the customs revenue management software ASYCUDA *(structural benchmark for end-December 2011)*. The system now incorporates the NIF through an interface with the general tax directorate, thus improving taxpayer identification.

21. We are committed to continuing to reform the system of exemptions and, to that end, we intend to: (i) strictly apply the law, as a first step; (ii) introduce a requirement for all enterprises granted exemptions to file tax returns or face suspension of their exemptions in case of noncompliance; and (iii) assign the necessary staff to estimate the tax expenditure of the government and draft a report on tax expenditure, which will be annexed to the 2012 supplementary budget. The previously established coordination committee is to be disbanded since the various entities (ANPI, tax, customs) that deal with exemptions now fall under the authority of the Ministry of Finance. We have not yet revoked the tax exempt status of those

enterprises that failed to file their tax returns *(structural benchmark for end-March 2012).* To that end, we will compile in the coming weeks a full, updated list of enterprises granted exemptions, which we intend to review on a regular basis and publish on the website of the Ministry of Finance.

22. In the context of fiscal reform, we intend to continue our reflections on the tax system in Djibouti, in particular during the tax forum scheduled for June 2012. Our aim is to bring together the various national actors concerned, policymakers, operators and partners, to devise a tax strategy that could help boost the economy, for instance by focusing on the taxation of small and medium enterprises and by reviewing the taxation of large enterprises, as well as revising the system of exemptions.

Expenditure control and public financial management

23. In 2012, we plan to continue efforts to control public finance management by pursuing (i) a policy of transferring the balances of government accounts and of donor-financed project accounts to the treasury single account; (ii) the preparations for the establishment of a medium-term budget framework for the 2013 budget, with technical assistance from our partners, in particular the IMF and UNDP; (iii) continued publication of the monthly fiscal reporting table (TOFE) on the Ministry of Finance website within a maximum of two months (*continuous structural benchmark*); and (iv) efforts to apply the new budget classification. The acquisition of the budget nomenclature software (*structural benchmark for end-December 2011)* has been delayed once again because of the delays of our development partners in confirming their financing. We have, however, identified a potential supplier to install an integrated management system, to which the budget classification software could be added, and which could hopefully be installed by early 2013.

Arrears and cross debt

24. We remain determined to reduce the stock of domestic arrears still outstanding, including those accumulated in 1995–2001, and to prevent further accumulation, despite the absence of assistance from donors. After finalizing the recalculation of cross-debt, in 2011 we proceeded with the early repayment of DF 4,200 million in domestic arrears accumulated between 1997 and 2001 and reconciled in 2003. Based on the original timetable, the payment should have been completed in 2013. However, because of liquidity constraints, the annual repayment schedule was not always respected in past years. The balance outstanding, therefore, stands at DF 9.9 billion instead of the DF 4.4 billion initially projected. Taking into account our fiscal resources, we undertake to repay this amount over a maximum of 5 years, giving precedence to private suppliers and public enterprises. A preliminary schedule is annexed.

25. To avoid further accumulation of arrears, we will: (i) continue to implement controls on the public expenditure chain so as not to accumulate further arrears with the exception of those attributable to the one-month lag in the payment of public wages and the three-month

lag in social security contributions, which we intend to reduce depending on the availability of resources; (ii) monitor, on a regular basis, the situation of domestic arrears and the execution of payments to public utilities (which will be reported to Fund staff on a quarterly basis) in the context of the bi-monthly treasury planning exercises; and (iii) continue to remain prudent in our budget appropriations for spending related to external financing for which agreements have not yet been signed.

III. External Debt

26. Progress in relations with the Paris Club creditors has facilitated the conclusion of bilateral agreements and the entry into force of the second phase of the agreement concluded in October 2008. In accordance with the clause of comparability of treatment under the Paris Club agreement, we have signed bilateral agreements with Saudi Arabia and have approached the United Arab Emirates and Kuwait to begin negotiations with a view to obtaining treatment comparable to the Paris Club agreement.

27. Given the strained liquidity situation in the first half of 2011, more external arrears were accumulated in the course of 2011 by the government and some public enterprises vis-à-vis multilateral and bilateral creditors, including Paris Club members. These arrears were settled in the course of the last quarter of 2011. We undertake to avoid any future accumulation of external arrears, including from public enterprises, and, to that effect, we have strengthened the monitoring of debt service payments, in particular through systematic verification with creditors of the actual execution of such payments, and we will also ensure regular transmission of the monthly debt service reports to the IMF.

28. To preserve debt sustainability, we will continue to contract only concessional loans and to establish an order of priority of projects to be financed under the INDS, paying particular attention to major infrastructure projects under negotiation, even beyond the end of the current ECF arrangement. In that context, under the leadership of the Ministry of Finance, we have improved coordination between the various ministerial departments in the context of the government's financing programs as well as the related policies and actions. We have also extended to public enterprises the requirement to avoid contracting nonconcessional debt.

IV. Monetary and Financial Policies

29. Our monetary policy continues to be underpinned by the currency board arrangement, which is consistent with the structure of our economy by ensuring price stability. We undertake to continue to ensure coverage of all our foreign currency-denominated liabilities and maintaining a rate of coverage higher than 105 percent of reserve money and government deposits with the BCD. Our external position is bolstered by the absence of encumbrances on our foreign-currency reserves, and we are committed to pursuing this prudent policy.

30. The recent strong growth in the banking system has increased risks. Nevertheless, despite the slight increase in 2011 of nonperforming loans, financial soundness indicators remained positive at end-2011. In anticipation of potential vulnerabilities, we remain firmly committed to implementing our reform program in accordance with the broad guidelines of the Financial System Assessment Program (FSAP). In that context, we have strengthened banking supervision, and will closely monitor any changes in the financial soundness indicators. The banking system will also be strengthened through the implementation of laws that have recently been passed or amended, notably the raising of the minimum capital requirement, which will be tripled to DF 1 billion over a maximum period of three years, and the tightening of conditions for the granting of new licenses, on which we have imposed a de facto suspension to avoid overcrowding in the financial system. We also intend to request a new FSAP in the coming months.

31. In addition, we are preparing for the upcoming introduction of reserve requirements, which will be an important new liquidity management tool for the BCD. Similarly, we plan to equip the central bank with a foreign currency cash flow forecasting tool to facilitate the efficient monitoring of the evolution of its foreign exchange reserves.

A. Banking Supervision

32. We conducted on-site inspection of five banks and one microfinance institution in 2011 and plan to inspect five banks, five auxiliary financial institutions, and two microfinance institutions in 2012 (three auxiliary financial institutions have already been inspected). We will also carry out continuous offsite supervision of banks, and are currently in the process of revising the charter of foreign exchange bureaus to bring it into compliance with the new banking law. Further, all banks now submit their internal audit reports as well as their monthly financial statements, thus allowing for the identification of credit, liquidity, and foreign exchange risks. We have also tightened the imposition of penalties on banks that fail to meet the requirement of regular disclosure of their financial statements. These data, provided regularly by banks, will enable us to compile financial stability indicators on a quarterly basis. For improved oversight of portfolio quality, the reporting threshold for nonperforming loans has been lowered.

33. We have developed a roadmap, based on a precise timetable, for implementing the laws approved in 2011. Preparation of the enabling texts of the banking law and supervision instruments has been completed and the new instructions adopted in December 2011 have been issued. In the coming months, we expect to adopt additional new instruments, particularly on liquidity, with technical assistance from the IMF.

B. Financial Sector Development

34. We intend to pursue our efforts to develop the financial sector and access to finance. With the help of our development partners (World Bank, African Development Bank, Islamic Development Bank, and UNDP), we will continue to work to (i) improve access to

microfinance for individuals and small and medium enterprises by setting up a dedicated unit at the CBD; (ii) improve the management of existing structures, such as the central credit register, and lay the groundwork for transitioning to a credit bureau; (iii) facilitate mobile banking transactions; and (iv) strengthen the payment system.

C. Governance of the Central Bank of Djibouti

35. To ensure the integrity of the CBD's operations, we are in the process of implementing the recommendations of the safeguards assessment mission and, in November, we hosted another similar mission in the context of the augmentation of access under the ECF. Starting with the financial report for 2010, the financial reports will be completed within six months of the end of the financial year as will the audit opinion. The full financial statements for 2010, including the audit opinion and the general information notes, have been published on the website of the CBD (*structural benchmark for end-December 2011*). We have strengthened internal control by updating our procedures. In September 2011, pursuant to our commitments, the Board of Directors adopted an official timetable of quarterly meetings and expanded its functions (*structural benchmark for end-June 2011*), including providing for the establishment within the Board of an audit committee responsible for overseeing internal control. An audit charter is under preparation.

D. Combating Money Laundering and Terrorism Financing

36. We are currently addressing the weaknesses in the area of combating money laundering, and terrorism financing through an amendment of the law on combating money laundering and two separate draft laws on the prevention of terrorism and the financing of terrorism, respectively, adopted in 2011. The BCD is currently considering long-term technical assistance in this area, to be financed by donors.

V. Competitiveness and Structural Reforms

37. Because of the currency board arrangement, Djibouti's attractiveness for investment depends essentially on the competitiveness of the economy, which is still hampered by the high costs of the principal factors of production and the weaknesses associated with the business climate. Accordingly, we are strongly committed to pursuing our program of structural reforms, which are aimed especially at reducing energy and water costs, restructuring public enterprises, and improving the legal and regulatory framework. The investment and commercial codes and the law on industrial property, as well as the labor code, are now fully in effect.

38. We are pursuing the reforms in the energy and water sectors. Interconnection with Ethiopia's electricity grid is now completed and, on average, covers more than 50 percent of current consumption in Djibouti at very favorable rates. This has enabled us to reduce electricity rates by 30 percent for low-consumption households, which comprise 60 percent of consumers. In the months ahead, we plan to update the energy master plan with a view to

clarifying our strategy and dealing more vigorously with the technical deficiencies of the EDD, while providing it with the tools to strengthen its management. Further, with support from the World Bank we are preparing to launch in the second half of 2012 a study aimed at assessing the various options for developing geothermal energy. We also implemented the recommendations of the study on the restructuring and reorganization of human resources for the EDD carried out by IDEA Consulting, which in recent years has led to a wage freeze at 2008 levels. Lastly, in the water sector, ONEAD is considering a large seawater desalination investment program to be financed by donors (with support from the EU).

VI. Data

39. The still-low quality of the statistical database continues to hamper our efforts to formulate and monitor economic policies. In January 2012, we joined the General Data Dissemination System and, with the support of our development partners, we are seeking to improve the quality, coverage, and timeliness of economic data, especially in the areas of national accounting, balance of payments, and government finance, using the new legal framework for the organization of statistical activity and the National Statistics System as a basis. With regard to the statistics base, in 2009, we completed the general population census. With support from our development partners, we expect that the survey of economic activities, which will provide data for the estimation of the national accounts, will be completed in 2012. A harmonized consumer price index is being finalized within COMESA and will be applied following the household consumption-budget survey set to begin in the first half of 2012.

VII. Conclusion

40. So as to pave the way for a possible new arrangement following the present ECF, we undertake over the coming months to (i) achieve the indicative targets for the budget balance and net banking system credit to the government, external and domestic arrears for June and December 2012, on the basis of the agreement with Fund staff and the attached Technical Memorandum of Understanding (TMU), (ii) observe the zero ceiling on nonconcessional debt contracted by the government or public enterprises, also pursuant to the TMU, and (iii) complete before the start of a new program, the structural benchmarks relating to the acquisition of a software program for budget nomenclature (*structural benchmark for end-December 2011*), and the preparation of the list of enterprises whose exemptions have been revoked for failing to file their tax returns (*structural benchmark for end-March 2012*).

41. On the basis of the understandings reached with Fund staff in the context of the fifth review, and endorsed by the IMF Executive Board, the program objectives at end-2011 have been met, with the exception of net credit to the government, which deviated from the revised target by 0.2 percent of GDP. However, since it was impossible to modify the performance criteria for end-December 2011, we request waivers for the nonobservance of the criteria at end-December 2011 relating to the budget balance and net banking system

credit to the government, and for the continuous performance criteria on nonaccumulation of domestic arrears, given the overall performance under the program and the policies stated in this Letter. We request the conclusion of the sixth and last review of the ECF with the disbursement of an amount of SDR 1.476 million and the second tranche of the augmentation of access under the ECF, for the amount of SDR 4.77 million.

42. The government believes that the policies and measures stated in this letter are sufficient to achieve the objectives of the ECF arrangement. We shall quickly take all the additional measures necessary for achievement of the program objectives. We shall consult with IMF staff at our own initiative or that of the IMF staff before adopting such measures or changes to the policies specified in the attached MEFP. We shall provide the IMF with any information it may request regarding progress made in implementation, within the framework of its economic and financial development policies and the achievement of the objectives of the program.

Yours sincerely,

/s/	/s/
Ilyas Moussa Dawaleh	Djama M. Haïd
Minister of the Economy and Finance,	Governor
Responsible for Industry and Planning	Central Bank of Djibouti

Table 1. Djibouti: Quantitative Performance Criteria and Indicative Targets, 2011–12 1/

(In millions of Djibouti francs; unless otherwise indicated)

(Cumulative flows)

	2011											2012				
	Jun. 30			Sept. 30		Dec. 31						Mar. 31		Jun. 30	Sep. 30	Dec. 31
	Performance Criteria			Indicative Target		CR/12/169 Performance Criteria			Revised Targets			CR/12/169	Revised Targets	Indicative Targets		
	Prog.	Adj. Prog.	Prel. Act.	Prog.	Prel. Act.	Prog.	Adj. Prog.	Prel. Act.	Prog.	Adj. Prog.	Prel. Act.	Prog.				
Performance Criteria																
I. Ceiling on accumulation of new domestic arrears 2/ 3/	2,260		2,629	2,135	…	2,279		2,290	2,279		2,290	2,279	2,279	2,417	2,417	2,417
II. Ceiling on accumulation of new external arrears 3/ 4/	0		176	0	165	0		0	0		0	0	0	0	0	0
III. Ceiling on net credit to government from the banking system	488	-1,817	-549	-2,015	…	-2,600	-159	2,187	-779	1,717	2,187	9	-1,845	1,761	-3,019	-2,616
IV. Floor on government budget balance (ordonnancement)	-2,628	-99	-378	-1,903	…	883	-692	-1,523	-938	-2,567	-1,523	-85	6	-675	-1,494	1,083
V. Ceiling on new medium- and long-term nonconcessional loans contracted or guaranteed by the government and by the CBD 3/	0		0	0	0	0		0	0		0	0	0	0	0	0
VI. Floor on currency board cover 3/ 5/	105		116	105	150	105		117	105		117	105	105	105	105	105
Indicative targets																
I. Floor on social spending	6,541		5,570	10,024	8,210	14,451		13,474	12,829		13,474	…	…	…	…	15,574
Memorandum items 1/ :																
Adjuster No.1 Projected French, U.S., and Japan military base payments	4,024		6,373	7,154	6,995	12,736		10,554	12,736		10,554	6,350	5,954	6,458	8,490	10,268
Adjuster No.2 External budgetary grants and loans	504		416	2,548	621	3,228		2,709	3,337		2,709	650	868	411	616	3,472
Adjuster No.3 Externally financed public investment loans (PIP)	3,228		3,004	4,466	5,043	6,815		5,948	6,815		5,948	1,935	1,384	2,946	4,945	6,683

Sources: Djibouti authorities; and Fund staff estimates and projections.

1/ See the Technical Memorandum of Understanding for definitions and adjustor calculations.

2/ Represents a rolling stock expressed in terms of one month's wages or and three months' pension fund contributions. Hence it may vary over time.

3/ To be impemented on a continuous basis.

4/ Includes arrears on direct and guaranteed debt, continuous.

5/ Gross foreign assets of the CBD in percent of monetary liabilities (reserve money plus government deposits at CBD).

Table 2. Djibouti: Structural Benchmarks Under the Extended Credit Facility (ECF)

Measures	Date	Motivation	Status
Structural benchmarks			
Budget and revenue management			
1. Strengthening of budget transparency with the monthly publication of the TOFE on the Ministry of Finance website with a maximum lag of two months	Continuous	Fiscal transparency	Met (for the period since 5th review).
2. Adoption by the Cabinet of a customs code consistent with the COMESA zone code	March 2011	Regional trade integration	Not met. The bill was adopted in June 2011
3. Recruitment of qualified staff in the Budget Department for the preparation of the MTBF	June 2011	PFM-Budget Process	Met. One jurist and three economists were recruited in June 2011 and started work in July 2011.
4. Sign cross-debt agreements with EDD, ONEAD, Djibouti Telecom	September 2011	Financial management	Not met. Finalized with EDD and Djibouti Telecom in September, and with ONEAD in November.
5. Acquisition of the software for the introduction of the new budget classification	December 2011	PFM-Budget Process	Not met. The authorities have started consultations with countries in North Africa for the acquisition of the software.
6. Inclusion in the 2012 budget of the lowering of the VAT basis from 80 to 50 million FD	December 2011	Strengthening of tax revenue	Met. The lowering of the VAT basis was included in the 2012 budget.
7. Increase of human resources in the unit in charge of VAT	December 2011	Strengthening of tax revenue	Met. The required staff were recruited in June 2011.
8. Set up the customs revenue management software ASYCUDA for all external trade transactions in Djibouti	December 2011	Strengthening of tax revenue	Met. The software has been installed for all external trade transactions.
9. Prepare a list of enterprises whose tax exempt status has been revoked for failure to file tax returns	March 2012	Strengthening of tax revenue	Not met.
10. Prepare a report estimating fiscal expenditures due to exemptions	June 2012	Strengthening of tax revenue	Removed.
Strengthening of supervision and regulation			
11. Creation of a unit dedicated to supervision, including AML/CFT supervision	June 2011	Strengthening bank supervision and AML/CFT	Met. The unit was created in May 2011 as part of the reorganization of the CBD.
12. Recruitment of two staff for the unit dedicated to supervision	June 2011	Strengthening bank supervision and AML/CFT	Met. The two staff were recruited in May 2011 and three other staff have been redeployed to the unit.
13. Develop a roadmap with a precise timetable for the application of the banking laws	September 2011	Strengthening bank supervision	Met.
Strengthening of the Safeguard framework			
14. Adoption of an official timetable for biannual meetings of the Board of Directors and extension of its rights to oversee internal control	June 2011	Strengthening central bank governance	Not met. The timetable was approved with a delay in September 2011.
15. Publication of the full set of 2010 audited financial statements of the CBD on the CBD website, including the audit opinion and disclosure notes (changed from "Approval of audit reports and publishing the audit opinion on the CBD website six months after the end of the fiscal year")	December 2011	Strengthening central bank governance	Not met. The remaining elements of the set of 2010 audited financial statements have been published in April 2012.

APPENDIX II. TECHNICAL MEMORANDUM OF UNDERSTANDING

I. INTRODUCTION

1. This memorandum defines: (a) the quantitative performance criteria, adjustors, and structural benchmarks for the program supported by the Extended Credit Facility (ECF), which are shown in the Letter of Intent and the related tables; and (b) the scope and frequency of data to be provided for program monitoring purposes.

II. QUANTITATIVE INDICATORS

A. Definitions and Concepts

2. **Test dates**. Quantitative performance criteria are set for June 30, 2011 and December 31, 2011, and must be met at the end of each period, unless otherwise specified.

3. **Government**. For the purposes of the program, "government" is defined as the central government, excluding the social security system.

B. Quantitative Performance Criteria and Indicative Targets

Quantitative Performance Criterion 1: Continuous ceiling on accumulation of new domestic arrears

4. Definition: *New domestic arrears* are defined as payments which are authorized (*ordonnancé*) and are past due date on the wage bill and to private suppliers, public enterprises, and pension funds, incurred as of January 1 of the year and up to the end of the complementary period. The wage bill includes all gross salaries, wages, allowances, benefits, and payments, including housing assistance, that the government agrees to pay to civil servants, to military and security personnel (whether permanent or temporary), and to all other government employees, regardless of the means of payment used (cash, check, or other instrument) or the payment agent (the Treasury or another agency acting on behalf of the government). The ceiling on domestic arrears applies to the total unpaid amount subject to the technical lag (reported in the TOFE as "new arrears"), which must not exceed the sum of one month's wages or three months' pension fund contributions. The ceiling, set for each quarter in Table 1, should be respected on a continuous basis and will be monitored on a monthly basis.

Quantitative Performance Criterion 2: Continuous ceiling on accumulation of new external arrears

5. Definition: *External arrears* are defined as overdue payments (principal and interest) on external debt contracted or guaranteed by the central government or the Central Bank of Djibouti (CBD), excluding debt subject to rescheduling or cancellation. Technical arrears

(as defined in the loan contract) are not considered external arrears for program monitoring purposes. The ceiling should be respected on a continuous basis.

Quantitative Performance Criterion 3: Ceiling on net banking system credit to the government

6. Definition: *Net banking system credit to the government* is defined as the sum of net bank financing, namely, claims on the government minus government deposits with the financial system.

Quantitative Performance Criterion 4: Floor government budget balance on the commitment-basis (*ordonnancement*)

7. Definition: *The government budget balance on a commitment-basis* is defined as the overall balance (on a commitment basis, including grants) shown in the fiscal reporting table (TOFE), representing the difference between total revenue (including grants) and total expenditure, including extra-budgetary expenditure.

Quantitative Performance Criterion 5: Continuous ceiling on contracting or guaranteeing new medium- and long-term nonconcessional external debt by the government, the CBD, and public enterprises

8. Definition: Medium- and long-term nonconcessional external debt contracted or guaranteed by the government, the CBD, and public enterprises, is defined as foreign debt defined by the residency of the creditor, maturing in at least one year, contracted or guaranteed by the government, the CBD, and public enterprises, with a grant component (Net Present Value, NPV, compared with the nominal value) of at least 35 percent, based on the currency- and maturity-specific discount rates announced by the OECD (benchmark commercial interest reference rates - CIRR). The ten-year CIRR is applied to debt maturing in at least 15 years; the six-month CIRR is applied to debt maturing in less than 15 years. For program purposes, the definition of debt is set out in Executive board No. 6230-(79/140), as amended by Decision No. 14416(09/91), including commitments contracted or guaranteed for which value has not been received. The ceiling should be respected on a continuous basis.

Quantitative Performance Criterion 6: Continuous floor on currency board coverage

9. Definition: *Currency board coverage* is defined as the gross foreign assets of the CBD, divided by the sum of government deposits at the CBD and reserve money. The gross foreign assets of the CBD represent the value of the external assets of the CBD, consisting of: (a) monetary gold; (b) SDR holdings; (c) the IMF reserve position; (d) foreign currency holdings; and (e) claims on nonresidents, such as deposits abroad. The foreign assets of the CBD exclude assets that are committed or otherwise encumbered, including but not limited to assets used as collateral or guarantees for foreign liabilities of third parties (assets not immediately available). The floor should be respected on a continuous basis.

Indicative Target 1: Floor on social spending

10. Definition: *Social spending* is defined as subsidies and transfers to public entities, including health organizations, sports clubs, non-profit entities; and transfers to households in the form of scholarships.

III. PROGRAM ADJUSTORS

11. The quantitative performance criteria can be adjusted as follows:

Adjustor 1: French, U.S. and Japanese payments related to the use of military bases

12. Definition: *The ceiling net banking system credit to the government* will be lowered (raised) by the amount of any excess (shortfall) compared with the projected French, U.S. and Japanese payments for 2011, related to the use of military bases (as reported in Table 1 of LOI). *The floor on the government budget balance on a commitment-basis* will be lowered (raised) by the amount of any shortfall (excess) compared with the expected French, U.S. and Japanese payments for 2011, related to the use of military bases (as reported in Table 1 of LOI).

Adjustor 2: Foreign budgetary grants and loans

13. Definition: *The ceiling on net banking system credit to the government* will be lowered (raised) by one-half of any excess (shortfall) in the total amount of the foreign budgetary grants and loans actually disbursed, compared with the program projections (as reported in Table 1 of LOI). *The floor on the government budget balance on a commitment basis* will be lowered (raised) by one-half of any shortfall (excess) in the total amount of the foreign budgetary grants actually disbursed, compared with the program projections (as reported in Table 1 of LOI).

Adjustor 3: Foreign project loans

14. Definition: *The floor on government budget balance on a commitment basis* will be lowered (raised) by any excess (shortfall) in the total amount of the foreign project loans actually disbursed, compared with the pertinent program projections (as reported in Table 1 of LOI).

Domestic arrears

15. Domestic arrears, which were audited by the company Actuaria in 2003, were reconciled again at end-2001, through negotiations with EDD, ONEAD, and Djibouti Telecom. The total of domestic arrears equals to DF 9.898.428.197 and will be reimbursed between 2012 and 2016 according to the scheduling payment below.

in Djibouti Franc	2012	2013	2014	2015	2016
Amount of arrears to repay per year	1,700,000,000	2,200,000,000	2,200,000,000	2,200,000,000	1,598,428,197

IV. REPORTING OBLIGATIONS

16. The authorities will provide the IMF with all data necessary for monitoring economic developments and the results of the program, including but not limited to the specific information below. Any revision of data reported previously will be quickly forwarded to the staff with appropriate explanations.

Real, monetary, and financial sectors:

17. The balance sheet of the central bank, the consolidated balance sheet of the commercial banks, and the monetary survey, within four weeks of the end of the reporting period (the end of each month).

18. The consumer price index, within four weeks of each month-end.

Fiscal sector, including social spending:

19.

- The monthly TOFE data on operations, revenue, expenditure, and budget financing items, including data on capital budget execution, with details on the externally financed portion and the counterpart funds of the central government for which donor terms apply;
- The extra-budgetary expenditure recorded at least quarterly in the TOFE;
- Execution of FSN expenditure, on, at least, a quarterly basis, shown as a separate line in TOFE;
- Repayment of the domestic arrears accumulated in 2009, on at least quarterly basis, shown as a separate line in TOFE;
- Committed expenditure for which payment authorizations (*ordonnancement*) have not been issued (on a quarterly basis).
- Total payments to the public utilities for services executed in the current year, both in DF and as a percentage of the total budgeted for the year, on a quarterly basis.

These data will be provided within 30 days of each month-end.

Arrears:

20. Data on domestic arrears (*ordonnancement* basis) related to: (1) the current year (monthly flows of new accumulations of arrears in all categories); and (2) the stock at the end of the previous year. Consolidated data for (1) and (2) will be reported monthly, within no more than four weeks.

21. External arrears data related to: (1) the current year, and (2) the stock at the end of the pr*evious year; c*onsolidated data for (1) and (2) will be reported monthly, within no more than four weeks.

External sector, external assistance and debt:

22. The quarterly balance of payments statistics, end of each quarter with a two quarter lag.

23. The monthly data on foreign grants and loans received by the government and by public enterprises, by creditor and by disbursement currency, within four weeks of each month-end.

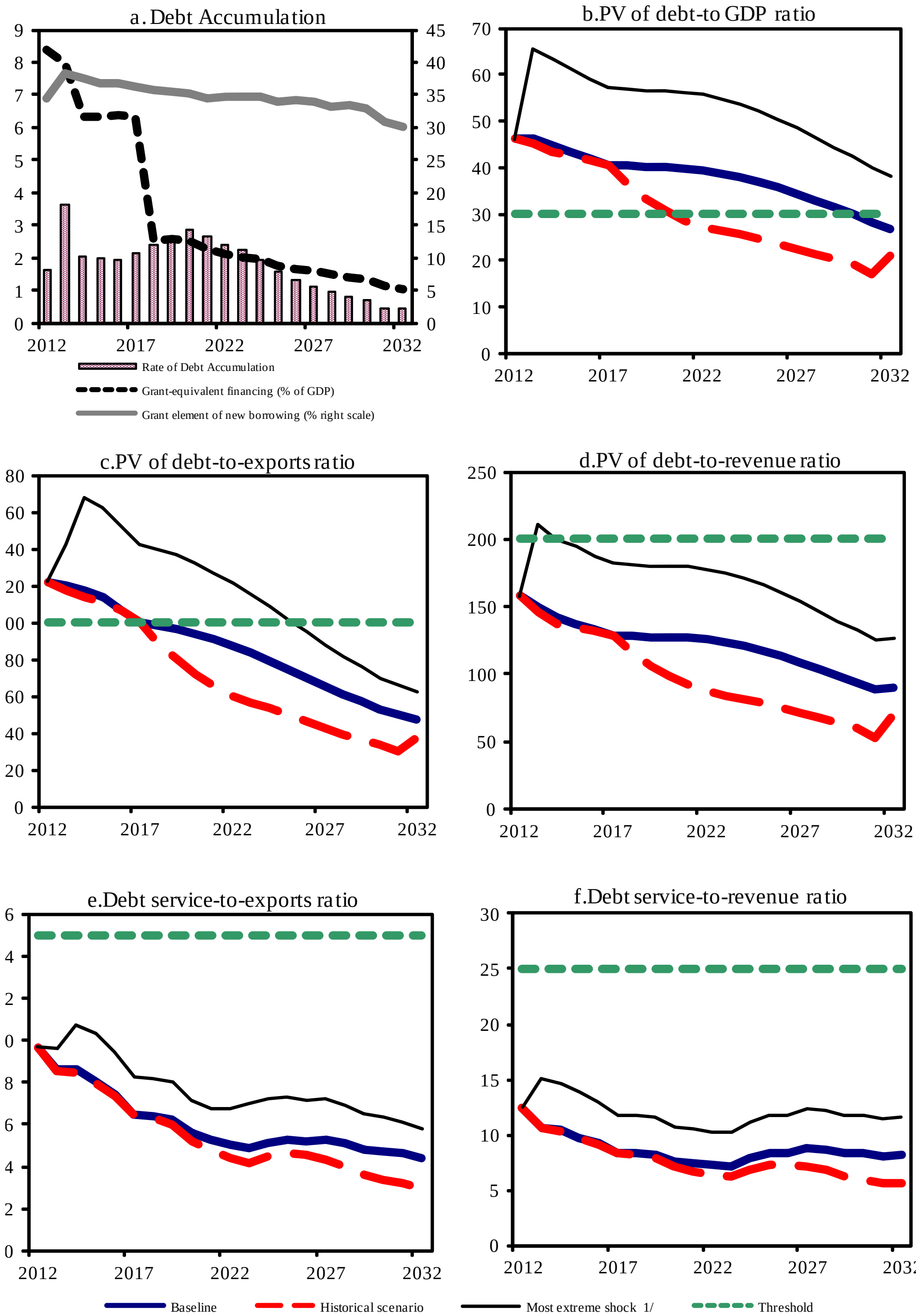
24. The monthly data on the evolution of external debt, including arrears and rescheduling operations, within six weeks of each month-end.

25. The monthly list of medium- and long-term external loans contracted and guaranteed by the government for each month, with the following details on each loan: the creditor, the borrower, the amount, the currency, the maturity, the grace period, and the interest rate arrangements. These data will be reported within four weeks of each month-end.

26. The quarterly data on the balance of the external debt stock, by creditor, debtor, and currency, within six weeks of the end of each quarter.

APPENDIX III. DEBT SUSTAINABILITY ANALYSIS CHARTS AND TABLES

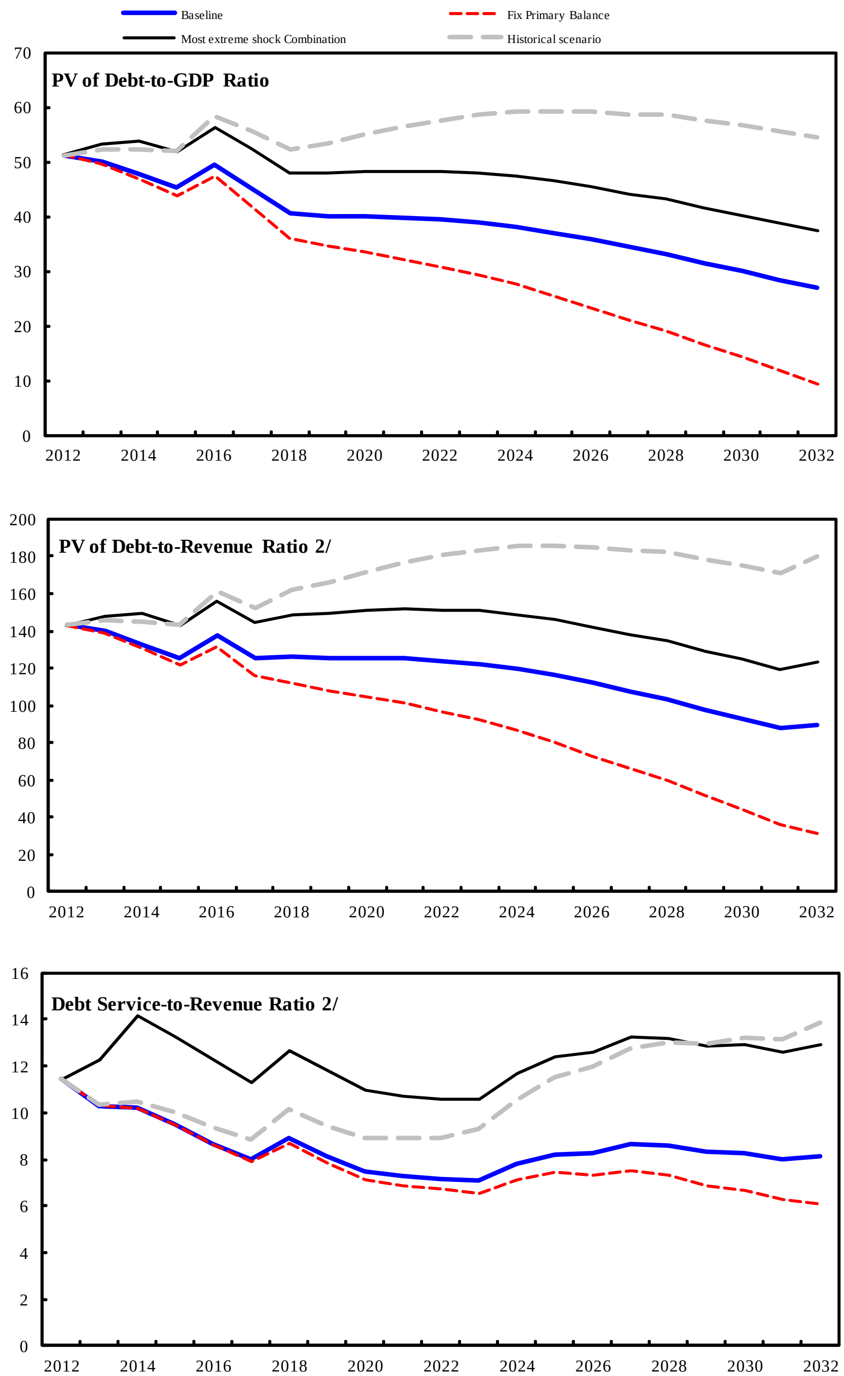
Figure 1. Djibouti: Indicators of Public and Publicly Guaranteed External Debt
Under Alternatives Scenarios, 2012-32 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2022. 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. Djibouti: Indicators of Public Debt under Alternative Scenarios, 2012-32 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2022.

2/ Revenues are defined inclusive of grants.

Table 1a.Djibouti: Public Sector Debt Sustainability Framework, Baseline Scenario, 2009-2032
(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2009	2010	2011	Average 5/	Standard Deviation 5/	2012	2013	2014	2015	2016	2017	2012-17 Average	2022	2032	2018-32 Average
Public sector debt 1/	74.2	68.6	51.8			48.1	51.4	51.8	52.0	59.3	53.8		50.9	37.2	
o/w foreign-currency denominated	59.8	56.1	52.3			51.3	53.5	53.0	52.3	51.6	49.2		50.7	37.2	
Change in public sector debt	-2.3	-5.6	-16.8			-3.7	3.3	0.4	0.2	7.3	-5.5		-0.1	-2.0	
Identified debt-creating flows	-0.3	-4.7	-5.4			-4.8	-4.2	-4.4	-4.6	-4.5	-4.6		-3.4	-2.6	
Primary deficit	3.3	-0.6	-0.5	0.6	1.8	-2.9	-2.1	-2.4	-2.0	-1.6	-0.9	-2.0	-1.0	-0.5	-0.8
Revenue and grants	37.0	35.5	34.5			35.8	35.9	36.0	36.0	36.0	36.1		31.8	30.2	
of which: grants	6.4	5.3	6.0			6.6	4.9	4.3	4.4	4.5	4.6		0.5	0.3	
Primary (noninterest) expenditure	40.3	34.9	34.0			32.9	33.7	33.6	34.0	34.4	35.2		30.8	29.8	
Automatic debt dynamics	-3.6	-4.1	-5.0			-1.9	-2.1	-2.0	-2.6	-2.9	-3.7		-2.4	-2.2	
Contribution from interest rate/growth differential	-7.1	-3.7	-3.7			-0.6	-1.8	-1.8	-2.4	-2.6	-3.4		-2.7	-2.4	
of which: contribution from average real interest rate	-3.4	-1.2	-0.7			1.7	0.4	0.7	0.3	0.2	-0.1		0.1	-0.2	
of which: contribution from real GDP growth	-3.7	-2.5	-2.9			-2.4	-2.3	-2.5	-2.7	-2.9	-3.3		-2.8	-2.2	
Contribution from real exchange rate depreciation	3.4	-0.4	-1.3			-1.3	-0.3	-0.3	-0.3	-0.3	-0.3		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	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)	0.0	0.0	0.0			0.0	0.0	0.0	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	-2.0	-0.9	-11.4			1.1	7.5	4.8	4.8	11.8	-0.9		3.3	0.7	
Other Sustainability Indicators															
PV of public sector debt	...	...	48.2			42.9	44.2	43.6	43.1	49.9	44.8		39.1	26.9	
o/w foreign-currency denominated	...	...	48.7			46.0	46.3	44.8	43.5	42.2	40.2		39.0	26.8	
o/w external	...	...	48.7			46.0	46.3	44.8	43.5	42.2	40.2		39.0	26.8	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	6.0	2.2	2.6			1.2	1.6	1.3	1.5	1.5	2.0		1.3	2.0	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	139.6			119.7	123.2	121.3	119.8	138.5	124.0		123.0	88.8	
PV of public sector debt-to-revenue ratio (in percent)	...	...	169.2			146.8	142.6	137.6	136.6	158.4	142.1		125.0	89.6	
o/w external 3/	...	...	171.2			157.7	149.4	141.2	137.7	134.2	127.5		124.7	89.4	
Debt service-to-revenue and grants ratio (in percent) 4/	7.3	7.8	9.0			11.4	10.3	10.2	9.5	8.7	8.0		7.2	8.0	
Debt service-to-revenue ratio (in percent) 4/	8.8	9.2	10.9			14.0	11.9	11.6	10.8	9.9	9.2		7.3	8.1	
Primary deficit that stabilizes the debt-to-GDP ratio	5.6	5.1	16.3			0.8	-5.4	-2.8	-2.1	-8.9	4.5		-0.9	1.5	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	5.0	3.5	4.5	4.1	1.1	4.8	5.0	5.0	5.5	5.8	5.8	5.3	5.8	5.8	5.8
Average nominal interest rate on forex debt (in percent)	1.4	1.3	1.4	1.4	0.1	4.2	1.9	2.4	1.8	1.9	1.4	2.3	2.1	1.2	1.8
Average real interest rate on domestic debt (in percent)	1.1	-1.1	-1.2	-1.7	2.3	-91.1	-15.3	-21.2	-33.0	-72.2	1.5	-38.5	10.6	16.8	11.4
Real exchange rate depreciation (in percent, + indicates depreciation)	6.4	-0.8	-2.4	-1.3	3.5	-2.5	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.7	4.0	5.1	3.7	2.5	4.3	2.5	2.5	2.5	2.5	2.5	2.8	1.3	1.3	1.3
Growth of real primary spending (deflated by GDP deflator, in percent)	0.1	-0.1	0.0	0.1	0.1	0.0	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.0	0.0
Grant element of new external borrowing (in percent)	...	...	...	...	...	34.6	38.2	37.8	36.5	36.0	34.8	36.3	34.8	30.0	...

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

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 generally derived over the past 10 years, subject to data availability.

Table 2a.Djibouti: Sensitivity Analysis for Key Indicators of Public Debt 2012-2032

	Projections							
	2012	2013	2014	2015	2016	2017	2022	2032
PV of Debt-to-GDP Ratio								
Baseline	51	50	48	45	49	45	39	27
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	51	52	52	52	58	56	58	55
A2. Primary balance is unchanged from 2012	51	50	47	44	47	42	31	9
A3. Permanently lower GDP growth 1/	51	50	48	46	50	46	43	36
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2013-2014	51	52	51	49	54	50	48	39
B2. Primary balance is at historical average minus one standard deviations in 2013-2014	51	53	54	51	55	50	44	29
B3. Combination of B1-B2 using one half standard deviation shocks	51	53	54	52	56	52	48	37
B4. One-time 30 percent real depreciation in 2013	51	68	64	59	62	56	46	29
B5. 10 percent of GDP increase in other debt-creating flows in 2013	51	57	54	51	55	51	44	30
PV of Debt-to-Revenue Ratio 2/								
Baseline	143	140	133	126	137	125	124	89
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	143	146	145	144	161	152	180	180
A2. Primary balance is unchanged from 2012	143	138	130	122	131	116	97	31
A3. Permanently lower GDP growth 1/	143	140	134	127	140	128	134	120
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2013-2014	143	143	141	136	149	139	149	129
B2. Primary balance is at historical average minus one standard deviations in 2013-2014	143	148	149	141	152	139	137	97
B3. Combination of B1-B2 using one half standard deviation shocks	143	148	149	143	156	144	151	124
B4. One-time 30 percent real depreciation in 2013	143	189	177	165	172	156	144	96
B5. 10 percent of GDP increase in other debt-creating flows in 2013	143	158	150	142	153	140	138	98
Debt Service-to-Revenue Ratio 2/								
Baseline	11	10	10	10	9	8	7	8
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	11	10	10	10	9	9	9	14
A2. Primary balance is unchanged from 2012	11	10	10	9	9	8	7	6
A3. Permanently lower GDP growth 1/	11	10	10	10	9	8	7	9
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2013-2014	11	10	11	10	9	8	8	10
B2. Primary balance is at historical average minus one standard deviations in 2013-2014	11	10	10	10	9	8	7	9
B3. Combination of B1-B2 using one half standard deviation shocks	11	10	11	10	9	8	8	10
B4. One-time 30 percent real depreciation in 2013	11	12	14	13	12	11	11	13
B5. 10 percent of GDP increase in other debt-creating flows in 2013	11	10	11	10	9	8	7	9

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.

Table 3a.: External Debt Sustainability Framework, Baseline Scenario, 2009-2032 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical 6/ Average	Standard 6/ Deviation	Projections									
	2009	2010	2011			2012	2013	2014	2015	2016	2017	2012-2017 Average	2022	2032	2018-2032 Average
External debt (nominal) 1/	**59.8**	**56.2**	**52.3**			**51.3**	**53.5**	**53.0**	**52.3**	**51.6**	**49.2**		**50.7**	**37.2**	
o/w public and publicly guaranteed (PPG)	59.8	56.1	52.3			51.3	53.5	53.0	52.3	51.6	49.2		50.7	37.2	
Change in external debt	-0.4	-3.6	-3.8			-1.1	2.2	-0.6	-0.6	-0.7	-2.5		-0.1	-2.0	
Identified net debt-creating flows	-4.3	-0.7	1.3			1.7	-2.9	-3.7	-5.4	-5.6	-6.4		-2.5	-12.2	
Non-interest current account deficit	**8.3**	**5.1**	**11.8**	**7.6**	**9.4**	**10.1**	**11.0**	**9.7**	**8.8**	**8.9**	**7.3**		**5.5**	**-5.5**	4.5
Deficit in balance of goods and services	17.1	13.3	18.2			17.8	17.0	14.2	10.8	10.1	8.3		7.0	-3.7	
Exports	38.1	31.8	38.0			37.7	38.5	38.3	38.3	39.2	40.4		45.2	56.3	
Imports	55.1	45.1	56.3			55.6	55.4	52.6	49.0	49.3	48.7		52.1	52.6	
Net current transfers (negative = inflow)	-0.3	0.0	-1.3	-1.6	1.8	-1.8	-1.7	-0.7	-0.6	-0.5	-0.5		-0.3	-0.1	-0.3
o/w official	-1.0	-0.8	-2.0			-2.5	-2.4	-1.3	-1.2	-1.1	-1.1		-0.9	-0.5	
Other current account flows (negative = net inflow)	-8.5	-8.1	-5.1			-6.0	-4.2	-3.9	-1.4	-0.7	-0.4		-1.2	-1.7	
Net FDI (negative = inflow)	**-9.5**	**-2.4**	**-6.3**	**-10.3**	**9.0**	**-8.1**	**-12.4**	**-12.1**	**-12.4**	**-12.5**	**-11.6**		**-6.2**	**-5.0**	-6.2
Endogenous debt dynamics 2/	**-3.0**	**-3.5**	**-4.3**			**-0.3**	**-1.5**	**-1.3**	**-1.8**	**-1.9**	**-2.1**		**-1.8**	**-1.7**	
Contribution from nominal interest rate	0.8	0.7	0.7			2.0	0.9	1.2	0.9	0.9	0.7		1.0	0.4	
Contribution from real GDP growth	-2.8	-1.9	-2.3			-2.3	-2.4	-2.5	-2.7	-2.8	-2.8		-2.8	-2.1	
Contribution from price and exchange rate changes	-1.0	-2.3	-2.7			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**3.9**	**-2.9**	**-5.1**			**-2.7**	**5.1**	**3.2**	**4.8**	**4.9**	**3.9**		**2.5**	**10.2**	
o/w exceptional financing	-1.8	-0.7	-1.1			-0.7	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	48.7			46.0	46.3	44.8	43.5	42.2	40.2		39.0	26.8	
In percent of exports	...	...	128.2			121.9	120.4	116.8	113.6	107.9	99.4		86.4	47.6	
PV of PPG external debt	**...**	**...**	**48.7**			**46.0**	**46.3**	**44.8**	**43.5**	**42.2**	**40.2**		**39.0**	**26.8**	
In percent of exports	**...**	**...**	**128.1**			**121.9**	**120.4**	**116.8**	**113.6**	**107.9**	**99.4**		**86.4**	**47.6**	
In percent of government revenues	**...**	**...**	**171.2**			**157.7**	**149.4**	**141.2**	**137.7**	**134.2**	**127.5**		**124.7**	**89.4**	
Debt service-to-exports ratio (in percent)	**5.9**	**7.6**	**7.0**			**9.6**	**8.6**	**8.6**	**8.1**	**7.4**	**6.4**		**5.0**	**4.3**	
PPG debt service-to-exports ratio (in percent)	**5.9**	**7.6**	**7.0**			**9.6**	**8.6**	**8.6**	**8.1**	**7.4**	**6.4**		**5.0**	**4.3**	
PPG debt service-to-revenue ratio (in percent)	**7.4**	**8.0**	**9.4**			**12.5**	**10.6**	**10.4**	**9.8**	**9.2**	**8.3**		**7.3**	**8.0**	
Total gross financing need (Millions of U.S. dollars)	10.7	58.4	101.8			75.6	28.1	13.0	-9.1	-13.9	-33.0		42.8	-454.1	
Non-interest current account deficit that stabilizes debt ratio	8.7	8.8	15.7			11.1	8.8	10.2	9.4	9.5	9.8		5.6	-3.5	
Key macroeconomic assumptions															
Real GDP growth (in percent)	5.0	3.5	4.5	4.1	1.1	4.8	5.0	5.0	5.5	5.8	5.8	5.3	5.8	5.8	5.8
GDP deflator in US dollar terms (change in percent)	1.7	4.0	5.1	3.7	2.5	4.3	2.5	2.5	2.5	2.5	2.5	2.8	1.3	1.3	1.3
Effective interest rate (percent) 5/	1.4	1.3	1.4	1.4	0.1	4.2	1.9	2.4	1.8	1.9	1.4	2.3	2.1	1.2	1.8
Growth of exports of G&S (US dollar terms, in percent)	8.2	-10.1	31.2	8.7	11.0	8.5	9.6	7.2	7.9	11.0	12.0	9.4	10.4	7.0	9.6
Growth of imports of G&S (US dollar terms, in percent)	-17.8	-11.9	36.9	11.7	17.2	7.9	7.2	2.1	0.9	9.0	7.2	5.7	6.8	6.9	7.7
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	34.6	38.2	37.8	36.5	36.0	34.8	36.3	34.8	30.0	33.9
Government revenues (excluding grants, in percent of GDP)	30.6	30.1	28.5			29.2	31.0	31.7	31.6	31.5	31.5		31.3	30.0	31.4
Aid flows (in Millions of US dollars) 7/	116.4	77.5	108.4			115.6	134.1	110.3	115.6	125.4	121.8		69.6	69.3	
o/w Grants	67.2	60.2	74.9			89.6	70.9	66.7	75.1	83.4	91.8		14.6	14.6	
o/w Concessional loans	49.2	17.3	33.4			26.0	63.2	43.6	40.5	42.0	30.0		55.0	54.7	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			8.3	8.0	6.3	6.4	6.5	5.9		2.1	1.0	1.8
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			71.8	61.2	65.5	64.8	65.2	71.3		41.4	36.4	40.2
Memorandum items:															
Nominal GDP (Millions of US dollars)	1049.1	1128.6	1239.1			1353.6	1455.8	1566.4	1693.6	1836.1	1990.9		2805.0	5620.8	
Nominal dollar GDP growth	6.8	7.6	9.8			9.2	7.5	7.6	8.1	8.4	8.4	8.2	7.2	7.2	7.2
PV of PPG external debt (in Millions of US dollars)			603.6			623.1	674.1	701.1	736.2	775.7	799.8		1094.4	1506.5	
(PVt-PVt-1)/GDPt-1 (in percent)						1.6	3.8	1.9	2.2	2.3	1.3	2.2	2.4	0.5	1.6
Gross workers' remittances (Millions of US dollars)	-6.0	-6.6	-6.9			-7.1	-7.4	-7.7	-8.0	-8.4	-8.7		-10.6	0.0	
PV of PPG external debt (in percent of GDP + remittances)	...	...	49.0			46.3	46.5	45.0	43.7	42.4	40.3		39.2	26.8	
PV of PPG external debt (in percent of exports + remittances)	...	...	130.0			123.7	122.0	118.3	115.0	109.2	100.4		87.1	47.6	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	7.1			9.8	8.7	8.7	8.2	7.5	6.5		5.1	4.3	

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 exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
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 generally derived over the past 10 years, subject to data availability.
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 3b.Djibouti: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2012-2032
(In percent)

	Projections							
	2012	2013	2014	2015	2016	2017	**2022**	2032
PV of debt-to GDP ratio								
Baseline	46	46	45	43	42	41	**39**	27
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	46	45	43	43	42	41	**27**	21
A2. New public sector loans on less favorable terms in 2012-2032 2	46	48	48	48	48	47	**51**	43
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	46	47	47	45	43	42	**41**	28
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	46	49	52	50	49	47	**45**	29
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	46	47	46	44	43	41	**40**	28
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	46	55	61	59	56	54	**51**	30
B5. Combination of B1-B4 using one-half standard deviation shocks	46	53	59	57	55	53	**50**	31
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	46	65	63	61	59	57	**56**	38
PV of debt-to-exports ratio								
Baseline	122	120	117	113	107	100	**87**	48
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	122	117	113	111	106	100	**60**	37
A2. New public sector loans on less favorable terms in 2012-2032 2	122	126	126	126	121	117	**113**	77
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	122	120	117	113	107	100	**87**	48
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	122	143	168	162	152	143	**121**	62
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	122	120	117	113	107	100	**87**	48
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	122	142	159	153	144	134	**112**	54
B5. Combination of B1-B4 using one-half standard deviation shocks	122	146	166	160	151	141	**118**	58
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	122	120	117	113	107	100	**87**	48
PV of debt-to-revenue ratio								
Baseline	158	149	142	137	133	129	**126**	90
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	158	146	137	135	132	129	**87**	70
A2. New public sector loans on less favorable terms in 2012-2032 2	158	156	153	152	151	150	**163**	144
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	158	152	147	143	138	134	**131**	93
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	158	158	165	160	154	149	**142**	95
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	158	151	145	141	136	132	**129**	92
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	158	177	192	186	179	173	**162**	102
B5. Combination of B1-B4 using one-half standard deviation shocks	158	173	187	181	175	169	**159**	102
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	158	211	200	194	188	182	**178**	127

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(In percent)

	2012	2013	2014	2015	2016	2017	**2022**	2032
Debt service-to-exports ratio								
Baseline	10	9	9	8	7	6	**5**	4
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	10	9	8	8	7	6	**4**	3
A2. New public sector loans on less favorable terms in 2012-2032 2	10	9	9	8	8	7	**7**	6
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	10	9	9	8	7	6	**5**	4
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	10	10	11	10	9	8	**7**	6
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	10	9	9	8	7	6	**5**	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	10	9	9	9	8	7	**6**	5
B5. Combination of B1-B4 using one-half standard deviation shocks	10	9	10	10	9	8	**7**	6
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	10	9	9	8	7	6	**5**	4
Debt service-to-revenue ratio								
Baseline	12	11	10	10	9	8	**7**	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2012-2032 1/	12	11	10	10	9	8	**6**	6
A2. New public sector loans on less favorable terms in 2012-2032 2	12	11	11	10	10	9	**10**	11
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2013-2014	12	11	11	10	10	9	**8**	9
B2. Export value growth at historical average minus one standard deviation in 2013-2014 3/	12	11	11	10	10	9	**8**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2013-2014	12	11	11	10	9	8	**7**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2013-2014 4/	12	11	11	11	10	9	**9**	10
B5. Combination of B1-B4 using one-half standard deviation shocks	12	11	11	11	10	9	**9**	10
B6. One-time 30 percent nominal depreciation relative to the baseline in 2013 5/	12	15	15	14	13	12	**10**	12
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	34	34	34	34	34	34	**34**	34

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.

INTERNATIONAL MONETARY FUND

DJIBOUTI

Sixth Review Under the Extended Credit Facility Arrangement and Request for Waivers of Nonobservance of Performance Criteria

Informational Annex

Prepared by the Middle East and Central Asia Department
(In consultation with other departments)

May 9, 2012

- **Relations with the Fund.** Describes financial and technical assistance from the Fund and provides information on the safeguards assessment and the exchange rate system. Outstanding purchases amounted to SDR 16.92 million (106.43 percent of quota) as of March 31, 2012.

- **Joint managerial Action Plan—June 2011–May 2012.** Describes the Fund and World Bank Group's joint work programs.

- **Statistical Issues.** Assesses the quality of statistical data. Data provided to the Fund are broadly adequate for surveillance and program monitoring purposes but significant deficiencies remain.

- **Table of Common Indicators Required for Surveillance.** Provides information on statistical data for surveillance purposes.

Contents Page

ANNEX I. DJIBOUTI: RELATIONS WITH THE FUND
(As of March 31, 2012)

I. Membership Status: Joined: December 29, 1978; Article VIII

II. General Resources Account:	**SDR Million**	**%Quota**
Quota	15.90	100.00
Fund holdings of currency	14.80	93.08
Reserve Tranche Position	1.10	6.92
Lending to the Fund		
Notes Issuance		
Holdings Exchange Rate		

III. SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	15.16	100.00
Holdings	9.21	60.76

IV. Outstanding Purchases and Loans:	**SDR Million**	**%Quota**
ECF Arrangements	16.92	106.43

V. Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF [1/]	Sep 17, 2008	Jun 16, 2012	22.26	16.01
ECF [1/]	Oct 18, 1999	Jan 17, 2003	19.08	13.63
Stand-By	Apr 15, 1996	Mar 31, 1999	8.25	7.27

1/ Formerly PRGF

VI. Projected Payments to Fund[2/]

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2012	2013	2014	2015	2016
Principal	0.91		0.92	1.07	1.36
Charges/Interest	0.01	0.01	0.05	0.05	0.04
Total	**0.92**	**0.01**	**0.97**	**1.11**	**1.41**

2/When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

VII. Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI): Not Applicable

IX. Implementation of HIPC Initiative: Not Applicable

X. Safeguards assessments

A safeguards assessment mission of the Banque Centrale de Djibouti which was completed in 2009 in the context of the ECF arrangement found that serious risks are present in most areas. These risks are partly mitigated by the currency board arrangement and the relatively straightforward nature of the BCD's operations. Priority measures recommended by the assessment focus on formalizing Board oversight, enhancing the external and internal audit mechanisms, and improving financial reporting transparency through publication and a sequenced transition to International Financial Reporting Standards. Implementation of most of these recommendations has been delayed. However, recently the BCD authorities have started to implement some of these reforms. An update safeguards assessment was triggered in 2011 when Djibouti requested an augmentation of access by 60 percent of quota under the ECF to meet additional financing needs in 2011–12 caused by drought and international price shocks. The update found that limited progress was made in implementing key safeguards measures since the last assessment. Fundamental governance and oversight gaps persist, including the absence of an internal audit function. Statutory compliance is not monitored, and transparency of financial reporting remains limited. The external audit broadly adheres to international standards; however, the timing of its completion could be improved.

XI. Exchange arrangements

Djibouti has a currency board arrangement. The Djibouti franc is pegged to the U.S. dollar at the rate of DF 177.721 = US$1. Djibouti maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

XII. Article IV Consultation

The staff report for the 2010 Article IV consultation was discussed by the Executive Board on January 7, 2011.

XIII. FSAP Participation

The FSAP, including the assessment of the AML-CFT framework, was approved by the Board in June 2009. Key findings were (i) the banking sector does not appear to pose an immediate systemic threat, but it is vulnerable to a deterioration of credit quality and interest rate movements; (ii) the CBD's regulatory and supervisory framework is rudimentary and not well-suited to handle the entry of new banks; (iii) the CBD should introduce a reserve requirement and bolster its capacity to provide emergency liquidity support, (iv) the CBD should, in cooperation with the banking community, develop a comprehensive modernization strategy of the national payments system that responds to the needs of the growing economy; (v) the assessment of AML/CFT noted a combination of weak capacity to address ML/FT and multiple vulnerability factors. The CBD has started to implement some of these recommendations. It has adopted measures to strengthen banking supervision and regulation, including onsite and offsite bank inspections. Furthermore, the CBD has reinforced prudential measures by increasing the minimum capital requirements and reducing the single-borrower limit.

XIV. Technical Assistance

FAD—Budget control and cash management of the treasury	April 2000
FAD—Direct tax reform	September 2000
FAD/MCD—Budget control and cash management of the treasury	February 2001
FAD—Tax administration and possible introduction of a VAT	April 2002
STA—Government finance statistics	May 2001
STA—National accounts and balance of payments statistics	January 2002
STA—Balance of payment statistics	November 2003
MFD—Banking supervision	December 2002
MFD—Banking supervision	December 2003
STA—Money and banking statistics	November/December 2004
FAD—Tax and customs administration	January/February 2005
MFD—Central banking accounting	October 2005
FAD—Tax administration	January 2007
FAD—Tax policy	January 2007
LEG—AML/CFT	June 2007
STA—Balance of payments statistics	June 2007
FAD—Tax policy	June 2007
FAD—Tax administration	July 2007
MCM—Central Bank Accounting	November 2007
STA—Monetary and Financial Statistics	December 2007
FAD—Public Fiscal Management	February 2008
MCM—Central Bank Accounting	February 2008
STA—Monetary and Financial Statistics	January 2009
FAD—Public Financial Management	May 2009
MCM—Central Bank Supervision	April, September 2010
MCM—Liquidity Management	May 2010
FAD—Medium Term Fiscal Framework	January 2011
FAD—VAT Assessment and Tax Policy	February-March 2011
MCM—Banking Supervision	April-July 2011
STA—Balance of payments statistics	December 2011
FAD—Public Financial Management	January 2012
FAD—Subsidies Reform	March 2012
MCM—Banking Supervision	March-May 2012

XV. Resident Representative

The IMF had a resident representative in Djibouti from 1998. The last resident representative left the post in April 2007. A new resident representative, Mr. Samba Thiam, took up the post in November 2010.

Annex II. DJIBOUTI: JOINT MANAGERIAL ACTION PLAN
JUNE 2011 – MAY 2012

Title	Products	Provisional Timing of Missions	Expected Delivery Date
1. Bank Work Program	Country Partnership Strategy (2013-2016)-Discussion	March 2012	FY13
	Growth Model Study	September 2011, January 2012 June 2012	May 2012
	Workshop on Judicial reforms and Anti Corruption with the EU	June 2012	June 2012
	Monitoring and Evaluation System for the INDS	December 2010 January 2012	February 2012
	Drought Post Disaster Needs Assessment *First mission* *Risk Reduction Donors' Round-Table)*	 *October 2012* *April 2012*	 May2012
	Vision 2035 (TA)	May 2012 June 2012 September 2012,	November 2012
	Construction of a new CPI (TA)	May 2012 October 2012	
	TA Study on Regulation of Private Port Operators	April 2012	
	Assessment of Transport and Trade Facilitation	Jan 2012	
2. Fund Work Program	TA on Fuel Subsidies TA on GDSS TA on BOP Statistics TA on Banking Supervision TA on Public Financial Management TA on DSA TA on Reserves Management 5th Review of the ECF 6th Review of the ECF Strengthening national account statistics	January 2012 December 2011 November 2011 January 2012 January 2012 January 2012 March 2012 October 2011 March 2012	February 2012 January 2012 December 2011 February 2012 February 2012 February 2012 April 2012 February 2012 May 2012
3. Joint Bank/Fund Program	Participation in Post-Disaster Needs Assessment Joint work on INDS Participation in the Donor Conference	October 2011	November 2011 June 2012 June 2012

ANNEX III. DJIBOUTI: STATISTICAL ISSUES

General: *Data provided to the Fund are broadly adequate for surveillance*. There are, however, serious shortcomings in the areas of national accounts, the balance of payments (BOP), external debt, and recently in fiscal data. Djibouti began participating in the General Data Dissemination System (GDDS) in February 2012.

National accounts: Despite the creation of the National Statistical Office (DISED) in 2002 and several TA missions to enhance the capacity of the statistical system and the efficient use of available resources, the authorities do not compile national accounts data, mostly due to low implementation capacity. Djibouti urgently needs assistance in this area as this significantly hampers surveillance. A population census, completed in 2009, followed by poverty and household consumption surveys in the first half of 2012, should help to revise the CPI basket weights and to update various social indicators, and, in particular, to provide new poverty and income distribution estimates.

External sector: Substantial progress has been made in improving balance of payments statistics in line with recommendations made by Fund's TA missions over the past few years. However, significant issues remain, which were highlighted by a June 2007 BOP mission. Problems were identified in compiling trade statistics, coverage of direct investment transactions in the BOP, and estimating workers' remittances. Improvements could also be made to several items such as freight transportation, investment income, transactions related to foreign military bases, and other investment of private sector (use of IBS data). Despite the introduction of a new system for the management of external debt in 2002, debt statistics continue to be provided irregularly and with a delay. A technical assistance mission on external sector BOP has visited Djibouti in November 2011 to assist the authorities in improving the compilation of BOP and IIP statistics and in preparing an effective transition from *BPM5* to *BPM6*.

Government finance: Fiscal data are available on a monthly basis although with a substantial delay (2 month lag). Moreover, these data do not cover a number of extra-budgetary accounts, including three pension funds. Foreign-financed capital expenditure is reported regularly. Moreover, additional efforts are needed to improve the compilation and coverage of fiscal data, particularly at the institutional level, in order to fulfill the recommendations made by a government finance statistics mission in 2001. The MOF is reporting neither annual data for dissemination in the *GFS* Yearbook nor high-frequency data for publication in the *International Finance Statistics* (*IFS*). To improve data collection and reporting, a macroeconomic unit has been set up in the MOF.

Monetary accounts: Monetary statistics are generally adequate and cover the central bank and the aggregated balance sheet of all commercial banks. Djibouti received three monetary and financial statistics missions (2004-2009) on compiling monetary and financial statistics in accordance with the Fund's *Monetary and Financial Statistics Manual (MFSM).* Over this period, the CBD has implemented some of the recommendations, in particular those concerning the establishment of a sectorization of the economic entities of Djibouti. However, majority of the recommendations have not been implemented, mainly because of staffing constraints at the CBD.

Annex IV. Djibouti: Table of Common Indicators Required for Surveillance
As of January, 2012

	Date of Latest Observation	Date Received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	Na	na	na	na	na
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	January 2012	March 2012	M	M	NA
Reserve/Base Money	January 2012	March 2012	M	M	M
Broad Money	January 2012	March 2012	M	M	M
Central Bank Balance Sheet	January 2012	March 2012	M	M	A
Consolidated Balance Sheet of the Banking System	January 2012	March 2012	M	M	A
Interest Rates[2]	December 2011	April 2012	M	M	A
Consumer Price Index	December 2011	February 2012	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	January 2012	March 2012	M	M	NA
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	January 2012	March 2012	M	M	NA
Stocks of Central Government and Central Government-Guaranteed Debt[5]	December 2011	February 2012	A	A	NA
External Current Account Balance	September 2011	March 2012	A	A	A
Exports and Imports of Goods and Services	December 2011	March 2012	Q	Q	A
GDP/GNP	December 2011 [8]	February 2012	A	A	A
Gross External Debt	December 2011	February 2012	A	A	I
International Investment Position[6]	December 2010	March 2011	A	A	A

[1]Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (excluding extra budgetary funds and social security funds, and state and local governments).
[5] Including currency and maturity composition. .
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D); Weekly (W); Monthly (M); Bi-monthly (B); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).
[8] GDP data estimated by staff on the basis of partial data provided by the authorities.

Press Release No.12/190
FOR IMMEDIATE RELEASE
May 24, 2012

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Sixth and Final Review Under the Extended Credit Facility Arrangement for Djibouti and Approves US$9.5 million Disbursement

The Executive Board of the International Monetary Fund (IMF) has completed the sixth and last review of Djibouti's performance under the economic program supported by the Extended Credit Facility[3] arrangement (ECF). Completion of the review enables the immediate disbursement of SDR 6.246 million (about US$9.5 million), bringing total disbursements under the arrangement to SDR 22.26 million (US$33.9 million).

In completing the review the Executive Board approved the authorities' request for waivers of nonobservance of the end-December 2011 performance criteria on the fiscal balance and on the net banking system credit to the government. Furthermore, the Board also approved a waiver of nonobservance of the continuous performance criterion on the accumulation of new domestic arrears (related to delays in social security payments). These waivers were granted on the grounds of temporary or minor deviations from the program objectives and the corrective measures undertaken by the authorities.

The ECF arrangement for Djibouti was approved on September 17, 2008 (see Press Release No. 8/211) for an amount equivalent to SDR 12.72 million (about US$19.4 million, or 80 percent of the country's quota in the Fund). On January 7, 2011, the ECF arrangement was extended by 9 months, through June 16, 2012 (see Press Release No. 11/3). The Executive Board subsequently approved an augmentation of financing under the ECF

[3] The Extended Credit Facility (ECF) has replaced the Poverty Reduction and Growth Facility (PRGF) as the Fund's main tool for medium-term financial support to low-income countries by providing a higher level of access to financing, more concessional terms, enhanced flexibility in program design features, and more focused streamlined conditionality. Financing under the ECF currently carries a zero interest rate, with a grace period of 5½ years, and a final maturity of 10 years (http://www.imf.org/external/np/exr/facts/ecf.htm). The Fund reviews the level of interest rates for all concessional facilities every two years.

arrangement by SDR 9.54 million (about US$14.5 million or 60 percent of quota) on February 6, 2012. See Press Release No.12/38.

After the Executive Board's discussion on May 23, Ms. Nemat Shafik, Deputy Managing Director and Acting Chair, said:

“Since 2011, Djibouti has been hit hard by external challenges including the surge in commodity prices and the drought in the Horn of Africa, which have affected particularly the poorest households. As a consequence, higher imports, especially of food and fuel, have increased the current account deficit and external financing needs, and have put pressure on fiscal space through lower tax revenues and higher fuel subsidies. Nevertheless, the economy grew at a good pace in 2011, thanks to the recovery of transshipment activities and the transit trade to Ethiopia. Economic activity is expected to remain strong in 2012, buoyed by port activity, trade with Ethiopia, construction and foreign direct investment. However, growth remains concentrated in the port and the free trade zone, and unemployment and poverty remain key challenges.

“The program supported by the IMF’s Extended Credit Facility, which began in 2008, is nearing its conclusion. Despite a mixed implementation record, the program has helped Djibouti maintain macroeconomic stability in a period that saw a transformation of the economy, when massive foreign direct investment expanded port activity, transit trade to Ethiopia soared, the banking system boomed, and the country played an increasingly important geopolitical role. The program has also helped Djibouti make progress toward economic reform, job creation, and poverty reduction. The competitiveness of the economy has strengthened through cost-reducing structural reform and an improved business climate, but much remains to be done in this area to support private sector development.”

Statement by Mr. Kossi Assimaidou, Executive Director
May 23, 2012

I – Introduction

My Djiboutian authorities thank staff and management for their continued support in implementing the ECF-supported program, which enabled Djibouti to stabilize the macroeconomic framework and lay the foundations for a sustainable and balanced growth as well as for a substantial poverty reduction. In a difficult environment, marked by severe drought and piracy activities in the region, increases in world prices of fuel and food, Djibouti has successfully implemented its ECF-supported program. The program's implementation has resulted in sustained economic growth, improved financial public management, and far-reaching structural reforms to underpin fiscal and monetary policies and enhance the economy's competitiveness. However, my authorities are cognizant that more efforts are needed in order to pursue the transformation of the Djiboutian economy into a sub-regional hub for trade, financial services and transportation logistics.

The authorities' commitment to reforms and adjustment measures has helped to maintain the program-performance broadly on track at the end of 2011. Fiscal performance improved and a fiscal deficit of 0.7 percent of GDP in line with the program target was achieved. However, bank financing to the government was marginally higher than programmed due to large repayments of domestic arrears while the ceiling on the accumulation of domestic arrears was missed by a very small margin. On the structural front, all benchmarks for 2011-12 were met. However, capacity constraints coupled with delays in donor financing have prevented the authorities to meet their targets on beneficiary companies defaulting on the requirement to file tax returns and on the introduction of the new budget classification consistent with the GFS standards.

Based on their continued efforts and good performance in implementing the ECF-supported program, my Djiboutian authorities are requesting the support of the Board for the completion of the sixth review and waivers for the nonobservance of performance criteria. Given the need to pursue structural reforms aimed at tackling the numerous challenges facing Djibouti, the authorities have expressed an interest for a successor program based on lessons drawn from the completion of their first ECF-supported arrangement.

II - Recent Macroeconomic Developments

During the period covering the current program, macroeconomic stability was enhanced, which contributed to economic transformation of Djibouti. Massive foreign direct investment expanded capacities of the port and hotels, and contributed to a growing construction sector. Transit trade with Ethiopia has continued to develop, and the electricity grids of the two countries were connected. Thanks, in part, to monetary stability stemming from the currency board arrangement, the banking system expanded rapidly with deposits and credit to private sector growing at double-digit rates. In this context, economic growth is projected to increase from 4.4 percent in 2011 to 4.8 percent in 2012. Inflation will decline from 5 percent in 2011to about 4 percent in 2012 due mainly to the stabilization of world food prices, increases in the supply from the state-owned farms abroad and the reduction of electricity tariffs following the connection to the Ethiopian grid.

While the international reserves increased and ensured the coverage of the currency board, the current account deficit remains large owing to the impact of the severe drought and the high commodity prices, which resulted in higher imports in 2011. Unfortunately, the adverse effects of the drought, notably the famine, will persist in 2012, putting continued pressures on government expenditures.

Amid this challenging environment, the authorities maintained a remarkable and broad-based fiscal discipline. Tax collection increased and made up for the shortfall due to the drought and government transition in the first half of 2011. Moreover, cuts in current and investment expenditures helped compensate shortfall in revenues from the lease on the military base and in external assistance. However, a higher-than-planned repayment of domestic arrears resulted in an increase in net bank credit to government. This repayment will help clean up the public enterprises' balance sheets and make them financially more viable.

Despite this progress, my Djiboutian authorities are mindful of the challenges they face in the period ahead, notably reducing unemployment and poverty through higher growth rates, maintaining fiscal discipline through strong revenue collection and expenditure control while preventing the accumulation of new external and domestic arrears. To this end, my authorities are committed to maintaining sound macroeconomic policies for the rest of 2012. They intend to pursue fiscal reforms and achieve a fiscal surplus. They will also continue their efforts to enhance debt sustainability and further improve banking supervision.

III – Policies and Reforms for 2012

Going forward, my Djiboutian authorities are determined to pursue prudent policies and sound structural reforms, building on the progress achieved under the current ECF-supported program. Smooth implementation of the remaining agenda will be critical to the envisioned transformation of Djibouti into a sub-regional hub and to the objectives of reducing the high unemployment and poverty rates. In this endeavor, the authorities expect to continue benefiting from the assistance of the IMF and other development partners.

Fiscal policy and reforms

For 2012, the authorities aim at a budget surplus of 0.5 percent of GDP. They will also pursue their efforts to improve debt sustainability, repay domestic arrears and strengthen the government financial position with the banking system. This requires accelerated efforts in revenue collection and, in particular, tight control on current spending.

The reform of the tax exemption system remains a priority for the authorities. They are committed to compiling and publishing a list of tax-exempt companies as this step is necessary in their efforts to collect tax returns. In addition, a review of the tax framework in consultation with the private sector will be undertaken with a view to support SMEs and boost Djibouti's role as services and transportation hub in the sub-region. Efforts to enhance the public financial management will also be pursued. Moreover, the authorities remain committed to reforming fuel subsidies. They expect to benefit from Fund's technical assistance to help design and implement better-targeted social safety nets.

Public debt management

Djibouti's external public debt ratio remained broadly stable at about 55 percent of GDP in 2011. However, the updated debt sustainability analysis states that Djibouti remains at high risk of debt distress. The authorities are mindful of the risks that could derive from their ambitious investment plan under the long-term vision entitled Djibouti 2035. They are committed to rely on concessional financing and public–private partnerships in their efforts to execute this investment plan while ensuring debt sustainability.

In addition, the authorities have introduced corrective measures following the accumulation of external arrears in 2011, in order to prevent such occurrences. They are also hopeful that, in the context of an approved successor IMF-supported program, an arrangement with the Paris Club could be achieved in their efforts to reduce Djibouti's external debt stock.

Monetary and financial issues

The currency board arrangement has served the Djiboutian economy well, and the authorities' efforts to maintain the committed rate of coverage will be enhanced. The banking sector remains profitable and highly liquid according to end-2011 indicators. However, the ratio of non-performing loans increased to 9.4 percent. The authorities agreed that this risk is significant and could be exacerbated by governance problems in the banking sector. Thus, they are strongly determined to intensify their efforts, with the Fund TA, to further strengthen the banking supervision and introduce regulation to put into effect the 2011 banking law.

Structural reforms and competitiveness

Enhancing Djibouti's competitiveness is at the top of my authorities' agenda. To this end, their efforts aim at improving the business climate, reducing the costs of factors including labor, electricity and water, as well as restructuring public enterprises for improved public services. The interconnection with the Ethiopian electricity grid has resulted in 30-percent reduction of tariff and substantial decrease in fuel imports by the state owned power company *Electricité de Djibouti*. In addition, the authorities intend to undertake studies to evaluate available sources for domestic electricity production. They also intend to update the National Initiative for Social Development based on the results of the poverty and household budget consumption survey. This step should pave the way for the donor conference planned to take place towards the end of 2012.

IV – Conclusion

My Djiboutian authorities' commitment to reforms under the ECF-supported program has helped the country preserve its macroeconomic stability, improve public financial management and make progress in structural reforms with a view to increasing the economy's competitiveness. Based on their track record, they are requesting the support of the Board for the completion of the sixth review and waivers for non-observance of performance criteria.

My authorities are mindful of the need to pursue the reforms and continue implementing prudent fiscal and monetary policies. In this regard, they are keenly interested in a new arrangement following the present ECF. I would appreciate the Board's support for my Djiboutian authorities' request and their efforts ahead.