INTERNATIONAL MONETARY FUND

IMF Country Report No. 16/385

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

December 2016

SECOND REVIEW UNDER THE EXTENDED CREDIT FACILITY, AND REQUEST FOR WAIVERS FOR NONOBSERVANCE OF PERFORMANCE CRITERIA AND MODIFICATION OF PERFORMANCE CRITERIA—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

In the context of the Second Review under the Extended Credit Facility, and Request for Waivers for Nonobservance of Performance Criterion and Modification of Performance Criteria, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on December 9, 2016, following discussions that ended on September 28, 2016, with the officials of the Democratic Republic of São Tomé and Príncipe on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on November 15, 2016.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for the Democratic Republic of São Tomé and Príncipe.

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

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

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

Press Release No. 16/549
FOR IMMEDIATE RELEASE
December 9, 2016

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Washington, D. C. 20431 USA

IMF Executive Board Completes Second ECF Review for São Tomé and Príncipe, and Approves US$0.9 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the second review of São Tomé and Príncipe's economic program, supported by an Extended Credit Facility (ECF) [1] arrangement. Completion of the review enables the immediate disbursement of SDR 634,285 (about US$0.9 million), bringing total disbursements under the arrangement to SDR 1.9 million (about US$2.6 million).

The Executive Board also approved the authorities' request for waiver for nonobservance of the end June 2016 performance criteria on the domestic primary deficit and net international reserves, based on corrective measures introduced by the authorities. In addition, the Board also approved modification of the end-December target on net international reserves and approved new program targets for 2017.

São Tomé and Príncipe's three-year ECF arrangement for SDR 4.44 million (about US$6.2 million or 60 percent of quota at the time of approval of the arrangement), aims to support the government's economic reform program for stronger and more inclusive growth, was approved on July 13, 2015 (see Press Release No. 15/336).

Following the Executive Board's discussion of the review, Mr. Mitsuhiro Furusawa, Acting Chair and Deputy Managing Director, made the following statement:

"São Tomé and Principe's growth has been subdued, though still positive, reflecting delayed external financing that affected spending on key growth-enhancing capital projects. While the macroeconomic outlook is positive, fiscal and debt sustainability concerns remain critical to maintain a careful balance between growth-enhancing spending and macroeconomic stability.

[1] The ECF is a lending arrangement that provides sustained program engagement over the medium to long term in case of protracted balance of payments problems.

"Recent performance under the ECF-supported program has been mixed. While the structural reform agenda is broadly on track, except for the delayed implementation of the automatic fuel price adjustment mechanism, there were some slippages due to delayed disbursement of external financing which resulted in missing both the domestic primary balance and net international reserves performance criteria for end-June 2016. However, the authorities took corrective measures to keep the end-2016 fiscal program on track.

"The introduction of the automatic fuel price adjustment mechanism at the end of November 2016 should help tackle the longstanding problems of arrears and prevent the accumulation of new domestic arrears and support the authorities' fiscal consolidation efforts. In addition, the planned energy-sector reforms to reduce cost and enhance efficiency are crucial to further strengthen public finances and encourage private sector participation.

"Banking sector vulnerabilities continue to remain a source of concern. It is important that the authorities follow through with the implementation of the strategy to reduce the large stock of non-performing loans, backed by a comprehensive asset quality review. The authorities should also push ahead with measures to reform debt enforcement and insolvency regimes, out-of-court workouts, and improve operational capacity of banks. In the process of liquidating Banco Equador, it is important that attention is paid to safeguard financial stability and minimize costs to the budget.

"Continued commitment to the authorities' structural reform agenda, which prioritizes export diversification and cost competitiveness, is important to support growth and external stability."

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

November 15, 2016

SECOND REVIEW UNDER THE EXTENDED CREDIT FACILITY, AND REQUEST FOR WAIVERS FOR NONOBSERVANCE OF PERFORMANCE CRITERIA AND MODIFICATION OF PERFORMANCE CRITERIA

EXECUTIVE SUMMARY

Context: Growth in the first half of the year was subdued, as the stronger stimulus expected from a timely execution of public investment projects failed to materialize because of the delayed disbursements of external financing. There was also a large fiscal slippage in the first half of the year ahead of the presidential elections. Two end-June program performance criteria and a structural benchmark (SB) were missed, but the targets for the year remain attainable.

Focus: Discussions focused on measures to address the fiscal slippage, manage liquidation of Banco Equador to safeguard financial stability and minimize fiscal cost, and enhance liquidity management by developing a secondary market.

Review: The authorities met four of the six performance criteria (PC). The floors on domestic primary balance and on net international reserves of the central bank were missed. Some indicative targets were also missed. However, good progress was made in implementing the structural reforms under the program, with two out of three end-June 2016 SBs met. The missed SB on the introduction of an automatic fuel price adjustment mechanism is now a prior action for the completion of the review. Based on corrective measures introduced, staff recommends completion of the second review under the Extended Credit Facility and modifications of end-December 2016 PC on net international reserves and supports the authorities' request for waivers for nonobservance of the end-June 2016 PCs on the domestic primary deficit and net international reserves.

Outlook and risks: The economic outlook for 2017 and the medium term is favorable, but not without risks. The main sources of short-term risks to the outlook are ongoing pressures on foreign exchange supply, liquidation of Bank Equador, and continued weakness in the banking sector. In addition, the economy will remain vulnerable to global developments, including weak demand in the key European and emerging markets.

Approved By
David Owen (AFR) and Andrea Richter Hume (SPR)

Discussions were held in São Tomé during September 15–28. The staff team included Maxwell Opoku-Afari (head), Dalmacio F. Benicio, Jehann Jack, Werner Keller and Yun Liu (all AFR). The mission was assisted in headquarters by Bakar Ould Abdallah and Estanislao Rengifo. The mission was joined by Mr. David Owen, the Deputy Director of the African Department at the IMF, and met with the President of the Democratic Republic of São Tomé and Príncipe H.E. Evaristo Carvalho, Vice President of the National Assembly Levy Nazare, Minister of the Presidency of the Council of Ministers and Parliamentary Affairs Afonso Varela da Silva, Minister of Finance and Public Administration Americo d'Oliveira Ramos, the Governor of the Central Bank of São Tomé and Príncipe Maria do Carmo Trovoada Silveira, senior government officials, representatives of the private sector, including banks and the Chamber of Commerce, the international donor community, and student groups.

CONTENTS

TABLES

APPENDICES

CONTEXT: ENTRENCHED POLITICAL STABILITY—AN OPPORTUNITY FOR DEEPER REFORMS

1. **Mr. Evaristo Carvalho, backed by the ruling Independent Democratic Action (ADI) party, won the August 7, 2016 presidential run-off election.**[1] He defeated incumbent President Pinto da Costa, who was a distant runner-up in the first round and boycotted the second round, alleging electoral fraud. Mr. Carvalho was sworn in as president on September 3, 2016.

2. **The election outcome confirms the ruling party's dominance of São Tomé and Príncipe's politics and government.** The party has now consolidated the control of all branches of the government, paving the way for greater political stability for the remainder of the current prime minister, Patrice Trovoada's term in office. It also comes with greater responsibility to deliver the promises of improved economic outcomes and better living standards for the people. This opens a unique window of opportunity for moving forward with far reaching reforms, including in the judiciary system, and to significantly remove structural bottlenecks that have hampered the development of the private sector to support inclusive and shared growth.

RECENT ECONOMIC DEVELOPMENTS

3. **Economic activity in 2016 has been subdued, though still positive.** Real GDP growth is now estimated at 4 percent, lower than the projected 5 percent, mainly reflecting lower-than-projected foreign-financed capital spending and lackluster credit growth. Meanwhile, two key sectors, cocoa and tourism, have performed strongly to offset part of the slowdown in economic activity. There are signs of growing underlying inflationary pressures, with inflation increasing to 5.8 percent at the end of September from 4 percent in December 2015, driven by food shortages resulting from constrained imports (¶ 4), adverse effects of insect plague on harvest, and a change in the CPI basket.

4. **A significant shortfall in external financing created short-term foreign exchange supply constraints which is being addressed.**[2] It is estimated that about 7 percent of GDP of external financing (including planned privatization proceeds) has not materialized. However, the bulk of donor budget support (from the World Bank and the EU) is expected in the last quarter of the year. Looking ahead, both the World Bank and the EU are considering re-aligning the timing of their budget support to avoid the bulge in the last quarter of the year. The central bank was slow in responding to the growing foreign exchange needs.

[1] São Tomé and Príncipe's head of government is the prime minister, while the president is head of state with more limited powers.

[2] São Tomé and Príncipe has a fixed exchange rate arrangement, pegged to the euro since January 2010. There is a credit line agreement with Portugal that triggers when reserves fall below three months of import cover.

However, in line with staff recommendations, they are now meeting all foreign exchange demands from banks.

5. **The current decline in imports will temporarily improve the current account in 2016.** The import contraction in the second half of the year, combined with strong cocoa production and exports, will lead to an improvement in the current account deficit to about 8.9 percent of GDP at the end of 2016 compared to the 12.2 percent of GDP projected earlier. The services account is improving significantly due to stronger growth in net travel receipts and contained non-factor services imports. Foreign direct investment increased due to renewed interest for petroleum exploration in the exclusive economic zone despite inactivity in the Joint Development Zone (JDZ) with Nigeria. Gross international reserves have however, declined to US$57.1 million (4.1 months of imports) at the end of June 2016, but remain adequate.

6. **There was a large fiscal slippage in the first half of the year.** The domestic primary deficit exceeded the end-June 2016 target of 0.7 percent of GDP by 1.3 percent of GDP, because of higher-than-programmed domestic primary spending (mainly goods and services and transfers), more than offsetting slightly better-than-projected tax revenue collection. Transfers and spending on goods and services were frontloaded in the first half of the year (Text Table 1), reflecting electoral spending pressures ahead of the July and August presidential elections. The overall fiscal balance however, turned out better than targeted, because of shortfalls in foreign-financed capital spending.

7. **Treasury bill issuance, planned for the year, was frontloaded to finance the primary deficit.** Part of the domestic primary spending was financed by frontloading the issuance of 2 percent of GDP of treasury bills, as privatization proceeds failed to materialize from the planned off-loading of part of the government shares in the largest commercial bank and the largest telecom company[3] (amounting to about 5 percent of GDP). These sales are no longer expected to be finalized this year, due to delays in the negotiations with interested parties. Disbursement for external financing for capital projects was also delayed, including about 3.8 percent of GDP financing from Turkey and Kuwait. Negotiations of these loans now look unlikely to be finalized this year. As a result, staff excluded this financing and privatization proceeds from the baseline projection. The authorities did however, receive an unbudgeted disbursement of US$4.5 million from Angola, constituting the third disbursement of the loan contracted in 2014.

[3] As indicated in the staff report of the first ECF review, the government was expecting proceeds from off-loading its shares in the largest commercial bank and the telecoms company to finance critical investment.

Text Table 1. Sources of Fiscal Slippages, June 2013–16

	Jun-13	Jun-14	Jun-15	Jun-16			2016		
				Program	Actual	Difference	Program	Projection	Difference
(in percent of GDP, unless otherwise specified)						(Act. - Prog.)			(Act. - Prog.)
Total revenue and grants	12.7	11.8	9.4	12.3	11.5	-0.8	35.1	31.1	-3.9
Total domestic revenue	9.1	6.7	7.4	6.3	7.6	1.3	17.1	15.7	-1.4
Tax revenue	7.6	6.1	6.8	5.4	6.0	0.6	14.9	13.5	-1.5
of which: excluding ENCO's payment of tax arrears	6.6	6.1	5.6	5.4	6.0	0.6	14.9	13.5	-1.5
Nontax revenue	1.5	0.7	0.6	0.9	1.6	0.7	2.2	2.3	0.1
of which: excluding oil revenue	1.5	0.7	0.6	0.9	0.7	-0.2	1.3	1.4	0.1
Grants	3.7	5.0	2.0	6.0	3.9	-2.1	17.3	14.7	-2.6
Total expenditure and net lending	14.9	16.3	15.1	16.1	13.3	-2.9	44.1	29.5	-14.6
Current expenditure	9.0	9.1	8.7	7.4	8.4	0.9	17.4	16.0	-1.4
Personnel costs	4.3	4.6	4.4	4.0	4.0	0.0	8.6	8.7	0.1
Goods and services	1.9	1.8	1.7	1.2	1.6	0.4	3.1	3.0	-0.1
Transfers	2.3	1.8	1.7	1.5	2.0	0.5	4.0	2.9	-1.1
Other expenditures	0.2	0.6	0.7	0.4	0.5	0.1	1.0	0.8	-0.3
Capital expenditure	5.9	7.2	6.3	8.7	4.8	-3.9	25.8	12.6	-13.2
Financed by the Treasury	0.7	0.5	0.2	0.4	0.4	0.0	0.7	0.7	0.0
Financed by external sources	5.2	6.7	6.1	8.3	4.4	-3.9	20.2	11.9	-8.3
HIPC Initiative-related social expenditure	0.0	0.0	0.1	0.0	0.1	0.1	0.9	0.9	0.0
Domestic primary balance [1]	-0.4	-2.6	-1.3	-0.7	-2.0	-1.3	-2.0	-2.0	0.0
Overall fiscal balance (commitment basis)	-2.2	-4.5	-5.7	-3.8	-1.8	2.0	-9.0	1.6	10.6
Memo items:									
Disbursements of project loans	2.1	3.1	6.6	3.6	1.8	-1.8	8.4	2.8	-5.6
Nominal GDP (in billions of Dobras)	5,581	6,227	7,030	7,790	7,774	…	7,847	7,774	…

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

[1] Exclude oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlays.

8. The arrears reduction plan is being broadly implemented as agreed under the program. In addition to staying current on payments of utility bills, the government signed an agreement with the oil importing company (ENCO) in June, detailing a plan to clear the outstanding arrears over a forty-year period, with the payment of the first installment expected in the second half of the year. There are ongoing efforts to get a similar agreement signed between ENCO and the electricity and water producing company (EMAE) by the end of the year, after its restructuring plan has been approved by the government. Overall, government and EMAE arrears to ENCO (10 and 13.5 percent of GDP respectively) increased by less than projected (a combined 0.3 percent of GDP) at the end of June 2016, with the increase in EMAE's new arrears more than offsetting the decline in the government arrears on the account of lower international oil prices. Government arrears to the general suppliers have been kept in line with the program (3.6 percent of GDP).

9. Excess liquidity in the banking system remains high despite a contraction of monetary aggregates and modest credit expansion in the first half of the year. Broad money fell by 6.2 percent during the first seven months of the year, primarily on account of lower net foreign assets that reflected weak economic activity and the fall in foreign exchange inflows. Private sector credit however, increased marginally as interest rates fell across all classes of deposits and loans. That notwithstanding, the excess liquidity in the banking system remains high, close to a third of deposits, reflecting the lack of commercial lending opportunities (including lack of bankable projects) for commercial banks in an environment of persistently high non-performing loans.

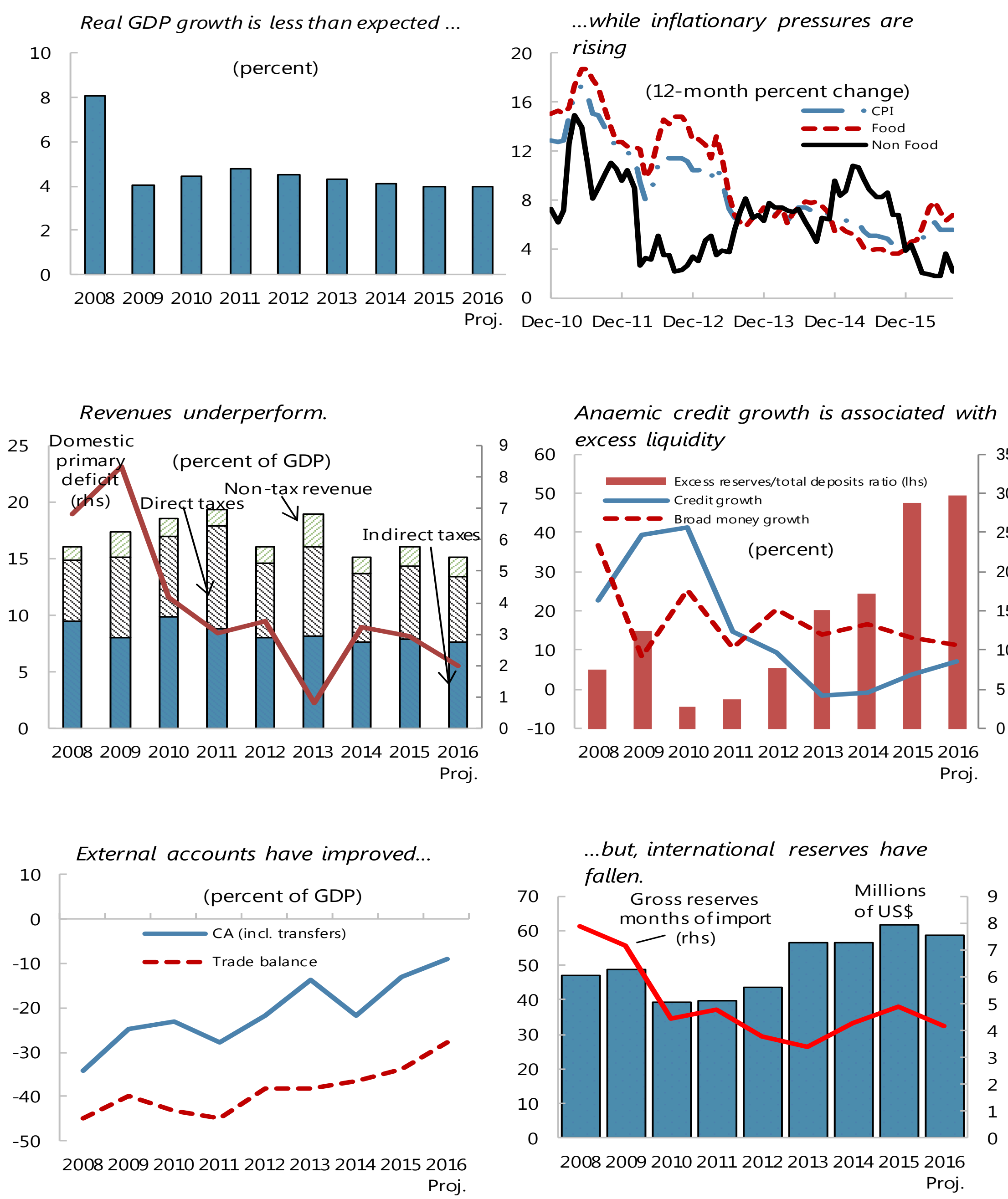
10. Signs of stress in the banking sector remain. Capital adequacy for the industry remains strong with the risk-weighted assets ratio at 23.9 percent at end-June 2016, even though this varies across banks. Banks remain loss-making, albeit less so than in earlier periods. Return on assets and return on equity improved by 2.9 and 14.9 percentage points respectively, though they still negative. The industry non-performing loans (NPLs) ratio also increased by 6.1 percentage points to 35.9 percent between December 2015 and June 2016, reflecting loan reclassifications after on-site inspections and rising bad debt in the construction sector.[4] The NPL ratio excluding Banco Equador was 28 percent at the end of June 2016.

11. The central bank of São Tomé and Príncipe (BCSTP) moved ahead to resolve Banco Equador[5], by cancelling its license on August 1, 2016 while protecting small and non-connected depositors. An application has been submitted to the Court of Tribunal to initiate liquidation proceedings in line with the new banking resolution law. This action was the last resort after failure to identify a suitable investor to buy a transitional bank created from good assets and liabilities of Banco Equador. The bank, the fourth largest by assets (8 percent of GDP), has been under Administration since January 2015. The central bank has provided financing of €1.7 million (0.5 percent of GDP) to protect small but non-connected depositors, backed by a guarantee from the Council of Ministers. So far, the central bank has paid more than 50 percent of eligible deposits to other commercial banks. The central bank is expected to recover this cost through the sale of assets. In the meantime, the full cost of the liquidation, that is the €1.7 million and any additional cost from managing assets until liquidation is completed, will be reflected in the budget, starting with the 2017 budget.

[4] Banks attributed the increase in NPL in the construction sector to the slowdown in economic activity in the first half of the year and expect this to be resolved by the end of the year.

[5] The bank's equity structure shows that Mombaka Sociedade de Empreendimento, Lda., a firm established under Angolan law, has a dominant position (roughly 83 percent stake) in the institution.

Figure 1. São Tomé and Príncipe: Recent Macroeconomic Developments



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

PROGRAM PERFORMANCE

12. Program implementation was mixed. The authorities met four of the six end-June performance criteria (PC) and five out of the 10 end-March indicative targets (IT) (see Table 1, MEFP Attachment I). There were some policy delays and slippages ahead of the July and August elections resulting from frontloading domestic primary spending and delayed disbursement of external financing. As a result, the end-June PCs, floors on domestic primary balance and on net international reserves of the central bank were missed, the former by a wide margin of about 1.3 percent of GDP (the target for end-June was -0.7 percent of GDP). Moreover, the indicative target ceiling on dobra base money was exceeded by almost 12 percent due to increases in net deposits of the central government, and pro-poor spending was below the floor by about 1 percent. On the other hand, indicative targets on new domestic arrears and tax revenue were met.

13. The authorities have also made progress in implementing key structural reforms under the program (see Table 2, MEFP Attachment I). Two of the three end-June 2016 structural benchmarks were met. The authorities submitted to staff a comprehensive strategy designed to help banks deal with high NPLs. As agreed during the first ECF review, the authorities have also been granted powers, by the National Assembly, to directly change five tax laws, including the legislation to transfer the collection of tax arrears from fiscal courts judges to the tax administration. The new legislation, transferring collection of tax arrears to the tax administration, came into effect in October, 2016. On the other hand, the end-June 2016 structural benchmark to introduce an automatic fuel price adjustment mechanism to address the longstanding problem of accumulation of domestic arrears, which has hampered fiscal consolidation efforts, was missed. The authorities attributed this delay to capacity constraints and delays in setting up the institutional and legal framework to support the entity in charge of implementing and monitoring this mechanism.

ECONOMIC OUTLOOK AND RISKS

14. While the economic outlook for the second half of 2016 is mixed, 2017 and beyond are more favorable albeit with downside risks. The expected pick-up in growth in the second half of the year is will depend on full resumption of foreign-financed capital spending. Strong tourism receipts and subdued imports will however, result in a larger-than-projected decline in the current account deficit from 13 percent of GDP in 2015 to 9 percent of GDP in 2016. Prospects for 2017 and the medium-term, however, remain favorable; the medium-term growth target of 5.5 percent remains attainable as the government steps up efforts to address the supply constraints impacting imports of capital and intermediate goods. It is also expected that foreign-financed capital spending will pick up in 2017. Inflation is expected to remain at 5.5 percent at the end of 2016 and then fall to 3 percent in 2017. Risks to this outlook are tilted to the downside. Domestically, the main risks emanate from the high and rising NPLs in the banking sector, which could disrupt the recent resumption of lending and general business and trade activity, as well as risks around the liquidation of Banco Equador. Externally, disbursement of foreign financing for capital spending could be further delayed while global economic and financial uncertainties could curtail FDI inflows, demand for cocoa, and tourist arrivals.

POLICY DISCUSSIONS

A. Address Fiscal Slippage

15. The end-December 2016 domestic primary deficit target of 2 percent of GDP remains feasible and appropriate, despite the slippage in the first half of the year. However, it will require greater fiscal discipline amidst poorer revenue prospects in the second half of the year, as current slowdown in imports is holding back international trade tax revenue collection. It is currently estimated that this will result in a 1.4 percent of GDP shortfall in revenue. Notwithstanding this projected revenue shortfall and the expenditure slippages in the first half of the year, staff assesses that end-2016 fiscal targets are attainable. The fiscal slippage in the first half of the year will be corrected by ensuring that domestic spending on goods and services in the second half is kept within the annual target. To that end, staff and the authorities agreed on closer monitoring of budget execution to ensure expenditure commitments are issued based on available resources and in line with program objectives—in particular, keeping spending on goods and services in line with the annual budget ((¶ 5). In addition, the authorities have also agreed to cut transfers to sub national and autonomous entities and other current spending, amounting to 1.4 percent of GDP (Text Table 2) to fully offset the revenue shortfall that has emerged in the second half of the year, and ensure that the end-2016 domestic primary deficit target of 2.0 percent of GDP is achieved. Foreign-financed capital spending will pick up by 8.1 percent of GDP in the second half of the year, including disbursements from Taiwan, Province of China (US$15 million), African Development Bank (US$9 million), Portugal (US$3.9 million) and the World Bank (US$5 million).

Text Table 2. Revenue Shortfalls and Corrective Measures, 2016[1]

	Percent of GDP
Slippages:	
Tax revenue shortfalls	1.4
Corrective measures:	
Transfers	-1.1
Other current expenditures	-0.3

Source: IMF staff estimates
[1]Relative to the program.

16. Staff and the authorities reached agreement on key parameters of the fiscal program for 2017, broadly in line with the baseline fiscal path agreed during the first review. Overall, the 2017 budget will target a lower tax revenue of 15.0 percent of GDP, 0.4 percent of GDP lower than agreed under the program, in line with the actual growth in tax revenue over the past three years, but also reflecting current developments in imports and delays in reaping the gains of the new legislation to speed up tax arrears collection. However, the domestic primary deficit target of 1.8 percent of GDP will be maintained as agreed under the program. Consistent with the program's medium-term objective of moving from high to moderate risk of debt distress, foreign-financed capital spending will be capped to the level of disbursements of already contracted project loans and grants and limited new borrowing. The budget will also make provision for new issuance of treasury bills (at least 2 percent of GDP), payment of the second installment of amortization of arrears to ENCO (1 percent of GDP), first of the seven annual installments of the contingency costs of the liquidation of Banco Equador (0.05 percent of GDP) in the form of forgone transfers from the central bank. The budget is expected to be submitted to the National Assembly by the end of November this year.

17. Fiscal reforms agreed under the program remain on track (MEFP Attachment I ¶ 11). These include enhancing revenue mobilization through legislative and tax administration reforms, strengthening Public Financial Management (PFM) to ensure transparency, sound, and efficient management of public resources, and improving debt management. The authorities will also finalize and submit a draft public private partnership (PPP) law for the approval to parliament by the end of June 2017 (*structural benchmark*).

B. Strengthen Liquidity Management

18. Excess liquidity continues to undermine the authorities' efforts at monetary management. Banks' liquidity management continues to be hindered by the slow pick up of the recently introduced interbank market as almost all banks refuse to participate in the interbank market. As a result, banks continue to maintain a high level of precautionary reserves, although this position varies across banks.

19. Staff and the authorities agreed on the need to further refine the liquidity forecasting and management tools and review the functioning of the nascent money market, including the experience with this year's issuance of treasury bills (MEFP Attachment I ¶ 12). Staff and the authorities agreed on the need to focus on creating the platform to more aggressively use central bank notes to mop up excess liquidity, the development of a secondary market for government securities, creation of conditions for long-term liquidity management, and steps to reduce the stigma associated with participating in the interbank money market by enforcing mandatory publication of banks' audited financial statements. The BCSTP is in the early stages of developing a secondary market and introducing longer-term securities, including a 3–year note, responding to growing market interests.

C. Reduce Risks in the Banking Sector

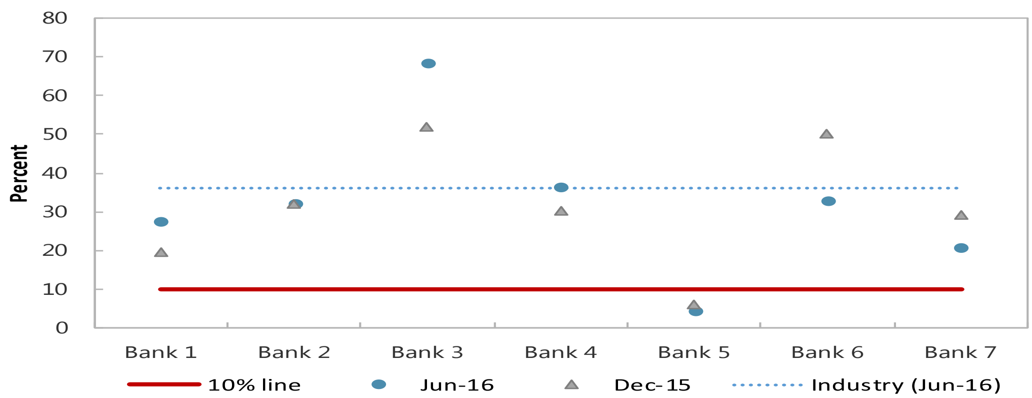
20. Banking sector vulnerabilities continue to be a source of concern (MEFP Attachment I ¶ 13). The central bank's action to officially liquidate Banco Equador has not generated any spillover effect to the rest of the banking industry—there have been no defaults as a result of the liquidation and there has not been any legal challenge so far. The liquidation of Banco Equador has not impacted credit supply given that it has not been active in the credit market in the past 18 months while under administration. Key stakeholders in the banking industry welcomed the central bank's decision, noting that it addresses a source of uncertainty in the industry, given the long period that the bank had been under administration. The court is yet to officially rule on the liquidation application and appoint a liquidator. The Fund, in the meantime, provided technical assistance in November to guide the central bank and the liquidator in the liquidation process to ensure that the process is handled carefully to protect financial stability and minimize cost to the budget (MEFP Attachment I ¶ 14).

21. Staff emphasized the urgency of implementing the time-bound action plan to address the large stock of NPLs in the banking system. The latest quarterly financial sector indicators show further worsening in the non-performing loans (NPL) ratio by 6.1 percentage points since the beginning of the year to 35.9 percent at end-June 2016, largely representing increases in NPLs at Banco Equador.[6] The BCSTP has already taken initial steps in implementing its NPL reduction strategy; work has started with banks to strengthen their credit risk evaluation and management expertise and implement basic internal asset quality reviews (AQRs) in the context of its on-site inspections. These efforts have already started yielding results; there have been asset reclassifications in banks that have recently completed on-site supervision inspections resulting in increases in provisions.

22. A comprehensive AQR will back the NPL reduction strategy. To further consolidate these efforts, the authorities are seeking support (including from the World Bank) to get an independent firm to conduct a comprehensive AQR for all banks (*end-December 2017 structural benchmark*). It is also expected that the BCSTP will be fully equipped, after the AQR, to decide on which banks need to improve internal policies and procedures, increase provisioning, and promptly recapitalize if appropriate. In the meantime, staff also urged the authorities to begin introducing some measures to reform debt enforcement and insolvency regimes, out-of-court workout aimed at rehabilitating viable debtors, and improve the operational capacity of banks to reduce NPLs. Efforts to strengthen the risk-based supervision practices are ongoing and an assessment of regulation and supervision (in lieu of a full assessment of compliance with Basel Core Principles) was concluded in August 2016 (*end-December 2016 structural benchmark*).

[6] The end-June NPL ratio excluding Banco Equador is 28 percent.

Text chart 1. NPL Ratios by Bank, Dec–15 and Jun–16



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

D. Structural Reforms

23. The structural reform agenda has appropriately focused on reducing the cost and improving reliability of energy supply. The main components of the government's strategy to address the unreliable supply and high cost of electricity—including the substitution of the existing thermo-powered plant with cheaper alternatives—are progressing well. The World Bank energy sector project which aims to double the capacity of hydropower generation to 4 megawatts and invest in the electrical grid has started. Moreover, the government through EMAE has signed Memoranda of Understanding and is currently finalizing a number of power purchase agreements with two private companies to build and operate gas (20 megawatts) and a solar (10 megawatts) power plants that will produce and sell electricity by 2017 at less than half the current cost. While recognizing that these private initiatives can enable EMAE to eliminate cross-subsidies and move to more competitive cost-recovery electricity tariffs (*end-December 2016 structural benchmark*), staff urged the authorities to ensure that the contracts with the private companies avoid taking on any liability (explicit or otherwise) of the public sector.

24. The government is working on key strategic documents with a view to operationalize its 2030 transformation agenda. Work is underway on a new 5–year National Development Plan intended to guide government actions going forward. The plan which is expected to be completed by the end of the year, with help of the UNDP, will be aligned with the sustainable development goals and will replace the current PRSP-II which expires at the end of 2016. The completion of an export diversification strategy focusing on tourism sector, initially an end-December 2016 structural benchmark, has been delayed due to setbacks in securing external support to develop the strategy document. The World Bank is currently helping the authorities to develop an export diversification strategy as part of the broad project of developing an investment promotion strategy. The export diversification strategy is now expected to be completed at the end-December 2017 (MEFP Attachment I ¶ 39).

PROGRAM ISSUES, SAFEGUARDS, AND RISKS

25. The authorities are requesting waivers for nonobservance of the PCs on the domestic primary balance and net international reserves. Even though the end-June 2016 PC on domestic primary balance has been missed, staff believes that the end-December 2016 target can be met. As discussed earlier (¶ 14, and Text Table 2), staff believes that the proposed corrective measures—cutting transfers and other current expenditure in the second half—would ensure that the end-December 2016 target is met. With regards to the floor on net international reserves, staff proposes a revision to the end-December 2016 target to reflect the delayed disbursement of the loans from Turkey and Kuwait and the uncertainties surrounding privatization proceeds. The current adjuster in the program is not fully adequate to account for this large deviation (about 7 percent of GDP).

26. In addition, staff proposes to set the 2017 PCs (see Table 3, MEFP Attachment I). Staff proposes to set end-June and end-December 2017 PCs and end-March and end-September 2017 indicative targets. Besides changes suggested above, all other PCs and indicative targets will remain the same as proposed in the first ECF review.

27. Staff and the authorities agreed on the way forward on key structural benchmarks. The structural benchmark on the introduction of the automatic fuel price adjustment mechanism (see country report No. 16/174), which was missed at the end of June 2016, is now a prior action for the completion of the second review. This reform is macro-critical as it ensures full cost recovery of domestic fuel prices and addresses a long standing arrears problem between the government and ENCO, which has hampered fiscal consolidation. In the current low international oil price environment, the introduction of this mechanism at current domestic fuel prices, will ensure positive price gains which the government has agreed to use to reduce the stock of arrears with ENCO. The government will announce the introduction of the mechanism at the end of November and the effective price of the different categories of fuel, including a schedule of the pricing mechanism. In addition, staff and the authorities propose to: (i) extend the deadline for the completion of a national export diversification strategy from end-December 2016 to end-December 2017 due to setbacks in securing external support to develop the document; (ii) complete an assessment of regulation and supervision in lieu of a full assessment of compliance with Basel Core Principles; and (iii) introduce two new structural benchmarks for 2017 covering a public partnership law and an independent and detailed asset quality review of banks (Table 4, MEFP Attachment I). The third ECF review is expected to be completed on or after April 15, 2017, the fourth review on or after October 15, 2017, and the fifth review on or after April 15, 2018.

28. The program is fully financed and staff's assessment of São Tomé and Príncipe's capacity to repay the Fund remains broadly unchanged from the ECF arrangement request (Table 11). São Tomé and Príncipe's capacity to repay the Fund remains strong, as obligations remain small relative to exports and reserves.

29. Safeguards. The BCSTP is committed to implementing the recommendations from the September 2015 safeguards assessment, which included independent oversight of the audit mechanisms, internal controls, financial reporting (*end-December 2016 structural benchmark*), and amendments to the central bank legislation to strengthen the bank's institutional and financial autonomy, and provide for independent oversight in the governance structure.

30. Statistics. Efforts to address data shortcomings will continue, including improving the balance of payments statistics and extending the coverage of the international investment position. The national statistics institute (INE) has completed the rebasing of the national accounts to 2008 and a new CPI, reflecting price movements in a broader basket of goods and services, using 2014 as the base year. The next steps include splicing the pre–and post–2008 GDP and pre–and post–2014 CPI series, and improving the statistics by developing data on the components of GDP on the demand side and quarterly GDP, including high frequency indicators of economic activity. Scheduled STA TA in early 2017 will support these initiatives.

31. Risks to the program are high. Slower growth than envisaged and financial sector vulnerabilities could become more pressing. While recent gains in political stability provide the right environment for deepening reforms, weak capacity could constrain program implementation. There are also risks that the persistent high NPLs could delay the resumption in credit to support economic activity. Continued technical assistance particularly in banking supervision, PFM and tax administration and policy would in part mitigate risks related to capacity. In addition, there was heavy rainfall on October 18, 2016 in the autonomous Island of Principe that resulted in severe flooding and landslides affecting a number of properties. The full extent of the damage is currently being assessed and there is the likelihood that the central government may have to intervene which could impact budget execution for 2016.

STAFF APPRAISAL

32. São Tomé and Príncipe's macroeconomic performance in 2016 remains satisfactory as challenges emerge. Economic activity has been subdued. GDP is now projected to grow at 4 percent instead of the 5 percent projected earlier. Budget execution for the rest of the year will be challenging due to the impact of falling imports on tax revenue collection. Staff welcomes the authorities' commitment to keep spending on goods on services in the second half of the year within the annual budget and to cut transfers in order to achieve the end year fiscal target. There are underlying inflationary pressures resulting from rising food prices. Risks to the outlook are mainly on the downside.

33. Performance under the ECF arrangement has been uneven but staff and the authorities have reached an agreement on key measures to keep the program on track. Staff supports the authorities' commitment to cut domestic primary spending to fully offset expenditure slippages in the first half of the year as well as the projected shortfall in tax revenue in order to meet the 2 percent of GDP domestic primary deficit target at the end of December 2016. The introduction of 12 targeted amendments to the tax code (Appendix II), to update some specific taxes, transfer tax arrears collection from fiscal court to the tax administration, and fix the minimum taxable income, should help enhance domestic revenue collection to consolidate the fiscal reforms being introduced. The implementation of structural benchmarks continues to be strong even though there was a delay in introducing the key reform on automatic fuel price adjustment mechanism. Staff welcomes the authorities' commitment to implement this reform as a prior action for the completion of this review.

34. Staff supports the 2017 budget. The key parameters of the 2017 budget are in line with the objectives of the program. Successful execution of the budget will however, depend on a number of issues: first, realizing the tax revenue target to support the achievement of the domestic primary balance target, and second, prompt execution of donor financing to prevent additional pressure on domestically-financed spending as seen in the first half of 2016.

35. Staff strongly urges the authorities to carefully manage the growing risks in the banking sector. While staff welcomed the central bank's decision to finally liquidate Banco Equador, staff stresses the need for a careful handling of the liquidation process to protect financial stability and minimize costs to the budget. Staff also emphasizes the urgency of implementing the time-bound action plan to address the large stock of NPLs in the banking system. In that context, staff sees a completion of an independent and detailed asset quality review as essential to removing uncertainty on the quality of assets being carried by banks and also setting the stage for required remedial actions by banks. In the meantime, staff strongly encourages the authorities to begin introducing other fundamental reforms including reforming debt enforcement and insolvency regimes, introducing out-of-court workouts aimed at rehabilitating viable debtors, and improving the operational capacity of banks to reduce NPLs.

36. Efforts by the authorities to focus on advancing reforms in the electricity sector, business environment, and export diversification are welcome. While supporting the ongoing private sector involvement in the electricity sector, staff urges the authorities to avoid taking on any additional public sector liability, including providing tax exemptions which could undermine fiscal consolidation.

37. Staff recommends completion of the second review and the disbursement of an amount equivalent to SDR 634,285 under the ECF arrangement. Based on corrective measures taken (¶ 14, and Text Table 2), staff supports the authorities' request for waivers for nonobservance of the end-June 2016 PCs on domestic primary balance and net international reserves, and modification of the end-December 2016 PC on net international reserves, and setting end-June 2017 and end-December 2017 PCs.

Table 1. São Tomé and Príncipe: Selected Economic Indicators, 2014–19

(Annual change in percent, unless otherwise indicated)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
National income and prices										
GDP at constant prices	4.1	4.0	5.0	4.0	5.5	5.0	5.5	5.5	5.5	5.5
Consumer prices										
End of period	6.4	4.0	4.0	5.5	3.0	3.0	3.0	3.0	3.0	3.0
Period average	7.0	5.3	3.9	5.4	3.5	4.2	3.0	3.0	3.0	3.0
External trade										
Exports of goods and nonfactor services	64.3	1.7	9.2	7.2	7.2	10.6	6.5	6.6	8.2	4.6
Imports of goods and nonfactor services	28.6	-18.5	11.8	2.7	7.0	11.9	5.8	8.1	2.9	11.0
Exchange rate (dobras per US$; end of period) [1]	20,148	22,424	...	...	...	...	...	...	...	...
Real effective exchange rate (depreciation = -)	6.9	0.7	...	...	...	...	...	...	...	...
Money and credit										
Base money	23.2	37.5	10.4	10.3	6.3	6.8	7.2	7.2	9.7	7.9
Broad money (M3)	16.8	13.1	11.6	11.4	6.3	6.8	7.2	7.2	7.9	7.9
Credit to the economy	-1.0	3.8	7.0	7.1	4.8	4.8	5.2	5.2	7.5	7.5
Velocity (GDP to broad money; end of period)	2.7	2.6	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Central bank reference interest rate (percent)	12.0	10.0	...	...	...	...	...	...	...	...
Average bank lending rate (percent)	23.2	23.3	...	...	...	...	...	...	...	...
Average bank deposit rate (percent)	8.9	6.9	...	...	...	...	...	...	...	...
Government finance (figures in percent of GDP)										
Total revenue, grants, and oil signature bonuses	25.2	28.0	35.1	31.1	33.4	30.1	33.7	30.3	33.5	32.5
Of which: tax revenue	13.7	14.3	14.9	13.5	15.4	15.0	15.9	15.5	16.5	16.1
Nontax revenue	1.5	1.5	2.2	2.3	1.3	1.4	1.3	1.4	1.3	1.4
Grants	10.0	11.5	17.3	14.7	16.6	13.7	16.4	13.5	15.6	15.1
Oil signature bonuses	0.0	0.8	0.7	0.7	0.0	0.0	0.0	0.0	0.0	0.0
Total expenditure and net lending	30.5	34.3	44.1	29.5	37.3	31.8	36.2	32.7	33.9	33.6
Personnel costs	8.9	8.9	8.6	8.7	8.5	8.5	8.4	8.4	8.4	8.4
Interest due	0.7	0.8	0.7	0.7	0.7	0.8	0.7	0.7	0.7	0.7
Nonwage noninterest current expenditure	8.5	8.5	8.1	6.6	7.9	7.9	7.6	7.6	7.6	7.6
Treasury funded capital expenditures	0.9	0.7	0.7	0.7	1.6	1.1	2.2	1.8	2.5	2.1
Donor funded capital expenditures	11.4	14.8	20.2	11.9	17.9	12.8	16.7	13.7	14.0	14.0
HIPC Initiative-related social expenditure	0.2	0.6	0.9	0.9	0.6	0.6	0.5	0.5	0.7	0.7
Domestic primary balance [2]	-3.2	-3.0	-2.0	-2.0	-1.8	-1.8	-1.5	-1.5	-1.4	-1.4
Overall balance (commitment basis)	-5.3	-6.3	-9.0	1.6	-3.8	-1.7	-2.5	-2.4	-0.4	-1.1
External sector										
Current account balance (percent of GDP)										
Including official transfers	-21.8	-12.9	-12.2	-8.9	-12.7	-11.3	-12.6	-12.1	-10.5	-13.0
Excluding official transfers	-32.2	-25.2	-29.5	-23.6	-29.7	-25.2	-29.3	-25.8	-26.4	-28.1
PV of external debt (percent of GDP)	30.1	39.7	36.2	36.2	38.3	38.3	39.4	39.4	37.9	37.9
External debt service (percent of exports) [3]	3.7	3.8	4.8	6.8	4.3	6.0	4.0	5.6	3.8	5.4
Export of goods and non-factor services (US$ millions)	88.4	89.9	87.7	96.4	94.1	106.6	100.2	113.6	108.5	118.9
Gross international reserves [4]										
Millions of U.S. dollars	56.5	61.9	72.8	58.7	75.9	63.9	82.4	68.9	87.6	75.9
Months of imports of goods and nonfactor services [5]	4.3	4.9	5.0	4.2	5.0	4.3	5.1	4.3	5.0	4.5
National Oil Account (US$ millions)	9.9	10.3	11.5	11.5	9.3	9.3	7.6	7.6	6.2	6.2
Memorandum Item										
GDP										
Billions of dobras	6,435	7,018	7,847	7,774	8,287	8,248	8,839	8,839	9,533	9,533
Millions of U.S. dollars	348.5	317.7	349.2	351.5	371.2	374.7	396.0	402.5	428.8	436.7

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

[1] Central Bank (BCSTP) mid-point rate.

[2] Excludes oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlay.

[3] Percent of exports of goods and nonfactor services.

[4] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements and foreign currency deposits of commercial banks used application deposits for new licensing or for meeting capital requirements.

[5] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

Table 2. São Tomé and Príncipe: Financial Operations of the Central Government, 2014–19
(Billions of dobra)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Total revenue and grants	1618	1965	2754	2422	2771	2480	2981	2680	3194	3099
Total revenue	973	1108	1343	1224	1391	1349	1528	1490	1704	1662
Tax revenue	879	1006	1170	1047	1279	1237	1408	1370	1575	1532
Nontax revenue	94	102	172	177	112	112	119	120	129	130
of which: oil revenue	0	0	66	66	0	0	0	0	0	0
Grants	645	804	1355	1141	1380	1131	1453	1190	1490	1437
Project grants	500	610	995	781	1051	801	1121	859	1249	1144
Nonproject grants	103	61	212	212	180	181	184	183	125	177
of which: unconfirmed	...	...	0	0	37	37	42	42	47	47
HIPC Initiative-related grants	42	133	149	149	149	149	149	149	116	116
Oil signature bonuses	0	53	56	56	0	0	0	0	0	0
Total expenditure	1960	2405	3459	2294	3088	2621	3199	2893	3236	3204
Of which: Domestic primary expenditure	1181	1315	1819	1312	1543	1498	1664	1624	1836	1798
Current expenditure	1157	1274	1366	1248	1417	1418	1475	1475	1594	1600
Personnel costs	569	623	676	676	706	702	742	741	800	800
Interest due	44	54	56	56	60	66	59	59	65	71
Goods and services	223	239	240	234	254	253	271	271	292	292
Transfers	230	248	311	223	311	311	312	312	336	337
Other current expenditure	92	110	82	59	87	86	93	92	100	100
Capital expenditure	793	1087	2025	978	1619	1152	1675	1369	1573	1535
Financed by the Treasury	58	51	53	53	134	94	199	159	238	200
Financed by privatization proceeds	...	...	388	0	0	0	0	0	0	0
Financed by external sources	735	1036	1584	926	1485	1057	1476	1210	1335	1335
HIPC Initiative-related social expenditure	10	44	68	68	52	52	49	49	70	70
Domestic primary balance [1]	-208	-207	-155	-154	-152	-148	-136	-133	-132	-136
Overall fiscal balance (commitment basis)	-342	-440	-705	127	-317	-141	-218	-212	-42	-105
Net change in arrears, float, and stat. discrepancies (reduction = -)	135	-93	-85	-85	-86	-86	-86	-86	-86	-86
External arrears	11	-12	0	0	0	0	0	0	0	0
Domestic arrears	35	-82	-85	-85	-86	-86	-86	-86	-86	-86
Float and statistical discrepancies	89	1	0	0	0	0	0	0	0	0
Overall fiscal balance (cash basis)	-207	-533	-790	43	-403	-227	-304	-298	-128	-191
Financing	207	533	790	-42	403	227	304	298	128	192
Net external	199	576	478	34	353	229	286	283	109	172
Disbursements (projects)	236	742	659	215	434	256	355	352	217	252
Program financing (loans)	80	20	0	0	0	24	0	0	0	0
Scheduled amortization	-117	-187	-181	-181	-81	-51	-69	-69	-108	-79
Net domestic	7	-43	312	-76	49	-2	18	15	19	19
Net bank credit to the government	7	-43	-76	-76	49	-2	18	15	19	19
Banking system credit (excluding National Oil Account)	-37	-33	0	0	-2	-53	-24	-26	-14	-14
National Oil Account	44	-10	-76	-76	51	51	42	42	34	34
Nonbank financing	0	0	388	0	0	0	0	0	0	0
Of which: Privatisation	0	0	388	0	0	0	0	0	0	0
Financing gap	0	0	0	0	0	0	0	0	0	0
Memorandum items:										
National Oil Account balance (US$ million, excl. transfers to budget)	9.9	10.3	11.5	11.5	9.3	9.3	7.6	7.6	6.2	6.2

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

[1] Exclude oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlays.

Table 3. São Tomé and Príncipe: Financial Operations of the Central Government, 2014–19
(Percent of GDP)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Total revenue and grants	**25.2**	**28.0**	**35.1**	**31.1**	**33.4**	**30.1**	**33.7**	**30.3**	**33.5**	**32.5**
Total revenue	15.1	15.8	17.1	15.7	16.8	16.4	17.3	16.9	17.9	17.4
Tax revenue	13.7	14.3	14.9	13.5	15.4	15.0	15.9	15.5	16.5	16.1
Nontax revenue	1.5	1.5	2.2	2.3	1.3	1.4	1.3	1.4	1.3	1.4
Grants	10.0	11.5	17.3	14.7	16.6	13.7	16.4	13.5	15.6	15.1
Project grants	7.8	8.7	12.7	10.0	12.7	9.7	12.7	9.7	13.1	12.0
Nonproject grants	1.6	0.9	2.7	2.7	2.2	2.2	2.1	2.1	1.3	1.9
of which unconfirmed	…	…	0.0	0.0	0.4	0.4	0.5	0.5	0.5	0.5
HIPC Initiative-related grants	0.7	1.9	1.9	1.9	1.8	1.8	1.7	1.7	1.2	1.2
Total expenditure	**30.5**	**34.3**	**44.1**	**29.5**	**37.3**	**31.8**	**36.2**	**32.7**	**33.9**	**33.6**
Of which: Domestic primary expenditure	18.4	18.7	23.2	16.9	18.6	18.2	18.8	18.4	19.3	18.9
Current expenditure	18.0	18.1	17.4	16.1	17.1	17.2	16.7	16.7	16.7	16.8
Personnel costs	8.9	8.9	8.6	8.7	8.5	8.5	8.4	8.4	8.4	8.4
Interest due	0.7	0.8	0.7	0.7	0.7	0.8	0.7	0.7	0.7	0.7
Goods and services	3.5	3.4	3.1	3.0	3.1	3.1	3.1	3.1	3.1	3.1
Transfers	3.6	3.5	4.0	2.9	3.7	3.8	3.5	3.5	3.5	3.5
Other current expenditure	1.4	1.6	1.0	0.8	1.0	1.0	1.0	1.0	1.0	1.0
Capital expenditure	12.3	15.5	25.8	12.6	19.5	14.0	18.9	15.5	16.5	16.1
Financed by the Treasury	0.9	0.7	0.7	0.7	1.6	1.1	2.2	1.8	2.5	2.1
Financed by privatization proceeds	…	…	4.9	0.0	0	0.0	0	0.0	0.0	0.0
Financed by external sources	11.4	14.8	20.2	11.9	17.9	12.8	16.7	13.7	14.0	14.0
HIPC Initiative-related social expenditure	0.2	0.6	0.9	0.9	0.6	0.6	0.5	0.5	0.7	0.7
Domestic primary balance [1]	-3.2	-3.0	-2.0	-2.0	-1.8	-1.8	-1.5	-1.5	-1.4	-1.4
Overall fiscal balance (commitment basis)	-5.3	-6.3	-9.0	1.6	-3.8	-1.7	-2.5	-2.4	-0.4	-1.1
Net change in arrears, float, and stat. discrepancies (reduction = -)	2.1	-1.3	-1.1	-1.1	-1.0	-1.0	-1.0	-1.0	-0.9	-0.9
External arrears	0.2	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic arrears	0.6	-1.2	-1.1	-1.1	-1.0	-1.0	-1.0	-1.0	-0.9	-0.9
Float and statistical discrepancies	1.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-3.2**	**-7.6**	**-10.1**	**0.5**	**-4.9**	**-2.8**	**-3.4**	**-3.4**	**-1.3**	**-2.0**
Financing	**3.2**	**7.6**	**10.1**	**-0.5**	**4.9**	**2.8**	**3.4**	**3.4**	**1.3**	**2.0**
Net external	3.1	8.2	6.1	0.4	4.3	2.8	3.2	3.2	1.1	1.8
Disbursements (projects)	3.7	10.6	8.4	2.8	5.2	3.1	4.0	4.0	2.3	2.6
Program financing (loans)	1.2	0.3	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0
Scheduled amortization	-1.8	-2.7	-2.3	-2.3	-1.0	-0.6	-0.8	-0.8	-1.1	-0.8
Change in arrears (principal)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net domestic	0.1	-0.6	4.0	-1.0	0.6	0.0	0.2	0.2	0.2	0.2
Net bank credit to the government	0.1	-0.6	-1.0	-1.0	0.6	0.0	0.2	0.2	0.2	0.2
Banking system credit (excluding National Oil Account)	-0.6	-0.5	0.0	0.0	0.0	-0.6	-0.3	-0.3	-0.1	-0.1
National Oil Account	0.7	-0.1	-1.0	-1.0	0.6	0.6	0.5	0.5	0.4	0.4
Nonbank financing	0.0	0.0	5.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: Privatisation	0.0	0.0	5.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
National Oil Account balance (US$ million, excl. transfers to budget)	9.9	10.3	11.5	11.5	9.3	9.3	7.6	7.6	6.2	6.2
Nominal GDP (Billions of dobras)	6,435	7,018	7,847	7,774	8,287	8,248	8,839	8,839	9,533	9,533

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

[1] Exclude oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlays.

Table 4. São Tomé and Príncipe: Summary Accounts of the Central Bank, 2014–19
(Billions of dobra)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Net foreign assets	**1,474**	**1,903**	**2,180**	**1,868**	**2,200**	**1,937**	**2,316**	**2,022**	**2,437**	**2,179**
Claims on nonresidents	1,795	2,243	2,561	2,243	2,595	2,331	2,740	2,446	2,847	2,590
Official foreign reserves	1,482	1,864	2,182	1,870	2,218	1,954	2,363	2,069	2,472	2,215
Other foreign assets	313	379	379	373	378	378	377	377	375	375
Liabilities to nonresidents	-321	-341	-381	-375	-395	-395	-424	-424	-411	-411
Short-term liabilities to nonresidents	-114	-120	-161	-158	-175	-175	-205	-205	-193	-193
Other foreign liabilities	-207	-221	-220	-217	-220	-220	-219	-219	-218	-218
Net domestic assets	**-338**	**-341**	**-455**	**-146**	**-367**	**-97**	**-346**	**-46**	**-281**	**-53**
Net domestic credit	117	110	86	88	136	86	154	102	175	122
Claims on other depository corporations	106	128	128	128	128	128	128	128	128	128
Net claims on central government	-84	-133	-160	-159	-113	-165	-98	-152	-80	-135
Claims on central government	255	247	247	243	246	246	246	245	246	244
Of which: use of SDRs/PRGF	*207*	*196*	*196*	*193*	*195*	*195*	*195*	*195*	*194*	*194*
Liabilities to central government	-339	-380	-407	-403	-360	-411	-344	-398	-326	-379
Ordinary deposits of central government	-18	-11	-11	-11	-13	-64	-37	-90	-51	-104
Counterpart funds	-93	-120	-120	-120	-120	-120	-120	-120	-120	-120
Foreign currency deposits	-228	-249	-276	-272	-227	-227	-188	-188	-155	-155
Of which: National oil account	*-200*	*-230*	*-257*	*-253*	*-208*	*-205*	*-169*	*-166*	*-136*	*-134*
Claims on other sectors	95	115	118	119	121	123	124	126	126	128
Other items (net) [1]	-455	-451	-541	-234	-503	-183	-500	-148	-456	-175
Base money	**1,136**	**1,562**	**1,725**	**1,722**	**1,833**	**1,839**	**1,966**	**1,971**	**2,155**	**2,126**
Currency issued	267	315	348	348	370	371	397	398	435	429
Bank reserves	869	1,247	1,376	1,375	1,463	1,468	1,569	1,573	1,720	1,697
Of which: domestic currency	704	980	1,083	1,081	1,151	1,156	1,234	1,237	1,353	1,335
Of which: foreign currency	165	266	294	294	312	312	335	336	367	362
Memorandum items:										
Gross international reserves (US$ millions) [2]	56.5	61.9	72.8	58.7	75.9	63.9	82.4	68.9	87.6	75.9
Months of imports of goods and nonfactor services [3]	4.3	4.9	5.0	4.2	5.0	4.3	5.1	4.3	5.0	4.5
Net international reserves (US$ millions) [4]	50.8	56.5	65.6	51.5	68.0	55.9	73.2	59.5	78.9	67.1
Months of imports of goods and nonfactor services [3]	3.9	4.4	4.5	3.7	4.5	3.8	4.5	3.8	4.5	3.9
National Oil Account (US$ millions)	9.9	10.3	11.5	11.5	9.3	9.3	7.6	7.6	6.2	6.2
Commercial banks reserves in foreign currency (US$ millions)	8.2	11.9	13.1	13.3	14.0	14.2	15.0	15.3	16.6	16.7
Guaranteed deposits (US$ millions)	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Base money (annual percent change)	23.2	37.5	10.4	10.3	6.3	6.8	7.2	7.2	9.7	7.9

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

[1] Shares and other equity, and unclassified assets changed relative to previous projections to account for actual outturn to July 2016 and revised assumptions.

[2] Gross international reserves exclude the National Oil Account and foreign currency deposits of commercial banks used as application deposits for new licensing or for meeting capital requirements.

[3] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

[4] Net international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements and foreign currency deposits of commercial banks used as application deposits for new licensing or for meeting capital requirements.

Table 5. São Tomé and Príncipe: Monetary Survey, 2014–19
(Billions of dobra)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Net foreign assets	**2,230**	**2,527**	**2,836**	**2,526**	**2,885**	**2,632**	**3,020**	**2,737**	**3,142**	**2,896**
Net foreign assets of the BCSTP	1,474	1,903	2,180	1,868	2,200	1,937	2,316	2,022	2,437	2,179
Net foreign assets of other depository corporations	756	624	656	658	685	696	704	715	706	717
Net domestic assets	**270**	**301**	**320**	**624**	**470**	**732**	**577**	**868**	**737**	**992**
Net domestic credit	1,630	1,630	1,740	1,742	1,887	1,837	2,208	1,965	2,398	2,155
Net claims on central government	-252	-323	-350	-349	-304	-355	-98	-342	-80	-325
Claims on central government	258	255	255	252	255	254	246	254	246	253
Liabilities to central government	-510	-578	-606	-601	-559	-610	-344	-596	-326	-578
Budgetary deposits	-18	-11	-11	-11	-13	-64	-37	-90	-51	-104
Counterpart funds	-93	-120	-120	-120	-120	-120	-120	-120	-120	-120
Foreign currency deposits	-399	-448	-475	-471	-426	-426	-188	-386	-155	-354
Of which: National Oil Account	-200	-230	-257	-253	-208	-205	-169	-166	-136	-134
Claims on other sectors	1,882	1,953	2,091	2,092	2,191	2,193	2,306	2,308	2,478	2,480
Of which: claims in foreign currency	766	608	1,006	690	931	931	982	982	1,058	1,058
(Millions of $US)	38	27	45	31	42	42	44	45	48	49
Other items (net) [1]	-1,360	-1,329	-1,420	-1,118	-1,417	-1,106	-1,631	-1,097	-1,661	-1,163
Broad money (M3)	**2,500**	**2,828**	**3,156**	**3,150**	**3,355**	**3,364**	**3,597**	**3,605**	**3,880**	**3,888**
Local currency liabilities included in broad money (M2)	1,563	1,894	1,988	2,090	2,114	2,239	2,266	2,399	2,444	2,588
Money (M1)	1,106	1,431	1,502	1,579	1,597	1,691	1,712	1,812	1,846	1,955
Currency outside depository corporations	222	247	259	272	260	275	270	286	245	259
Transferable deposits in dobra	884	1,184	1,243	1,306	1,337	1,416	1,442	1,527	1,602	1,696
Other deposits in dobra	456	463	486	511	517	548	554	587	598	633
Foreign currency deposits	937	934	1,168	1,060	1,241	1,125	1,331	1,206	1,436	1,300
Memorandum items:										
Velocity (ratio of GDP to M3; end of period)	2.7	2.6	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Money multiplier (M3/M0)	2.2	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Base money (12-month growth rate)	23.2	37.5	10.4	10.3	6.3	6.8	7.2	7.2	9.7	7.9
Claims on other resident sectors (12-month growth rate)	-1.0	3.8	7.0	7.1	4.8	4.8	5.2	5.2	7.5	7.5
M3 (12-month growth rate)	16.8	13.1	11.6	11.4	6.3	6.8	7.2	7.2	7.9	7.9
Dollarization ratio	39.4	35.9	n.a.	36.8	n.a.	36.4	n.a.	36.3	n.a.	35.8

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

[1] Shares and other equity, and unclassified assets changed relative to previous projections to account for actual outturn to July 2016 and revised assumptions.

Table 6. São Tomé and Príncipe: Financial Soundness Indicators, 2011–June 2016

	2011 December	2012 December	2013 December	2014 December	2015 December	2016 March	2016 June	2016 June[1]
Capital Adequacy								
Regulatory capital to risk-weighted assets	27.7	20.3	22.7	22.6	24.1	24.0	23.9	26.5
Percentage of banks greater or equal to 10 percent	100.0	87.5	75.0	75.0	85.7	85.7	85.7	100.0
Percentage of banks between 6 and 10 percent	0.0	0.0	12.5	0.0	0.0	0.0	0.0	0.0
Percentage of banks below 6 percent minimum	0.0	12.5	12.5	25.0	14.3	14.3	14.3	0.0
Capital (net worth) to assets	26.5	22.7	18.4	20.3	15.5	13.9	12.9	21.1
Deposits with banks below 6 percent (in billions of dobras)	0.0	83.2	59.0	325.1	455.3	436.8	435.2	0.0
Deposits with banks below 6 percent (percent of deposits)	0.0	4.6	2.9	13.7	17.5	17.7	17.9	0.0
Deposits with banks below 6 percent (percent of GDP)	0.0	1.7	1.1	5.1	6.5	5.6	5.6	0.0
Asset quality								
Foreign exchange loans to total loans	68.5	57.9	53.9	46.5	42.1	44.2	39.3	33.4
Past-due loans to gross loans	33.2	66.7	30.4	36.2	35.0	38.0	44.8	38.5
Nonperforming loans/credit (IFRS definition)	15.6	15.4	16.9	19.1	29.8	32.7	35.9	28.0
Watch-listed loans	17.5	51.3	13.6	17.2	5.2	5.3	8.9	10.4
Provision as percent of past-due loans	30.0	15.4	56.3	45.1	68.7	75.5	69.0	57.5
Earnings and profitability								
Return on assets	0.5	-0.8	-2.1	-3.2	-5.2	-1.8	-2.3	-0.1
Return on equity	1.5	-3.3	-9.3	-15.9	-27.1	-9.5	-12.1	-0.6
Expense (w/ amortization & provisions)/income	119.3	117.8	471.1	164.5	215.9	244.2	189.1	109.5
Liquidity								
Liquid assets/total assets	20.4	37.8	40.8	45.8	52.0	48.5	49.2	52.2
Liquid assets/short term liabilities	36.7	61.5	39.6	72.7	72.5	68.4	67.1	79.6
Loan/total liabilities	83.0	64.7	56.3	47.3	47.1	47.7	47.5	44.9
Foreign exchange liabilities/total liabilities	35.0	30.8	27.0	28.1	30.0	29.5	29.0	23.9
Loan/deposits	119.5	101.7	85.8	69.6	63.5	65.1	64.4	60.9
Sensitivity to market risk								
Foreign exchange liabilities to shareholders funds	97.0	105.0	119.3	110.3	162.8	183.2	196.1	107.3

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates.

Note: Beginning June 2013, data are based on improved methodology and not strictly comparable with earlier data.

[1] Excluding Banco Equador.

Table 7. São Tomé and Príncipe: Balance of Payments, 2014–19
(Millions of U.S. dollars)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Trade balance	**-127.4**	**-107.6**	**-113.3**	**-98.1**	**-122.1**	**-113.1**	**-133.8**	**-123.7**	**-134.4**	**-141.2**
Exports, f.o.b.	17.2	11.3	16.0	14.2	18.0	16.1	19.3	16.9	21.8	17.8
Cocoa	9.1	7.9	11.4	11.0	12.1	12.0	13.3	13.0	13.8	13.5
Re-export	7.0	2.2	3.4	2.0	4.0	2.9	4.3	2.6	5.1	2.9
Imports, f.o.b.	-144.6	-118.9	-129.2	-112.3	-140.0	-129.2	-153.1	-140.6	-156.2	-159.0
Of which : food	-42.5	-34.3	-34.3	-32.2	-35.9	-34.0	-37.7	-35.5	-39.7	-37.4
Petroleum products	-41.1	-31.3	-23.8	-22.1	-29.7	-26.1	-34.0	-28.1	-38.3	-29.9
Investment goods	-30.3	-27.9	-41.3	-30.0	-47.3	-40.7	-52.6	-48.0	-49.2	-64.0
Oil sector related investment goods	0.0	0.0	-2.1	-2.1	-2.1	-2.1	-2.1	-2.1	0.0	0.0
Services and income (net)	**-8.0**	**9.6**	**-10.0**	**1.0**	**-9.7**	**3.6**	**-5.1**	**3.9**	**-3.2**	**1.2**
Exports of nonfactor services	71.2	78.6	71.8	82.1	76.1	90.4	80.9	96.7	86.7	101.1
Of which : travel and tourism	56.0	62.2	54.7	70.0	58.2	77.7	62.0	83.3	66.7	86.9
Imports of nonfactor services	-84.9	-68.0	-82.8	-79.7	-87.0	-85.7	-87.2	-91.7	-91.1	-98.7
Factor services (net)	5.7	-1.0	1.0	-1.4	1.1	-1.2	1.1	-1.2	1.2	-1.1
Of which: oil related	0.0	0.0	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Private transfers (net)	**23.3**	**18.1**	**20.3**	**14.1**	**21.4**	**15.0**	**22.8**	**16.0**	**24.6**	**17.3**
Official transfers (net)	**36.0**	**38.8**	**60.3**	**51.6**	**63.1**	**52.4**	**66.2**	**55.2**	**67.9**	**66.0**
Of which : project grants	27.9	32.4	50.9	42.0	53.7	43.2	56.9	45.9	61.4	59.3
HIPC Initiative-related grants	0.8	4.8	6.6	6.7	6.7	6.8	6.7	6.8	5.2	6.8
Current account balance										
Including official transfers	-76.1	-41.1	-42.7	-31.4	-47.3	-42.2	-49.9	-48.6	-45.1	-56.7
Excluding official transfers	-112.1	-79.9	-103.0	-82.9	-110.4	-94.5	-116.1	-103.8	-113.1	-122.7
Capital and financial account balance	**37.4**	**53.8**	**55.9**	**30.4**	**47.9**	**45.0**	**55.3**	**52.7**	**50.9**	**64.2**
Financial account	37.4	53.8	55.9	30.4	47.9	45.0	55.3	52.7	50.9	64.2
Direct foreign investment	18.9	26.4	4.2	23.4	9.9	17.5	15.9	24.0	24.1	28.1
Of which: Oil signature bonuses	0.0	2.4	2.5	2.5	0.0	0.0	0.0	0.0	0.0	0.0
Petroleum related investment	11.1	24.8	3.2	15.0	3.2	3.2	3.2	3.2	0.0	0.0
Recovery of oil capital expense	-11.1	-24.8	-3.2	-15.0	-3.2	-3.2	-3.2	-3.2	0.0	0.0
Portfolio Investment (net)	-0.1	1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	18.6	26.0	51.7	7.1	38.0	27.5	39.4	28.7	26.8	36.1
Assets	15.5	16.7	5.8	-12.0	5.9	0.0	5.9	0.0	6.0	0.0
Public sector (net)	15.6	32.9	26.8	10.1	16.9	8.2	13.1	11.2	5.3	8.4
Project loans	13.1	34.7	29.3	14.7	19.5	11.6	15.9	16.0	9.8	11.5
Program loans	4.3	0.0	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0
Amortization	-0.7	-1.6	-1.3	-3.3	-1.4	-3.3	-1.6	-3.6	-4.8	-3.6
Other investment	-1.1	-0.1	-1.1	-1.2	-1.2	-1.1	-1.3	-1.2	0.4	0.5
Of which : transfers to JDA	-0.3	-0.2	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Private sector (net)	-12.5	-23.7	19.0	8.9	15.3	19.3	20.4	17.5	15.5	27.7
Commercial banks	-17.5	-9.7	1.5	2.0	1.4	1.8	0.9	0.5	0.3	0.3
Short-term private capital	5.0	-14.0	17.6	6.9	13.9	17.4	19.4	17.0	15.2	27.4
Errors and omissions	**48.2**	**5.8**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**9.5**	**18.5**	**13.2**	**-0.9**	**0.6**	**2.9**	**5.4**	**4.2**	**5.7**	**7.5**
Financing	-9.5	-18.5	-13.2	0.9	-0.6	-2.8	-5.4	-4.2	-5.7	-7.5
Change in official reserves, excl. NOA (increase= -)	-10.5	-18.2	-13.0	1.1	-3.9	-6.1	-8.4	-7.2	-6.7	-8.4
Use of Fund resources (net)	-1.4	0.0	1.0	1.0	1.1	1.1	1.2	1.2	-0.5	-0.5
Purchases	0.0	0.9	1.8	1.8	1.8	1.8	1.8	1.8	0.0	0.0
Repurchases (incl. MDRI repayment)	-1.4	-0.9	-0.7	-0.7	-0.6	-0.6	-0.5	-0.5	-0.5	-0.5
National Oil Account (increase = -)	2.3	-0.4	-1.2	-1.2	2.2	2.2	1.8	1.8	1.4	1.4
Financing Gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Current account balance (percent of GDP)										
Before official transfers	-32.2	-25.2	-29.5	-23.6	-29.7	-25.2	-29.3	-25.8	-26.4	-28.1
After official transfers	-21.8	-12.9	-12.2	-8.9	-12.7	-11.3	-12.6	-12.1	-10.5	-13.0
Debt service ratio (percent of exports) [1]	3.7	3.8	4.7	6.8	4.3	6.0	3.9	5.6	3.7	5.4
Gross international reserves [2]										
Millions of U.S. dollars	56.5	61.9	72.8	58.7	75.9	63.9	82.4	68.9	87.6	75.9
Months of imports of goods and nonfactor services [3]	4.3	4.9	5.0	4.2	5.0	4.3	5.1	4.3	5.1	4.5

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

[1] Percent of exports of goods and nonfactor services.

[2] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements and foreign currency deposits of commercial banks used application deposits for new licensing or for meeting capital requirements.

[3] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

Table 8. São Tomé and Príncipe: Balance of Payments, 2014–19
(Percent of GDP)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Trade balance	**-36.6**	**-33.9**	**-32.4**	**-27.9**	**-32.9**	**-30.2**	**-33.8**	**-30.7**	**-31.4**	**-32.3**
Exports, f.o.b.	4.9	3.6	4.6	4.1	4.8	4.3	4.9	4.2	5.1	4.1
Cocoa	2.6	2.5	3.3	3.1	3.3	3.2	3.4	3.2	3.2	3.1
Re-export	2.0	0.7	1.0	0.6	1.1	0.8	1.1	0.6	1.2	0.7
Imports, f.o.b.	-41.5	-37.4	-37.0	-32.0	-37.7	-34.5	-38.7	-34.9	-36.4	-36.4
Of which : food	-12.2	-10.8	-9.8	-9.2	-9.7	-9.1	-9.5	-8.8	-9.3	-8.6
Petroleum products	-11.8	-9.8	-6.8	-6.3	-8.0	-7.0	-8.6	-7.0	-8.9	-6.8
Investment goods	-8.7	-8.8	-11.8	-8.5	-12.7	-10.9	-13.3	-11.9	-11.5	-14.7
Oil sector related investment goods	0.0	0.0	-0.6	-0.6	-0.6	-0.6	-0.5	-0.5	0.0	0.0
Services and income (net)	**-2.3**	**3.0**	**-2.9**	**0.3**	**-2.6**	**1.0**	**-1.3**	**1.0**	**-0.8**	**0.3**
Exports of nonfactor services	20.4	24.7	20.5	23.4	20.5	24.1	20.4	24.0	20.2	23.1
Of which : travel and tourism	16.1	19.6	15.7	19.9	15.7	20.7	15.7	20.7	15.6	19.9
Imports of nonfactor services	-24.4	-21.4	-23.7	-22.7	-23.4	-22.9	-22.0	-22.8	-21.2	-22.6
Factor services (net)	1.6	-0.3	0.3	-0.4	0.3	-0.3	0.3	-0.3	0.3	-0.3
Of which: oil related	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private transfers (net)	**6.7**	**5.7**	**5.8**	**4.0**	**5.8**	**4.0**	**5.8**	**4.0**	**5.7**	**4.0**
Official transfers (net)	**10.3**	**12.2**	**17.3**	**14.7**	**17.0**	**14.0**	**16.7**	**13.7**	**15.8**	**15.1**
Of which : project grants	8.0	10.2	14.6	12.0	14.5	11.5	14.4	11.4	14.3	13.6
HIPC Initiative-related grants	0.2	1.5	1.9	1.9	1.8	1.8	1.7	1.7	1.2	1.6
Current account balance										
Including official transfers	-21.8	-12.9	-12.2	-8.9	-12.7	-11.3	-12.6	-12.1	-10.5	-13.0
Excluding official transfers	-32.2	-25.2	-29.5	-23.6	-29.7	-25.2	-29.3	-25.8	-26.4	-28.1
Capital and financial account balance	**10.7**	**16.9**	**16.0**	**8.7**	**12.9**	**12.0**	**14.0**	**13.1**	**11.9**	**14.7**
Financial account	10.7	16.9	16.0	8.7	12.9	12.0	14.0	13.1	11.9	14.7
Direct foreign investment	5.4	8.3	1.2	6.6	2.7	4.7	4.0	6.0	5.6	6.4
Of which: Oil signature bonuses	0.0	0.8	0.7	0.7	0.0	0.0	0.0	0.0	0.0	0.0
Petroleum related investment	3.2	7.8	0.9	4.3	0.9	0.9	0.8	0.8	0.0	0.0
Recovery of oil capital expense	-3.2	-7.8	-0.9	-4.3	-0.9	-0.9	-0.8	-0.8	0.0	0.0
Portfolio Investment (net)	0.0	0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	5.3	8.2	14.8	2.0	10.2	7.3	9.9	7.1	6.3	8.3
Assets	4.4	5.3	1.7	-3.4	1.6	0.0	1.5	0.0	1.4	0.0
Public sector (net)	4.5	10.4	7.7	2.9	4.5	2.2	3.3	2.8	1.2	1.9
Project loans	3.8	10.9	8.4	4.2	5.2	3.1	4.0	4.0	2.3	2.6
Program loans	1.2	0.0	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0
Amortization	-0.2	-0.5	-0.4	-0.9	-0.4	-0.9	-0.4	-0.9	-1.1	-0.8
Other investment	-0.3	0.0	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	0.1	0.1
Of which : transfers to JDA	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Private sector (net)	-3.6	-7.5	5.5	2.5	4.1	5.1	5.1	4.3	3.6	6.3
Commercial banks	-5.0	-3.1	0.4	0.6	0.4	0.5	0.2	0.1	0.1	0.1
Short-term private capital	1.4	-4.4	5.0	2.0	3.7	4.7	4.9	4.2	3.6	6.3
Errors and omissions	**13.8**	**1.8**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**2.7**	**5.8**	**3.8**	**-0.3**	**0.2**	**0.8**	**1.4**	**1.0**	**1.3**	**1.7**
Financing	-2.7	-5.8	-3.8	0.3	-0.2	-0.8	-1.4	-1.0	-1.3	-1.7
Change in official reserves, excl. NOA (increase= -)	-3.0	-5.7	-3.7	0.3	-1.0	-1.6	-2.1	-1.8	-1.6	-1.9
Use of Fund resources (net)	-0.4	0.0	0.3	0.3	0.3	0.3	0.3	0.3	-0.1	-0.1
Purchases	0.0	0.3	0.5	0.5	0.5	0.5	0.4	0.4	0.0	0.0
Repurchases (incl. MDRI repayment)	-0.4	-0.3	-0.2	-0.2	-0.2	-0.2	-0.1	-0.1	-0.1	-0.1
National Oil Account (increase = -)	0.7	-0.1	-0.4	-0.3	0.6	0.6	0.4	0.4	0.3	0.3
Financing Gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Debt service ratio (percent of exports) [1]	3.7	3.8	4.7	6.8	4.3	6.0	3.9	5.6	3.7	5.4
Gross international reserves [2]										
Millions of U.S. dollars	56.5	61.9	72.8	58.7	75.9	63.9	82.4	68.9	87.6	75.9
Months of imports of goods and nonfactor services [3]	4.3	4.9	5.0	4.2	5.0	4.3	5.1	4.3	5.1	4.5

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

[1] Percent of exports of goods and nonfactor services.

[2] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements and foreign currency deposits of commercial banks used application deposits for new licensing or for meeting capital requirements.

[3] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

Table 9. São Tomé and Príncipe: External Financing Requirements and Sources, 2014–19
(Millions of U.S. dollars)

	2014	2015	2016		2017		2018		2019	
			EBS/16/47		EBS/16/47		EBS/16/47		EBS/16/47	
	Actual	Est.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.	1st Rev	Proj.
Gross financing requirements	**-125.8**	**-100.7**	**-119.2**	**-87.1**	**-117.5**	**-105.8**	**-127.9**	**-116.3**	**-124.7**	**-134.7**
Current account, excluding official transfers	-112.1	-79.9	-103.0	-82.9	-110.4	-94.5	-116.1	-103.8	-113.1	-122.7
Exports, f.o.b.	17.2	11.3	16.0	14.2	18.0	16.1	19.3	16.9	21.8	17.8
Imports, f.o.b.	-144.6	-118.9	-129.2	-112.3	-140.0	-129.2	-153.1	-140.6	-156.2	-159.0
Services and income (net)	-8.0	9.6	-10.0	1.0	-9.7	3.6	-5.1	3.9	-3.2	1.2
Private transfers	23.3	18.1	20.3	14.1	21.4	15.0	22.8	16.0	24.6	17.3
Financial account	-3.2	-2.6	-3.2	-5.3	-3.2	-5.1	-3.4	-5.3	-4.9	-3.6
Scheduled amortization	-0.7	-1.6	-1.3	-3.3	-1.4	-3.3	-1.6	-3.6	-4.8	-3.6
IMF repayments	-1.4	-0.9	-0.7	-0.7	-0.6	-0.6	-0.5	-0.5	-0.5	-0.5
Other public sector flows (net)	-1.1	-0.1	-1.1	-1.2	-1.2	-1.1	-1.3	-1.2	0.4	0.5
Change in external reserves (-ve = increase)	-10.5	-18.2	-13.0	1.1	-3.9	-6.1	-8.4	-7.2	-6.7	-8.4
Available funding	**125.8**	**100.7**	**119.2**	**87.0**	**117.5**	**105.8**	**127.9**	**116.2**	**124.7**	**134.7**
National Oil Fund (net)	2.3	2.0	1.3	1.3	2.2	2.2	1.8	1.8	1.4	1.4
Oil signature bonuses	0.0	2.4	2.5	2.5	0.0	0.0	0.0	0.0	0.0	0.0
Saving (-ve = accumulation of oil reserve fund)	2.3	-0.4	-1.2	-1.2	2.2	2.2	1.8	1.8	1.4	1.4
Expected disbursements	53.4	73.4	89.6	66.3	82.6	65.1	82.2	71.2	77.7	77.5
Multilateral HIPC interim assistance	0.8	4.8	6.6	6.7	6.7	6.8	6.7	6.8	5.2	6.8
Grants [1]	35.2	34.0	53.7	44.9	56.5	45.6	59.6	48.4	62.7	59.1
Concessional loans	17.4	34.7	29.3	14.7	19.5	12.7	15.9	16.0	9.8	11.5
Project loans	13.1	34.7	29.3	14.7	19.5	11.6	15.9	16.0	9.8	11.5
Program loans	4.3	0.0	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0
Private sector (net)	70.0	24.3	26.6	17.7	31.0	36.8	42.2	41.5	45.6	55.8
IMF	0.0	0.9	1.8	1.8	1.8	1.8	1.8	1.8	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Residual financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

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

[1] Includes revenue from Nigeria oil program.

Table 10. São Tomé and Príncipe: Proposed Schedule of Disbursements Under the ECF Arrangement, 2015–18

Date[1]	Disbursement conditions	SDR Amount	Percent of Quota
07/13/15	Board approval of arrangement.	634,285	4.29
04/15/16	Observance of continuous and end-December 2015 PCs and completion of the first review.	634,285	4.29
10/15/16	Observance of continuous and end-June 2016 PCs and completion of the second review.	634,285	4.29
04/15/17	Observance of continuous and end-December 2016 PCs and completion of the third review.	634,285	4.29
10/15/17	Observance of continuous and end-June 2017 PCs and completion of the fourth review.	634,285	4.29
04/15/18	Observance of continuous and end-December 2017 PCs and completion of the fifth review	634,285	4.29
06/15/18	Observance of continuous and end-March 2018 PCs and completion of the sixth review.	634,290	4.29
	Total	4,440,000	30

Source: International Monetary Fund.

Table 11. São Tomé and Príncipe: Indicators of Capacity to Repay the Fund, 2016–28

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
Fund obligations based on existing credit (millions of SDRs)													
Principal	0.12	0.44	0.39	0.33	0.26	0.41	0.48	0.36	0.25	0.25	0.06	0.00	0.00
Charges and interest	0.00	0.00	0.00	0.01	0.01	0.01	0.01	0.01	0.00	0.00	0.00	0.00	0.00
Fund obligations based on existing and prospective credit (millions of SDRs)													
Principal	0.12	0.44	0.39	0.33	0.26	0.41	0.67	0.87	0.89	0.89	0.70	0.44	0.13
Charges and interest	0.00	0.00	0.00	0.02	0.02	0.02	0.01	0.01	0.01	0.01	0.01	0.00	0.00
Total obligations based on existing and prospective credit													
Millions of SDRs	0.12	0.44	0.39	0.35	0.28	0.43	0.68	0.88	0.90	0.90	0.71	0.44	0.13
Millions of U.S. dollars	0.17	0.62	0.55	0.49	0.40	0.61	0.96	1.25	1.27	1.27	1.00	0.62	0.00
Percent of exports of goods and services	0.17	0.58	0.48	0.42	0.31	0.45	0.65	0.78	0.75	0.70	0.51	0.30	0.00
Percent of debt service [1]	2.57	9.63	8.66	7.66	3.92	5.61	8.81	10.96	9.91	9.78	7.96	4.97	0.00
Percent of quota	1.62	5.95	5.27	4.73	3.78	5.81	9.19	11.89	12.16	12.16	9.59	5.95	1.76
Percent of gross international reserves [2]	0.23	0.79	0.65	0.53	0.37	0.54	0.83	1.03	0.99	0.95	0.71	0.42	0.00
Outstanding Fund credit													
Millions of SDRs	3.9	4.7	5.6	5.3	5.0	4.6	3.9	3.0	2.2	1.3	0.6	0.1	0.0
Millions of U.S. dollars	5.4	6.6	7.9	7.4	7.1	6.5	5.5	4.3	3.1	1.8	0.8	0.2	0.0
Percent of exports of goods and services	5.6	6.2	6.9	6.2	5.6	4.8	3.7	2.7	1.8	1.0	0.4	0.1	0.0
Percent of debt service [1]	83.0	102.9	124.1	114.9	70.0	59.8	50.8	37.9	23.8	13.8	6.4	1.5	0.0
Percent of quota	52.4	63.5	75.5	70.9	67.6	61.9	53.0	41.1	29.2	17.2	7.7	1.8	0.0
Percent of gross international reserves [2]	7.5	8.4	9.3	8.0	6.5	5.8	4.8	3.5	2.4	1.3	0.6	0.1	0.0
Memorandum items:													
Exports of goods and services (millions of U.S. dollars)	96.4	106.6	113.6	118.9	127.1	135.8	148.6	159.0	170.3	182.3	195.2	209.0	223.8
Debt service (millions of U.S. dollars)	6.5	6.4	6.3	6.5	10.1	10.8	10.9	11.4	12.9	13.0	12.6	12.5	9.1
Quota (millions of SDRs)	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4	7.4
Gross international reserves [2]	72.0	78.1	84.2	92.6	108.4	111.7	116.3	121.4	128.3	134.3	140.6	147.6	155.1
GDP (millions of U.S. dollars)	352	375	403	437	478	507	546	585	628	674	722	775	831

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

[1] After HIPC and MDRI debt relief. Including IMF repurchases and repayments in total debt service.

[2] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements and foreign currency deposits of commercial banks used application deposits for new licensing or for meeting capital requirements.

Table 12. São Tomé and Príncipe: Millennium Development Goals

	1990	1995	2000	2005	2010	2015	Status
Goal 1: Eradicate extreme poverty and hunger							Not Met
Population below $1 (PPP) per day, percentage	--	--	28.2[5/]	--	--	--	
Population below national poverty line, total, percentage	--	--	53.8[5/]	--	66.2[11/]	--	
Poverty gap ratio at $1 a day (PPP), percentage	--	--	7.9[5/]	--	--	--	
Poorest quintile's share in national income or consumption, percentage	--	--	5.2[5/]	--	--	--	
Employment to population ratio, both sexes, percentage	42.9[1/]	--	40.6	--	--	--	
Proportion of own-account and contributing family workers in total employment, both sexes, percentage	0.8[1/]	--	--	--	--	--	
Children under 5 moderately or serverely underweight, percentage	--	--	10.1	8.0[8/]	14.4[11/]	8.8[13/]	
Population undernourished, percentage	22.6[1/]	24	14.8	8.9	7.5	7.0[13/]	
Goal 2: Achieve universal primary education							Met
Total net enrollment ratio in primary education, both sexes	--	--	89.5[4/]	99.3	98.6	99.1	
Percentage of pupils starting grade 1 who reach last grade of primary, both sexes	--	--	58.8[5/]	68.9[7/]	68.0[10/]	98.0	
Literacy rates of 15-24 years old, both sexes, percentage	93.8[1/]	--	95.4[5/]	--	95.3	90.0	
Goal 3: Promote gender equality and empower women							Not Met
Gender Parity Index in primary level enrollment	--	--	0.97[4/]	0.97	1.00	1.00[13/]	
Gender Parity Index in secondary level enrollment	--	--	--	1.07	1.03	1.11[13/]	
Gender Parity Index in tertiary enrolment	--	--	--	--	0.98	--	
Share of women in wage enployment in the non-agricultural sector	32[1/]	--	--	--	--	--	
Seats held by women in national parliament, percentage	11.8	7.3[3/]	9.1	9.1	7.3	20.0	
Goal 4: Reduce child mortality							Met
Children under five mortality rate, per 1,000 live births	96.0	94.1	92.5	90.8	89.1	45.0[13/]	
Infant mortality rate (0-1 year) per 1,000 live births	62.2	61.2	60.3	59.3	58.3	38.0[13/]	
Children 1 year old immunized against measles, percentage	71.0	74.0	69.0	88.0	92.0	89.0[13/]	
Goal 5: Improve maternal health							Met
Maternal mortality ratio per 100,000 live births	150	120	110	87	70	76[13/]	
Births attended by skilled health personnel, percentage	--	--	79	81[8/]	82[10/]	92.5[13/]	
Current contraceptive use among married women 15–49 years old, any method, percentage	--	--	29	31[8/]	38[11/]	40.6[13/]	
Adolescent birth rate, per 1,000 women	107[1/]	--	91[5/]	110[8/]	--	92[13/]	
Antenatal care coverage, at least one visit, percentage	--	--	91	97[8/]	98[11/]	97.5[13/]	
Antenatal care coverage, at least four visits, percentage	--	--	--	--	72[11/]	--	
Unmet need for family planning, total, percentage	--	--	--	--	38[11/]	32.7[13/]	
Goal 6: Combat HIV/AIDS, Malaria and other diseases							Met
Condom use at last high-risk sex, 15–24 years old, women, percentage	--	--	--	56[8/]	54[11/]	65.2[13/]	
Condom use at last high-risk sex, 15–24 years old, men, percentage	--	--	--	--	64[11/]	82.5[13/]	
Men 15–24 years old with comprehensive correct knowledge of HIV/AIDS, percentage	--	--	--	--	43[11/]	42.2[13/]	
Women 15–24 years old with comprehensive correct knowledge of HIV/AIDS, percentage	--	--	11	44[8/]	43[11/]	--	
Notified cases of malaria per 100,000 population	--	--	--	--	2[11/]	0	
Malaria death rate per 100,000 population, all ages	--	--	--	--	8[11/]	0	
Malaria death rate per 100,000 population, ages 0–4	--	--	--	--	3[11/]	0	
Children under 5 sleeping under insecticide-treated bed nets, percentage	--	--	23	42[8/]	56[11/]	61.1[13/]	
Children under 5 with fever being treated with anti-malarial drugs, percentage	--	--	61	25[8/]	8[11/]	1.4[13/]	
Tuberculosis prevalence rate per 100,000 population (mid-point)	258	253	189	134	141	--	
Tuberculosis death rate per year per 100,000 population (mid-point)	28	29	18	10	13	--	
Tuberculosis incidence rate per year per 100,000 population (mid-point)	135	124	114	105	96	--	
Tuberculosis detection rate under DOTS, percentage (mid-point)	11	--	60	85	76	--	
Tuberculosis treatment success rate under DOTS, percentage	--	--	78	98	98[11/]	--	
Goal 7: Ensure environmental sustainability							Likely Met
Proportion of land area covered by forest, percentage	28	--	28	28	28	28	
Carbon dioxide emmisions (CO_2), thousand metric tons of CO_2 (CDIAC)	66	77	88	128	128[11/]	--	
Carbon dioxide emmisions (CO_2), metric tons of CO_2 per capita (CDIAC)	0.57	0.60	0.62	0.84	0.79[11/]	--	
Carbon dioxide emmisions (CO_2), kg CO_2 per $1 GDP (PPP) (CDIAC)	--	--	0.51	0.50	0.63[11/]	--	
Consumption of all Ozone-Depleting Substances in ODP metric tons	2.5	4.8	4.0	2.3	0.2	--	
Proportion of total water resources used, percentage	--	0.3	--	--	--	--	
Terrestrial and marine areas protected to total territorial area, percentage	0.0	0.0	0.0	0.0	0.0	--	
Proportion of the population using improved drinking water resources, total	--	75	79	85	89	93.9[13/]	
Proportion of the population using improved sanitation facilities, total	--	20	21	24	26	40.9[13/]	
Goal 8: Develop a global partnership for development							Not Met
Debt relief committed under HIPC initiative, cumulative million US$ in end-2009 NPV terms	--	--	--	--	--	164[13/]	
Debt relief delivered in full under MDRI initiative, cumulative million US$ in end-2009 NPV terms	--	--	--	--	--	46[13/]	
Debt service as a percentage of exports of goods and services and net income	29	27[3/]	22	61	3	15.1[13/]	
Fixed telephone lines per 100 inhabitants	1.9	2.0	3.3	4.7	4.7	3.4[13/]	
Mobile cellular subscriptions per 100 inhabitants	--	--	--	8	62	64.9[13/]	
Internet users per 100 population	--	--	5	14	19	24.4[13/]	
Net ODA received per capita (current US$)	466	657	247	213	298	284[13/]	
ODA received in small islands developing states as a percentage of their GNI	--	--	--	29	25	16.79[13/]	
Developed country imports from developing countries, admitted duty free, percent	--	--	97	100	100	--	
Developed country imports from the LDCs, admitted duty free, percentage	--	--	97	100	100	--	
Other							
Fertility rate, total (births per woman)	5.4	5.0	4.6	4.1	3.7	4.6[13/]	
GNI per capita, Atlas method (current US$)	--	--	--	750	1240	1670[13/]	
GNI, Atlas method (current US$, millions)	--	--	--	114	205	312[13/]	
Life expectancy at birth, total (years)	61	62	62	63	64	66[13/]	
Population, total (thousands)	116	128	141	153	165	186[13/]	
Trade (% of GDP)	--	--	79	67	76	84[13/]	

Source: World Bank Development Indicators.

1/ Correspond to 1991 2/ Correspond to 1992 3/ Correspond to 1997 4/ Correspond to 1999 5/ Correspond to 2001 6/ Correspond to 2002
7/ Correspond to 2004 8/ Correspond to 2006 9/ Correspond to 2007 10/ Correspond to 2008 11/ Correspond to 2009 12/ Correspond to 2011 13/ Correspond to 2014

Appendix I. Letter of Intent

São Tomé, November 7, 2016

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

Dear Ms. Lagarde:

1. The Democratic Republic of São Tomé and Príncipe has continued to advance implementation of its economic reform program, supported by an IMF arrangement under the Extended Credit Facility (ECF) since July 2015. Notwithstanding the country's fragility and dependence on foreign resources in an uncertain environment, the government's efforts to strengthen macroeconomic stability, foster sustainable and inclusive growth, and reduce poverty in the context of the second National Poverty Reduction Strategy Paper (PRSP-II) have yielded some success. In general, macroeconomic stability improved, evidenced by stable and sustainable growth and lower inflation. However, the economy continues to face significant challenges in terms of high debt, risks in the banking system, and weak competitiveness, undermining the job creation and poverty reduction efforts.
Our engagement with creditors and donors toward reaching a cooperative and meaningful solution for the country's large infrastructural needs is ongoing and we have been successful in bringing more bilateral donors onboard. Our ambitious structural reform agenda—primarily aimed at addressing bottlenecks to higher, sustained, and inclusive growth and strengthening the financial sector—is also being implemented with technical and financial assistance from our international partners.

2. The government believes that measures and policies described in the July 2015 Memorandum of Economic and Financial Policies (MEFP Attachment I) remain appropriate for attaining the objectives of our program. The attached supplement to the MEFP discusses performance under the program thus far and updates policies toward meeting these objectives. Our key focus going forward will be on measures to address the fiscal slippage in the first half of the year, manage liquidation of Banco Equador to safeguard financial stability and minimize fiscal cost, and enhance liquidity management by developing a secondary market.

3. Recently, the government concluded discussions on the second review under the ECF-supported program with an IMF staff mission, with focus on program implementation through end-June 2016, as well as on measures to be implemented during the rest of 2016 and 2017. We satisfied four of six end-June 2016 performance criteria (PCs). Policy delays and slippages ahead of the Presidential elections, combined with the delayed disbursement of external financing, led to missed PCs on the floors on domestic primary balance and on net international reserves of the central bank. We also overshot the indicative target ceiling on

dobra base money and spent slightly less than programmed in pro-poor expenditure. On the other hand, indicative targets on new domestic arrears and tax revenue were met. The government has since introduced corrective measures to address the revenue shortfall and believes these are well-entrenched to prevent future occurrence.

4. The attached MEFP describes government policies for 2016–18 that would support achieving program objectives under the ECF arrangement. We remain fully committed to achieve the objectives of the program and will take any additional measures necessary to that end. We will consult with the IMF on the adoption of such measures prior to any revision of the policies indicated in the MEFP.

5. In light of the progress in implementing the program, we request the IMF Executive Board to approve the waivers for non-observance of domestic primary deficit and net international reserves performance criteria with test date at end-June 2016, modification of performance criteria on net international reserves for end-December 2016, set end-June 2017 and end-December 2017 PCs, and request for the completion of the second review as well as the third disbursement of SDR 634,285 under this arrangement.

6. The government will continue to provide Fund staff with all relevant information mentioned in the Technical Memorandum of Understanding (TMU), concerning further progress made under the program. During the program period, the government will not introduce or strengthen any exchange controls, multiple exchange rate practices, or import restrictions for balance of payments purposes, nor will it conclude any bilateral payment agreements in violation of Article VIII of the Fund's Articles of Agreement.

7. The government agrees to make public this Letter of Intent, along with the attached MEFP and TMU, and the entire IMF staff report on the second review. We hereby authorize their publication and posting on the IMF website, once the IMF Executive Board approves the completion of the second review under the three-year arrangement under the ECF.

Sincerely yours,

/s/	/s/
Mr. Américo d'Oliveira Ramos, Minister of Finance, Commerce and Blue Economy	Ms. Maria do Carmo Trovoada Silveira, Governor of the Central Bank of São Tomé and Príncipe

Attachments:

1. Memorandum of Economic and Financial Policies.
2. Technical Memorandum of Understanding.

Attachment I. Memorandum of Economic and Financial Policies for 2016–18

This Memorandum of Economic and Financial Policies (MEFP) updates the one outlined for the completion of the first review approved by the IMF Executive Board on June 10, 2016. It describes recent macroeconomic developments, implementation of the ECF-supported program, the economic outlook and risks, and macroeconomic policies.

RECENT ECONOMIC DEVELOPMENTS

1. Economic activity in the first half of the year remained somewhat below expectation. Preliminary indicators suggest that economic activity, compared to last year, was boosted by tourism receipts and better cocoa yield supported by good rainfall patterns, as well as election-related spending. However, a stimulus expected from timely execution of externally-financed investment projects failed to materialize because of delays in the disbursement of financing; slow credit growth also continued to hamper economic activities. To compensate for the missed stimulus, the government brought forward the planned issuance of a nine-month treasury bill to financed key investment projects. The twelve-month inflation accelerated by 1.8 percentage points from December 2015 to 5.8 percent in September, driven by rising food prices and changes in the CPI basket.

2. Fiscal performance was mixed. Domestic primary spending was well above target (mainly on goods and services, transfers, and treasury-funded capital spending), more than offsetting slightly better-than-projected domestic revenues, resulting in a larger-than-targeted domestic primary deficit of 2 percent of GDP by 1.3 percent of GDP at the end of June 2016. The overall fiscal balance was, however, well below target, because of shortfalls in privatization and externally-financed capital spending. Part of the domestic primary spending was financed by frontloading the issuance of the planned 2 percent of GDP of treasury bills and transfers from the National Oil Account, as privatization proceeds failed to materialize. The planned off-loading of part of the government shares in the largest commercial bank and the largest telecom company[1] (amounting to about 5 percent of GDP) is no longer expected to be finalized this year due to delays in the negotiations with interested parties. Foreign-financed capital spending was also lower than projected, due to delayed disbursement of external financing, including about a 3.8 percent of GDP loan from Turkey and Kuwait which now looks unlikely to be finalized this year. This was however, partially off-set by an unbudgeted disbursement of US$4.5 million from Angola, constituting the third tranche of the loan contracted in 2014. Tax revenues were held back by lower-than-expected growth and imports and by delay in implementing corrective revenue measures agreed during the first review. That notwithstanding, tax revenue was higher than last year at 6 percent of GDP (compared to 5.6 percent of GDP in 2015, excluding 1.2 percent of GDP of ENCO tax arrears payments).

[1] The government was expecting proceeds from these privatizations to finance critical investment projects.

3. Excess liquidity in the banking system remains high despite a contraction of monetary aggregates and modest credit expansion in the first half of the year. Broad money fell by 6.2 percent during the first seven months of the year, primarily on account of lower net foreign assets that reflected weak economic activity and fall in foreign exchange inflows. In contrast, private sector credit increased slightly as interest rates fell across all classes of deposits and loans. That notwithstanding, the excess liquidity in the banking system remains high, close to a third of deposits, reflecting the lack of commercial lending opportunities (including lack of bankable projects) for commercial banks in an environment of persistently high non-performing loans.

4. Banking sector vulnerability continues to be a source of concern. Effective August 1, 2016, and in line with the new banking resolution law, the central bank (BCSTP) cancelled the license and initiated court bankruptcy proceedings against Banco Equador—the fourth-largest bank by assets—which had been under BCSTP administration since January 2015. This action was the last resort, after failure to identify a suitable investor to buy a transitional bank created from good assets and liabilities of Banco Equador. End-June 2016 financial sector indicators show a further 6.1 percentage point worsening of the non-performing loans (NPL) ratio to 35.9 percent from the beginning of the year, largely attributable to the decision to liquidate Banco Equador. Notwithstanding the level of capital adequacy, solvency ratio remained virtually unchanged, the basic and supplementary capital ratios were reduced slightly in the same period.

5. The current account improved due to a strong rebound in travel receipts and subdued imports. In the first half of 2016, imports increased moderately relative to 2015, due to slower-than-expected economic activity. The improvement of the current account balance was largely due to strong growth of tourism receipts. However, due to disappointingly low foreign grants and loans inflows, international reserves declined to US$51 million at the end of June 2016, equivalent to 3.7 months of projected 2016 imports.

PERFORMANCE UNDER THE ECF-SUPPORTED PROGRAM

6. Performance under the program through end-June 2016 was mixed. Four of the six performance criteria were met (Table 1). The floors on domestic primary balance and on net international reserves of the central bank were missed, the former by a wide margin of about 1.3 percent of GDP (the target for end-June was -0.7 percent of GDP), due to higher primary domestic spending. The floor on net international reserves was missed due to delayed disbursement of external financing. Moreover, the indicative target ceiling on dobra base money was exceeded by almost 12 percent due to higher net deposits of the central government, and pro-poor spending was below the floor by about 1 percent. On the other hand, indicative targets on new domestic arrears, and for tax revenue were met.

7. Good progress was made in implementing the structural reforms under the program (see Table 2). Two of the three end-June 2016 structural benchmarks were met. We have submitted to staff a draft comprehensive strategy to help banks deal with high NPLs. The strategy has been strengthened based on comments provided by the Fund's Monetary and Capital Market Department (MCM). We have received granted powers by the national assembly and have completed targeted amendments of twelve provisions of the tax code, including to transfer the collection of tax arrears from fiscal court judge to the tax administration. On the other hand, the end-June structural benchmark to introduce an automatic fuel price adjustment mechanism was not met, but significant progress has been made and we have committed to meeting this benchmark as a prior action for the completion of this review.

ECONOMIC OUTLOOK AND RISKS

8. The economic outlook for 2017 and the medium term is favorable despite some risks. The expected pick-up in growth in the second half of the year is uncertain due to further slowdown in economic activity in connection with lackluster imports. We expect growth to be at 4 percent this year instead of the 5 percent target, but the medium term target of 5.5 percent remains attainable. The expected modest recovery in world commodity prices would be offset by a fall in imports which may continue to hamper economic activity this year. There has been a recent uptick in inflation reflecting growing aggregate demand pressures and supply constraints. Risks to this outlook are tilted to the downside. Domestically, the main risks emanate from the high and rising NPLs, which could disrupt the recent resumption of lending and general business and trade activity, and it also presents a fiscal risk, including the ongoing liquidation of Banco Equador. Externally, disbursement of foreign financing for capital spending could be further delayed while global economic and financial uncertainties could curtail FDI inflows, demand for cocoa, and tourist arrivals.

MACROECONOMIC POLICIES

A. Address the Fiscal Slippage in the First Half of the Year

9. The end-December 2016 domestic primary deficit target of 2 percent of GDP remains feasible and appropriate, despite the slippage in the first half of the year. The government has stepped up efforts to strengthen revenue collection together with greater fiscal discipline, in particular with regard to domestic primary spending. The current fall in imports, as a result of ongoing pressures on foreign exchange, will undermine the revenue target. It is currently estimated that this will result in additional 1.4 percent of GDP fall in revenue. We are committed to cutting spending to fully offset the expected shortfall in revenue through greater coordination among line ministries and budget and treasury directorates, to ensure that the overall end-2016 fiscal target is achieved. In particular, the government has identified expenditure cuts in transfers and other current spending, amounting to 1.4 percent of GDP which will ensure that the end-2016 domestic primary deficit target of 2.0 percent of GDP is achieved. Foreign-financed capital spending will pick up by 8.1 percent of GDP in the second half of the year, [including disbursements from Taiwan, Province of China (US$15 million), African Development Bank (US$9 million), Portugal (US$3.9 million) and the World Bank (US$5 million).

10. Beyond 2016, the baseline fiscal path agreed during the first review remains broadly appropriate and guides the broad outline of 2017 budget. Consistent with the program's medium-term objective of moving from high to moderate risk of debt distress, we will cap foreign-financed capital spending to the level of disbursements of already contracted project loans and grants and limit new borrowing. The 2017 budget will target a tax revenue ratio of 15.0 percent of GDP, revised down from 15.4 percent of GDP initially projected before accounting for the full impact of sharp fall in imports including oil imports which is affecting international trade taxes significantly. The domestic primary expenditure level will be anchored on achieving a domestic primary deficit target of 1.8 percent of GDP. We will carefully review treasury-financed capital spending in light of our commitments of 2016, giving priority to already started projects over new ones.

11. We will continue to undertake ambitious structural fiscal reforms aimed at supporting the fiscal consolidation efforts, including:

- *Enhance revenue mobilization through legislative and tax administration reforms will continue in 2017*. The focus will be placed on the preparation of VAT legislation and changes to the income tax to maintain coherence in the tax system (*end-December 2016 structural benchmark*). Tax administration reforms will emphasize: (i) developing human capacity; (ii) improving working conditions; and (iii) strengthening fiscal operations, including more dynamic and secured management of a taxpayer database, management of taxpayer files based on risk analysis that reflects strong concentration of revenue from few taxpayers, reorientation of inspection activity towards broadening the tax base, imposing fines on tax evasion, improving customer services and taxpayers education, and adopting a modern computer information system with key functionalities such as automatic notification of taxpayers in default, extraction of statistical data, surveillance, and oversight support.

- *Strengthen fiscal discipline*. In light of recent expenditure slippages and uncertainty about the prospects for privatization proceeds, the government will rigorously restrain spending on goods and services and treasury-financed capital, and monitor budget execution closely to ensure expenditure commitments are issued based on available resources.

- *Strengthen Public Financial Management (PFM)*. The government is committed to achieving tangible progress in transparency, and sound and efficient management of public resources. We have already completed a diagnostic study of the electronic information management system (SAFEe) with the help of AfDB. The study includes terms of reference and cost estimate for development of customized applications that will allow the extension of SAFEe's reach to autonomous services and municipalities as well as enhancement of the system with critical added functionalities, including reconciliation of treasury accounts, management of government contracts, foreign aid, and public debt. The government has already extended oversight to the general inspection finance entity and is working on extending oversight to the Court of Public Accounts. To ensure value for money, the government will also move forward with the implementation of a centralized framework for appraising and prioritizing capital expenditure projects, public investment management assessment (PIMA) framework, and medium-term fiscal and expenditure frameworks.

- *Reduce fiscal risk and improve debt management*. The government remains committed to effectively apply the automatic fuel price adjustment mechanism and has taken all relevant actions as a prior action for the completion of the second review, to avert fiscal risks from rising oil prices under the present subsidized pricing system; it has communicated this clearly to the public. On debt management, we have submitted an updated medium term public debt management strategy to parliament together with the draft 2017 budget, have completed a new debt management performance assessment (DeMPA) with World Bank support, and the migration to a new debt database and the preparation of guidelines on debt management will be finalized in the first quarter of next year. We will finalize and submit a draft public private partnership (PPP) law for the approval to parliament (*end-June 2017 structural benchmark*).

- Consistent with the IMF's new policy on debt limits, the government has revised the borrowing plan submitted in the first ECF review (Text Table 1). All loans are expected to be on concessional terms, with the bulk to finance infrastructure projects and social spending. The government reserves the right to revise this plan during the next ECF review.

Text Table 1. Borrowing Plan, 2016–18

PPG external debt	Volume of new debt in 2016		PV of new debt in 2016 (program purposes)		PV of new debt in 2016 (including negative GEs)	
	USD million	Percent	USD million	Percent	USD million	Percent
By sources of debt financing	**1.8**	**100**	**1.2**	**100**	**1.2**	**100**
Concessional debt, of which	**0.0**	**0**	**0.0**	**0**	**0.0**	**0**
Multilateral debt	0.0	0	0.0	0	0.0	0
Bilateral debt	0.0	0	0.0	0	0.0	0
Other	0.0	0	0.0	0	0.0	0
Non-concessional debt, of which	**1.8**	**100**	**1.2**	**100**	**1.2**	**100**
Semi-concessional	1.8	100	1.2	100	1.2	100
Commercial terms	0.0	0	0.0	0	0.0	0
By Creditor Type	**1.8**	**100**	**1.2**	**100**	**1.2**	**100**
Multilateral	1.8	100	1.2	100	1.2	100
Bilateral - Paris Club	0.0	0	0.0	0	0.0	0
Bilateral - Non-Paris Club	0.0	0	0.0	0	0.0	0
Other	0.0	0	0.0	0	0.0	0
Uses of debt financing	**1.8**	**100**	**1.2**	**100**	**1.2**	**100**
Infrastructure	0.0	0	0.0	0	0.0	0
Social Spending	0.0	0	0.0	0	0.0	0
Budget Financing	0.0	0	0.0	0	0.0	0
Other	1.8	100.0	1.2	100.0	1.2	100.0
Memo Items						
Indicative projections						
Year 2	**21.8**		**13.8**		**13.8**	
Year 3	**21.8**		**13.8**		**13.8**	

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

B. Strengthen Liquidity Management

12. Against the backdrop of excess liquidity, the BCSTP remains committed to further refine the liquidity forecasting and management tools. With regards to forecasting, the focus will be on encouraging closer cooperation between the central bank and the treasury to further minimize forecasting errors and improve the assessment accuracy for liquidity needs of the banking system with a view to inform timing and issuance of treasury bills and bonds in the nascent money market. The BCSTP will also enhance existing liquidity management tools, including developing the secondary market for government securities, creating conditions for long-term liquidity management, and reducing the stigma associated with participating in the interbank money market through mandatory transparent, timely, accurate, and public reporting of banks' audited financial statements.

C. Reducing Risks in the Banking Sector

13. The government decided to protect small depositors as part of the liquidation of Banco Equador. The central bank withdrew the license of Banco Equador on August 1, 2016 after making all efforts to attract suitable partners to take over the bank. In addition, to safeguard financial stability and prevent social unrest ahead of the 2016 presidential elections which was held on August 7, the central bank decided to protect small depositors, excluding depositors' shareholders and their related parties, managers and their related parties, non-residents, debtors, and all customers with outstanding loans with the bank. The central bank has paid up to €4,000 per qualifying depositor so far and the next step is to distribute any remaining monies after the completion of the court-mandated liquidation process. The average value of deposits covered so far amounts to € 209 and the average value of fully-covered deposits amounted to €91. The total amount set aside by the central bank to pay out eligible depositors so far is €1.7 million (0.5 percent of GDP), of which €0.85 million has already been paid out. We have requested TA from the Fund to guide the process of finalizing the liquidation of Banco Equador with the overall objective of safeguarding the stability of the financial system and reducing fiscal cost. We believe that our actions have so far removed some doubts on the status of Banco Equador following the long period over which this bank has been under administration. So far there has not been any panic reaction from customers and on other banks and all banks have welcomed the central bank's decision to decisively deal with this liquidation, including the protection of small depositors.

14. Fiscal cost of liquidation has been minimized. We have made efforts to limit the use of public funds and use proceeds from sales of the bank's assets to bolster negative effects on depositors and the economy. We are very optimistic that the guarantee given by the council of ministers to back the central bank's financing to protect small depositors will not result in additional fiscal costs to the budget. There are clearly identified assets that are being protected as part of the liquidation process and proceeds from which would be used to offset the cost incurred by the central bank. The central bank has the preferred status and will be the first to be paid from any proceeds from the liquidation process. In the event that the full cost of liquidation is not realized by the central bank, following sales of identified assets due to deterioration in assets, the central bank plans to withhold dividends to government until recovery of full cost of the liquidation. Starting from the 2017 budget, the government has committed to make room to accommodate this contingent liability, which will amount to about 5.5 billion dobras per year over 7 years.

15. The BCSTP will move decisively to implement the time-bound action plan to address the large stock of NPLs in the banking system. This will include the completion of an independent detailed asset quality review (AQR) (*end-December 2017 structural benchmark*) and a recently concluded assessment of regulation and supervision in lieu of a full assessment of compliance with Basel Core Principles (*end-December 2016 structural benchmark*) with the help of MCM technical assistance. These assessments will reduce uncertainties about asset quality and banks' financial health and set the stage for remedial action. Following the AQR, the BCSTP will direct banks to improve internal policies and procedures, increase provisioning, and promptly recapitalize if appropriate. Moreover, the government will reform debt enforcement and insolvency regimes, out-of-court workout aimed at rehabilitating viable debtors, and improve the operational capacity of banks to reduce NPLs.

D. Structural Reforms

16. The structural reforms agenda prioritizes export diversification and cost competitiveness to support growth and external stability. The government is working with the World Bank on finalizing a national export diversification strategy (*end-December 2017 structural benchmark*) centered on sustainable tourism growth. In addition, we will pursue strategies to address the unreliable supply and high cost of electricity, including substitution to alternative and cheaper energy sources), reform the state electricity company (EMAE), eliminate cross-subsidies, and move to full cost recovery of electricity tariffs (*end-December 2016 structural benchmark*).

OTHER PROGRAM ISSUES

17. Safeguards. The BCSTP is committed to implementing the recommendations from the September 2015 safeguards assessment, which included independent oversight of the audit mechanisms, internal controls, financial reporting (*end-December 2016 structural benchmark*), and amendments to the central bank Organic Law.

18. Statistics. Efforts to address data shortcomings will continue. There is scope to improve the balance of payments statistics and extend the coverage of the international investment position. The national statistics institute (INE) has completed the rebasing of the national accounts to 2008 and a new CPI, reflecting price movements in a broader basket of goods and services, using 2014 as the base year. The next steps include splicing the pre–and post–2008 GDP and pre–and post–2014 CPI series, and improving the statistics by developing data on the components of GDP on the demand side and quarterly GDP, including high frequency indicators of economic activity.

PROGRAM MONITORING

19. The performance criteria (PC), indicative targets (IT), and structural benchmarks for the remainder of 2016 and for 2017 are presented in Tables 3 and 4. The definitions of quantitative PCs and ITs are provided in the attached Technical Memorandum of

Understanding (TMU), which also defines the scope and frequency of data reporting for program monitoring purposes. The third ECF review is expected to be completed on or after April 15, 2017, the fourth review on or after October 15, 2017, and the fifth review on or after April 15, 2018.

Table 1. São Tomé and Príncipe: Performance Criteria and Indicative Targets for End-June 2016

(Billions of dobra, cumulative from beginning of year, unless otherwise specified)

	2016					
	March		June			
	Indicative Target	Actual	Performance Criteria [1]	Performance Criteria [2] w/ adjustments	Actual	Status
	31-Mar-16		30-Jun-16			
Performance criteria:						
Floor on domestic primary balance (as defined in the TMU) [2, 12]	-23	-114	-54	-54	-158	Not met.
Ceiling on changes in net bank financing of the central government (at program exchange rate) [3, 4, 5]	0	88	0	61	45	Met
Floor on net international reserves of the central bank (US$ millions) [2, 4]	62	47	62	59	53	Not met.
Ceiling on central government's outstanding external payment arrears (stock, US$ millions) [5, 6, 7, 8]	0	0	0	...	0	Met
Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (US$ millions) [5, 6, 7, 8, 9]	0	0	0	...	0	Met
Ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP (stock, US$ millions) [5, 7, 8, 9]	0	0	0	...	0	Met
Indicative targets:						
Ceiling on change of central government's new domestic arrears [12]	0	-6	0	...	-2	Met
Ceiling on dobra base money (stock)	1,062	1,130	1,085	...	1,211	Not met.
Floor on pro-poor expenditures [12]	168	112	289	...	285	Not met.
Floor on tax revenue [12]	181	209	422	...	464	Met
Memorandum items:						
New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the BCSTP (US$ millions) [5, 7, 8, 10, 12]	14	0	14	...	0	...
Transfer from NOA to the budget (US$ millions)	1.6	2	1.6	...	2	...
Net external debt service payments [11]	18	62	43	...	116	...
Official external program support [11]	20	0	47	...	12	...
Treasury-funded capital expenditure	12	35	28	...	75	...

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

[1] Performance at the June 2016 test date is assessed on the second review.

[2] The floor will be adjusted upward or downward according to definitions in the TMU.

[3] The ceiling will be adjusted downward or upward according to definitions in the TMU.

[4] Excluding the National Oil Account (NOA) at the Central Bank.

[5] The term "central government" is defined as in ¶ 3 of the TMU, which excludes the operations of state-owned enterprises.

[6] This criterion will be assessed as a continuous performance criterion.

[7] The term "external" is defined in accordance with the residency of the creditor as indicated in point 2 of the IMF Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements adopted by the Decision No. 6230-(79/140) of the Executive Board of the IMF (as amended effective December 1, 2009).

[8] This performance criterion or memo item applies not only to debt as defined in point 9 of the IMF Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements adopted by the Decision No. 6230-(79/140) of the Executive Board of the IMF (as amended effective December 1, 2009) but also to commitments contracted or guaranteed for which value has not been received. For further details on the definition of debt and external arrears refer to the TMU, ¶ 4 and 14.

[9] Only applies to debt with a grant element of less than 35 percent as defined in point 8 g (i) of the IMF Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements adopted by the Decision No 6230-(79/140) of the Executive Board of the IMF (as amended effective October 11, 2013). For further details on the definition of concessionality refer to the TMU, ¶ 20.

[10] Only applies to debt with a grant element of at least 35 percent.

[11] As defined in the TMU, valued at the program exchange rate.

[12] Cumulative from end December 2015.

Table 2. São Tomé and Príncipe: Structural Benchmarks, End-June 2016

Policy Objectives and Measures	Timing	Macro Rationale	TA involved	Status
Strengthening Public Finances				
Adopt an automatic fuel price adjustment mechanism that allows timely pass-through of import costs with a view to its gradual introduction in 2016.	End-June 2016	To remove implicit fuel price subsidies and loss of fiscal revenues	FAD TA on design of automatic price adjustment mechanism	Not met.
Introduce legislation to transfer the execution for collection of tax arrears from fiscal court judge to the tax administration.	End-June 2016	To boost tax arrears collection	No TA involved	Met.
Enhancing Monetary Policy and Financial Stability				
Prepare and submit to staff a comprehensive strategy to help banks deal with high NPLs on their balance sheets.	End-June 2016	To support financial sector stability and growth	MCM TA	Met.

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

Table 3. São Tomé and Príncipe: Proposed Performance Criteria and Indicative Targets for 2016–17

(Billions of Dobra, cumulative from beginning of year, unless otherwise specified)

	2016		2017			
	September	December	March	June	September	December
	Indicative Target	Performance Criteria [1]	Indicative Target	Performance Criteria [1]	Indicative Target	Performance Criteria [1]
	30-Sep-16	31-Dec-16	31-Mar-17	30-Jun-17	30-Sep-17	31-Dec-17
Performance criteria:						
Floor on domestic primary balance (as defined in the TMU) [2, 12]	-100	-155	-74	-124	-173	-152
Ceiling on changes in net bank financing of the central government (at program exchange rate) [3, 4, 5]	0	0	0	0	0	0
Floor on net international reserves of the central bank (US$ millions) [2, 4]	51	49	50	50	50	54
Ceiling on central government's outstanding external payment arrears (stock, US$ millions) [5, 6, 7, 8]	0	0	0	0	0	0
Ceiling on the contracting or guaranteeing of new nonconcessional external debt by the central government or the BCSTP (US$ millions) [5, 6, 7, 8, 9]	0	0	0	0	0	0
Indicative targets:						
Ceiling on change of central government's new domestic arrears [12]	0	0	0	0	0	0
Ceiling on dobra base money (stock)	1,102	1,465	1,206	1,254	1,290	1,540
Floor on pro-poor expenditures [12]	359	448	171	301	417	501
Floor on tax revenue [12]	783	1,170	206	520	817	1,237
Memorandum items:						
New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the BCSTP (US$ millions) [5, 7, 8, 10, 12]	14	18	22	22	22	22
Transfer from NOA to the budget (US$ millions)	1.6	1.6	2.3	2.3	2.3	2.3
Net external debt service payments [11]	107	233	33	49	58	107
Official external program support [11]	88	205	0	8	8	205
Treasury-funded capital expenditure	50	101	25	25	25	94

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

[1] Performance at the December 2016 and June 2017 test dates are assessed on the third and fourth reviews respectively and performace at the December 2017 is assessed on the fifth review.

[2] The floor will be adjusted upward or downward according to definitions in the TMU.

[3] The ceiling will be adjusted downward or upward according to definitions in the TMU.

[4] Excluding the National Oil Account (NOA) at the Central Bank.

[5] The term “central government” is defined as in ¶ 3 of the TMU, which excludes the operations of state-owned enterprises.

[6] This criterion will be assessed as a continuous performance criterion.

[7] The term “external” is defined on the basis of the residency of the creditor per paragraph 5 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014).

[8] This performance criterion or memorandum item applies not only to debt as defined in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014), but also to commitments contracted or guaranteed for which value has not been received. For further details on the definition of debt and external arrears refer to the TMU, ¶¶ 6 and 15.

[9] Only applies to debt with a grant element of less than 35 percent. For further details refer to the TMU, ¶ 20.

[10] Only applies to debt with a grant element of at least 35 percent.

[11] As defined in the TMU, valued at the program exchange rate.

[12] Cumulative from end December 2015 and end December 2016 respectivelly.

Table 4. São Tomé and Príncipe: Structural Benchmarks and Prior Action, 2016–17

Policy Objectives and Measures	Timing	Macro Rationale	TA involved
Strengthening Public Finances			
Adopt an automatic fuel price adjustment mechanism that allows timely pass-through of import costs *(prior action)* .	End-November 2016	To support arrears clearance plan	FAD TA on design of automatic price adjustment
Adopt a plan to reform EMAE (state-owned electricity and water utilities company) to ensure full cost-recovery.	End-December 2016	To support arrears clearance plan	With World Bank and EU support
Submit to the National Assembly a new VAT law.	End-December 2016	To support the introduction of VAT	Forthcoming FAD/LEG TA
Complete a public investment management assessment (PIMA) and submit to staff a reform plan to strengthen public investment management practices.	End-December 2016	To enhance capacity for efficient public investment decision-making	With World Bank support
Submit the draft public private partnership (PPP) law to the National Assembly *(newly proposed).*	End-June 2017	To enhance capacity for efficient public investment decision-making	No TA involved
Enhancing Monetary Policy and Financial Stability			
Establish an Audit Board for BCSTP that specifies a role similar to a conventional audit committee, with responsibilities for oversight of internal and external audit mechanisms, and financial reporting.	End-December 2016	To enhance independent oversight of the audit and control mechanisms	No TA involved
Complete assessment of regulation and supervision in lieu of a full assessment of compliance with Basel Core Principles *(proposed for revision).*	End-December 2016	To improve soundness of financial system	Forthcoming MCM TA
Complete an independent detailed asset quality review of banks *(newly proposed).*	End-December 2017	To support financial sector stability and growth	No TA involved
Facilitating Business Activities			
Develop and submit to the National Assembly a National Export Diversification Strategy document *(proposed to reset to a later date).*	End-December 2017	To promote economic diversification and employment opportunities	TA yet to be identified by authorities

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

Attachment II. Technical Memorandum of Understanding, June 2016

1. This Technical Memorandum of Understanding (TMU) contains definitions and adjuster mechanisms that clarify the measurement of quantitative performance criteria and indicative targets in Table 3, which are attached to the Memorandum of Economic and Financial Policies for 2016 and 2017. Unless otherwise specified, all quantitative performance criteria and indicative targets will be evaluated in terms of cumulative flows from the beginning of each calendar year.

2. **The program exchange rate** for the purposes of this TMU[1] will be 20,299 dobra per U.S. dollar, 24,500 dobra per euro, and 29,236 dobra per SDR for both 2016 and 2017.

PROVISION OF DATA TO THE FUND

3. Data with respect to all variables subject to performance criteria and indicative targets will be provided to Fund staff on the frequency described below (paragraph 27) with a lag of no more than four weeks for data on net international reserves of the Central Bank of São Tomé and Príncipe (BCSTP) and six weeks for other data. The authorities will transmit promptly to Fund staff any data revisions. For variables that are relevant for assessing performance against program objectives but are not specifically defined in this memorandum, the authorities will consult with Fund staff as needed on the appropriate way of measuring and reporting. Performance criteria included in the program are defined below and refer to the floor on domestic primary balance; the ceiling on changes in net bank financing of the central government; the floor on net international reserves of the central bank; the ceiling on central government's outstanding external payments arrears; the ceiling on the contracting or guaranteeing of new non-concessional external debt with original maturity of more than one year by the central government or the BCSTP; and the ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP.

DEFINITIONS

4. For the purposes of this TMU, **external** and **domestic** shall be defined on a residency basis.

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

[1] Data refer to the mid-point exchange rates published on the BCSTP's webpage for the last day of 2014.

6. **Debt** is defined as in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014). Debt will be understood to mean a current, i.e., not contingent, liability, created under a contractual agreement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract.

7. **Government domestic revenue (excluding oil revenue)** comprises all tax and non-tax revenue of the government (in domestic and foreign currencies), excluding: (1) foreign grants, (2) the receipts from the local sale of in-kind grants (e.g., crude oil received from Nigeria, food aid, etc.), and (3) any gross inflows to the government on account of oil signature bonus receipts and accrued interest on the National Oil Account (NOA). Revenue will be measured on a cash basis as reported in the table of government financial operations prepared by the Directorate of Budget and the Directorate of Treasury in the Ministry of Finance and Public Administration.

8. **Domestic primary expenditure** comprises all government spending assessed on a commitment basis (*base compromisso*), excluding (1) capital expenditure financed with external concessional loans and grants and (2) scheduled interest payments. Reporting of government domestic expenditure will be based on the state budget execution prepared every month by the Directorate of Budget and the Directorate of Treasury in the Ministry of Finance and Public Administration.

PERFORMANCE CRITERIA

9. **Performance criterion on the floor on domestic primary balance.** This performance criterion refers to the difference between government domestic revenue (excluding oil revenue) and domestic primary expenditure. For reference, this balance for end-June 2016 was -158 billion dobra, broken down as follows:

	Government domestic revenue:	587 billion
Less:	Government primary expenditure:	
	(As defined in paragraph 8)	745 billion
Equals:	Domestic primary balance:	-158 billion

10. **Performance criterion on the ceiling on changes in net bank financing of the central government (NCG).** This performance criterion measures the increase (decrease) in the stock of all outstanding claims on the central government held by the BCSTP and by other depository corporations (ODCs), less all deposits held by the central government with the BCSTP and with ODCs, as they are reported monthly by the BCSTP to the IMF staff. The balance of the National Oil Account (NOA) is not included in NCG. All foreign exchange-denominated accounts will be converted to dobra at the program exchange rate.

For reference, at end-June 2016, outstanding net bank financing of the central government (excluding NOA) was 45 billion dobra, broken down as follows:

	BCSTP credit, including use of IMF resources:		237 billion
Less:	Government deposits with the BCSTP (excluding NOA)		233 billion
	Of which:	Treasury dobra-denominated accounts	65 billion
		Treasury foreign currency-denominated accounts	94 billion
		Counterpart deposits	74 billion
Equals:	Net credit to government by the BCSTP		4 billion
Plus:	ODC's credit to the government		151 billion
Less:	Government deposits with ODCs (including counterpart funds)		110 billion
Equals:	Net bank financing of the government (excluding NOA)		45 billion

11. Performance criterion on the floor on net international reserves (NIR) of the BCSTP. The NIR of the BCSTP are defined for program-monitoring purposes as short-term (i.e., original maturities of one year or less), tradable foreign assets of the BCSTP minus short-term external liabilities, including liabilities to the IMF. All short-term foreign assets that are not fully convertible external assets nor readily available to and controlled by the BCSTP (i.e., they are pledged or otherwise encumbered external assets, including but not limited to the HIPC umbrella SDR account and assets used as collateral or guarantees for third-party liabilities) will be excluded from the definition of NIR. Securities whose market value on the last day of the year differs by over 20 percent from their original nominal issue price will be assessed at their market value as reported by the BCSTP's Markets Department. The balance of (1) NOA at the BCSTP, (2) banks' deposits related to capital or licensing requirements, and (3) banks' reserves denominated in foreign currency are excluded from the program definition of NIR. All values are to be converted to U.S. dollars at the actual mid-point market exchange rates prevailing at the test date. For reference, at end-June 2016 NIR was 1,163 billion dobra, calculated as follows:

Gross international reserves:				1,459 billion
	Of which:	Cash		27 billion
		Demand deposits		196 billion
		Term deposits (including banks' deposits in foreign currency)		597 billion
		Securities other than shares		587 billion
		Of which:	Portuguese Treasury Bond I	220 billion
			Portuguese Treasury Bond II	243 billion
			Rede Ferroviaria Nacional bonds	123 billion
		Accrued interest on securities		35 billion
		Reserve position in the Fund		0 billion
		SDR holdings		17 billion
Less:	Short-term liabilities (including liabilities to the IMF)			92 billion
Less:	Banks' reserves denominated in foreign currency			204 billion

Less:	Banks' guaranteed deposits denominated in foreign currency	0 billion
Equals:	Net international reserves	1,163 billion
Plus:	Other foreign assets	369 billion
Less:	Medium and long-term liabilities (including SDR allocation)	219 billion
Equals:	Net foreign assets	1,313 billion
Memorandum item:	National Oil Account (NOA)	254 billion

12. Performance criterion on the ceiling on the contracting or guaranteeing of new nonconcessional external debt by the central government or the BCSTP. This is a continuous performance criterion that refers to the contracting or guaranteeing of new external debt of any maturity (including overdraft positions but excluding normal import and supplier credits) by the government and/or the BCSTP. Debt is considered nonconcessional if it includes a grant element less than 35 percent. The grant element is the difference between the nominal value of the loan and its net present value, expressed as a percentage of the nominal value. The net present value of the debt at the date on which it is contracted is calculated by discounting the debt service payments at the time of the contracting of the debt. The discount rate used for this purpose is 5 percent. With respect to the precautionary line of credit from Portugal to support the pegging of the dobra to the euro, unpaid balances outstanding during the first three quarters of a given calendar year will be excluded from this ceiling. However, outstanding balances at the end of a given calendar year will be included in the assessment of compliance with this performance criterion. This performance criterion does not apply to IMF facilities. Debt being rescheduled or restructured is excluded from this ceiling. Medium- and long-term debt will be reported by the Debt Management Department of the Ministry of Finance and Public Administration (as appropriate) by the BCSTP, measured in U.S. dollars at the prevailing exchange rates. The government should consult with IMF staff before contracting or guaranteeing new medium–or long–term debt obligations.

13. Performance criterion on the ceiling on central government's outstanding external payment arrears. This is a continuous performance criterion. Central government external payment arrears consist of external debt service obligations (principal and interest) that have not been paid at the time they are due, as specified in the contractual agreement, subject to any applicable grace period. This performance criterion does not apply to arrears resulting from the nonpayment of debt service for which a clearance framework has been agreed or for which the government is actively seeking a rescheduling agreement.

INDICATIVE TARGETS

14. Ceiling on change of central government's new domestic arrears is set on the difference between expenditure on a commitment basis and cash payments (amounts past due after 40 days and unpaid).

15. Ceiling on dobra base money is set on the sum of currency issued—which consists of currency outside depository corporations and cash in vaults—and banks reserves denominated in dobra. Bank reserves refer to reserves of commercial banks (in dobra) held with the central bank and include reserves in excess of the reserve requirements.

For reference, at end-June 2016 dobra base money was 1,211 billion dobra, calculated as follows:

Currency issued:		273 billion
Of which:	Cash in vaults	47 billion
	Currency outside depository corporations	226 billion
Plus:	Bank reserves denominated in dobra	938 billion
Equals:	Dobra base money	1,211 billion

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

a. **Pro-poor current spending:** These cover the following functional classifications and expenditure categories (by budget code) as described in the matrix below:

Code	Economic classification of current expenditure	Education	Health	Social Security and Assistance	Housing and Community Services	Culture and Sport	Fuel and Energy	Agriculture and Fisheries
310000	Personnel Expenses	x	x					
331210	Specialty Durable Goods	x	x					
331290	Other Durable Goods	x	x					
331120	Fuels and Lubricants[1]	x	x					
331130	Foodstuffs, Food[1] and Accommodation	x	x					
331140	Specialized Current Consumable Materials (Specific to Each Sector)	x	x					
331190	Other Consumer Non Durable Goods	x	x					
332110	Water and Energy Services	x	x					
332120	Communication Services	x	x					
332130	Health services	x	x					
332220	Maintenance and Conservation Services	x	x					
353900	Other Miscellaneous Current Expenses	x	x	x				
352200	Transfers to non-profit institutions (private)		x	x				
352310	Retirement Pension and Veterans		x	x				
352320	Family Benefit		x	x				
352330	Scholarships	x						
352390	Other Current Transfers to Families		x	x				
353100	Unemployment Fund		x	x				
Code	**Economic classification of capital expenditure**							
411110	Feasibility Study and Technical Assistance	x	x	x	x	x	x	x
411120	Procurement and Construction of Real Estate	x	x	x	x	x	x	x
411200	Rehabilitation Works and Facilities	x	x	x	x	x	x	x
411300	Means and Equipments of Transportation	x	x	x	x	x	x	x
411400	Machinery and Equipment	x	x	x	x	x	x	x
411900	Other Fixed Capital Goods	x	x	x	x	x	x	x
412000	Stocks	x	x	x	x	x	x	x

Source: Diário da Republica de São Tome e Principe No. 21 - May 7, 2008, pages 12-13.

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

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

17. **Floor on tax revenue** is set on tax revenue that includes direct and indirect taxes as well as recovery of tax arrears and additional collection efforts.

MEMORANDUM ITEMS

18. New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the BCSTP measures such debt with a grant element of at least 35 percent.

19. Net external debt service payments by the central government are defined as debt service due less the accumulation of any new external payment arrears, as defined under the performance criterion on the ceiling on central government's outstanding external payment arrears.

20. Official external program support is defined as grants and loans, including in-kind aid when the products are sold by the government and the receipts are earmarked for a budgeted spending item, and other exceptional financing provided by foreign official entities and incorporated into the budget.

21. Treasury-funded capital expenditure is classified as part of domestic primary expenditure and covers public investment projects that are not directly financed by project grants and concessional loans or that have to be partially co-financed with government resources. It includes spending on new construction, rehabilitation, and maintenance. Expenditure on wages and salaries and the purchase of goods and services related to the projects will not be classified as capital expenditure.

USE OF ADJUSTERS

22. The performance criterion on the domestic primary balance will have one adjuster. The limit on the domestic primary balance will be adjusted upward if the government finds budget support and privatization receipts in 2016 and 2017 in addition to that described in the MEFP; this adjuster will be capped at 70.3 billion dobra (about 1 percent of 2015 GDP) for 2016 and 2017.[2]

23. The performance criteria on net bank financing of the central government and net international reserves of the central bank will be adjusted in line with deviations from amounts projected in the program for budget transfers from the NOA, official external program support, net external debt service payments, and domestic arrears will trigger adjustments on the above mentioned performance criteria. These deviations will be calculated cumulatively from end-December 2015 or end-December 2016, as appropriate (MEFP Attachment I, Table 3). The following is an explanation of these adjustments:

- Adjusters on ceilings on changes in net bank financing of the central government (NCG): Quarterly differences between actual and projected receipts of budget transfers from the NOA, official external program support, net external debt service

[2] Grants and related expenditures to cover the cost of the elections will be excluded from the measurements of the domestic primary deficit.

payments, and domestic arrears will be converted to dobra at the program exchange rate and aggregated from end-December 2015 or end-December 2016, as appropriate, to the test date. The ceilings will be adjusted downward (upward) by cumulative deviations downward (upward) of actual from projected net external debt service payments, and by deviations upward (downward) in budget transfers from the NOA, official external program support, and domestic arrears. The combined application of all adjusters at any test date is capped at the equivalent to US$3million at the program exchange rate.

- Adjusters for the floor on net international reserves (NIR) of the BCSTP: Quarterly differences between actual and projected receipts of budget transfers from the NOA, official external program support, net external debt service payments, and domestic arrears in dobra, will be converted to U.S. dollars at the program exchange rate and aggregated from end-December 2015 or end-December 2016, as appropriate, to the test date. The floor will be adjusted upward (downward) by the cumulative deviation downward (upward) of actual from projected net external debt service payments of the central government, and by deviations upward (downward) for budget transfers from the NOA, official external program support, and domestic arrears.
The combined application of all adjusters at any test date is capped in such a way that the adjusted floor does not fall short of US$46 million in 2016 and US$51 million in 2017.

DATA REPORTING

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

1) **Fiscal Data:** The Directorate of Treasury and Directorate of Budget at the Ministry of Finance and Public Administration will provide the following information to IMF staff, within six weeks after the end of each month or quarter, except for the public investment program (PIP), which will be provided three months after each quarter:

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

   - Monthly data on net credit to the government by the BCSTP, recorded account by account in a format fully compatible with the monetary accounts of the BCSTP;

   - Monthly detailed data on tax and nontax revenues;

   - Monthly detailed data on domestically financed capital expenditure on commitment (*compromisso*) and cash payments (*caixa*);

   - Monthly data on domestic arrears by type and by creditor;

- Quarterly data on implicit arrears to ENCO on account of fuel retail prices eventually not covering import costs, distribution margins and applicable taxes.
- Quarterly data on EMAE's arrears to ENCO.
- Monthly data on official external program support (non-project);
- Quarterly data on the execution of the public investment program (PIP) by project and sources of financing;
- Quarterly data on the execution of Treasury-funded capital expenditure by project type, amount, timetable of execution, and progress of execution;
- Quarterly data on project grant and loan disbursement (HIPC and non-HIPC);
- Quarterly data on bilateral HIPC debt relief;
- Latest outstanding petroleum price structures and submission of new pricing structures (within a week of becoming available).

2) **Monetary Data:** The BCSTP will provide the IMF staff, within three weeks from the end of each month, the monetary accounts of the BCSTP. Other monetary data will be provided within six weeks after the end of each month for monthly data, within two months after the end of each quarter for quarterly data, and within two months after the end of the year for annual data. The BCSTP will provide the following information to IMF staff:

- Daily data on exchange rates, to be posted on the central bank's web site;
- Daily data on interest rates, to be posted on the central bank's web site;
- Daily liquidity management table, including dobra base money and currency in circulation, to be posted on the central bank's web site;
- Daily net international reserve position, to be posted on the central bank's web site;
- Monthly balance sheet data of BCSTP (in IMF report form 1SR, with requested memorandum items);
- Monthly consolidated balance sheet data of other depository corporations (in IMF report form 2SR);
- Monthly consolidated depository corporations survey (in IMF survey 3SG);
- Monthly central bank foreign exchange balance (*Orçamento cambial*);
- Quarterly table on bank prudential ratios and financial soundness indicators;

- Quarterly data on the BCSTP's financial position (profit and loss statement, deficit, budget execution, etc.).

3) **External Debt Data:** The Directorate of Treasury at the Ministry of Finance and Public Administration will provide the IMF staff, within two months after the end of each month the following information:

- Monthly data on amortization and interest on external debt by creditor; paid, scheduled, and subject to debt relief or rescheduled;

- Quarterly data on disbursements for foreign-financed projects and program support loans.

- Annual data on future borrowing plans.

4) **National Accounts and Trade Statistics:** The following data will be provided to the IMF staff:

- Monthly consumer price index data, provided by the National Institute of Statistics within one month after the end of each month;

- Monthly data on imports (value of imports, import taxes collected, and arrears) and commodity export values, provided by the Customs Directorate at the Ministry of Finance and Public Administration, within two months after the end of each month;

- Monthly data on petroleum shipments and consumption (volumes and c.i.f. prices, by product), provided by the Customs Directorate.

Appendix II. Twelve Legislative Changes Proposed by Tax Directorate

1. Amendment of stamp duty on documents.

2. Amendment to procedure code and tax procedure.

3. Proposed amendment of corporate income tax code.

4. Proposed amendment of vehicles tax regulation approved by decree–law no. 13/93, of February 26.

5. Tax on alcohol and spirits beverages and tobacco.

6. Proposed amendment of personal income tax code.

7. Legal regime of invoices and equivalents documents.

8. Legislation on presentation of certificate attesting the compliance with tax obligations for licensing procedures.

9. Forgiveness of interest under the exceptional regime for settlement of tax arrears, whose period for voluntary payment expired.

10. Legislation on reforming the consumption-tax on services.

11. Draft law for adjustment of rate applicable on local production.

12. Reformulation of minimum value of income tax.

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

November 15, 2016

SECOND REVIEW UNDER THE EXTENDED CREDIT FACILITY AND REQUEST FOR WAIVERS FOR NONOBSERVANCE OF PERFORMANCE CRITERIA AND MODIFICATION OF PERFORMANCE CRITERIA—INFORMATIONAL ANNEX

Prepared By: The African Department (in Consultation with Other Departments)

CONTENTS

RELATIONS WITH THE FUND

(As of September 30, 2016)

Membership Status

Joined: September 30, 1977; Article XIV

General Resources Account:	**SDR Million**	**% Quota**
Quota	14.80	100.00
Fund holdings of currency (exchange rate)	14.80	100.02
Reserve tranche position	0.00	0.00

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	7.10	100.00
Holdings	0.28	3.89

Outstanding Purchases and Loans:	**SDR Million**	**% Quota**
ECF Arrangements	3.25	21.93

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
ECF[1]	07/13/2015	07/12/2018	4.44	1.27
ECF[1]	07/20/2012	07/13/2015	2.59	1.11
ECF[1]	03/02/2009	03/01/2012	2.59	0.74

[1]/ Formerly PRGF.

Projected Payments to Fund[2]

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

	Forthcoming				
	2016	2017	2018	2019	2020
Principal		0.44	0.39	0.33	0.26
Charges/Interest	0.00	0.00	0.00	0.01	0.01
Total	0.00	0.45	0.39	0.34	0.27

[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.

Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	December 2000
Assistance committed	
by all creditors (US$ million)[1]	124.30
Of which: IMF assistance (US$ million)	1.24
(SDR equivalent in millions)	0.82
Completion point date	March 2007
Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	0.82
Interim assistance	…
Completion point balance	0.82
Additional disbursement of interest income[2]	0.04
Total disbursements	0.87

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

2/ Under the enhanced framework, an additional disbursement is made corresponding to interest income earned on the amount of HIPC assistance committed but not disbursed.

Implementation of Multilateral Debt Relief Initiative (MDRI):

MDRI-eligible debt (SDR Million)[1]	1.43
Financed by: MDRI Trust	1.05
Remaining HIPC resources	0.38

Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGT**	**Total**
December 2007	N/A	0.38	0.38
March 2007	N/A	1.05	1.05

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

Safeguards Assessments:

The recent update of safeguards assessment found that severe capacity constraints have contributed to a weak safeguards framework at the BCSTP. In particular, safeguards relating to independent oversight on audit, financial reporting, and control mechanisms need strengthening. In addition, the BCSTP's legal framework will need to be revised to align it with leading practices for central banks. While external audits conducted by a reputable audit firm continue to serve as a critical safeguard, ongoing institutional development will be needed to strengthen capacity and bolster the safeguards framework. Further, the engagement of the Audit Board with revised roles and responsibilities will be needed for better oversight.

Exchange Arrangements:

The de jure and de facto exchange rate arrangement is a conventional peg against the euro. Since January 2010 São Tomé and Príncipe has pegged the dobra to the euro at a rate of dobra 24,500 per euro. The organic law of the BCSTP authorizes it to make decisions regarding exchange rate policy. The commission on foreign exchange sales cannot be higher than 2 percent for the euroand 4 percent for other currencies. Purchases of euro must be done at the rate published by the BCSTP and no commissions are allowed. The official euro–U.S. dollar cross rate is based on the European Central Bank (ECB) reference rate of the previous day. The BCSTP finances current international transactions at the official exchange rate only after verification of the documentation establishing the bona fide nature of the bank's request. Access to foreign exchange is limited to institutions having a net position in the transaction currency of less than 12 percent of qualified capital, a net position in total foreign currency less than 25 percent of qualified capital, and which are in compliance with the central bank's regulations on bank liquidity and capital adequacy. Financial institutions are allowed access to the central bank's facilities regardless of the above conditions if the foreign exchange is to be used for importation of goods and services in periods of crisis or for the importation of fuel. Commercial banks that meet these requirements can buy foreign exchange directly from the central bank, which can charge up to 1.5 percent commission on sales of euro and up to a 0.5 percent commission on purchases of euro. The buying rate is mainly indicative because the BCSTP rarely makes purchases. The current exchange rate system has effectively eliminated the multiple currency practice related to the existence of numerous exchange rate markets with differing exchange rates for spot transactions that existed in previous years.

São Tomé and Príncipe continues to avail itself of the transitional arrangements under Article XIV, but it does not maintain restrictions under Article XIV. However, it maintains one measure subject to Fund approval under Article VIII: an exchange restriction arising from Article 3(i) and Article 10.1(b) of the Investment Code (Law No. 7/2008) regarding limitations on the transferability of net income from investment. The restriction results from the requirement that taxes and other obligations to the government have to be paid/full-filled as a condition for transfer, to the extent the requirement includes the payment of taxes and the fulfillment of obligations unrelated to the net income to be transferred.

Article IV Consultation:

The Executive Board concluded the last Article IV consultation with São Tomé and Príncipe on June 10, 2016.

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

None.

Resident Representative:

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

Technical Assistance:

Date of Delivery	Department/Purpose
August 2016	MCM mission on banking supervision and regulation
August 2016	FAD mission on tax policy
April 2016	FAD mission on arrears management
March 2016	MCM mission on banking supervision
November 2015	STA mission on national accounts statistics
November 2015	FAD mission on automatic fuel pricing mechanism
September/October 2015	FIN mission on safeguards assessment
September 2015	MCM mission on banking supervision
July 2015	FAD mission on tax administration
June 2015	STA mission on balance of payments and IIP
April 2015	FAD mission on medium-term fiscal framework
March 2015	FAD mission on tax administration
March 2015	MCM mission on banking supervision
November 2014	MCM mission on banking supervision
September 2014	STA mission on national accounts statistics
September 2014	MCM mission on liquidity management
April 2014	STA mission on balance of payments and IIP
April 2014	MCM mission on liquidity management
March 2014	MCM mission on banking supervision
February 2014	FAD mission on public accounting
December 2013	FAD short-term expert visit on public accounting
November 2013	MCM mission on banking supervision
August 2013	FAD mission on revenue administration

Date of Delivery	Department/Purpose
August 2013	MCM mission on banking supervision
June 2013	FAD mission on public accounting
March 2013	MCM mission on banking supervision
January 2013	MCM mission on liquidity management
January 2013	FAD mission on public accounting
November 2012	FAD mission on medium-term fiscal framework
November 2012	FIN mission on safeguards assessment
November 2012	LEG follow-up mission on AML/CFT
October 2012	MCM mission on banking supervision
October 2012	FAD diagnostic mission on customs
October 2012	FAD mission on public accounting
September 2012	MCM mission on liquidity management
July 2012	LEG diagnostic mission on AML/CFT
April 2012	FAD mission on revenue administration
March 2012	FAD mission on public financial management
March 2012	STA mission on balance of payments
February 2012	LEG diagnostic mission on AML/CFT
February 2012	FAD mission on implementation of SAFEe
January 2012	FAD diagnostic mission on tax administration
November 2011	MCM TA needs assessment mission
November 2011	MCM mission on liquidity management
November 2011	FAD mission on public accounting
October 2011	FAD mission on public financial management
August 2011	FAD mission on public accounting
June 2011	MCM mission on liquidity management
June 2011	FAD mission on public accounting
February 2011	MCM mission on bank resolution framework
January 2011	FAD mission on public accounting
September 2010	MCM mission on liquidity management
August/September 2010	STA mission on monetary and financial statistics
December 2009	MCM mission on banking supervision
August 2009	MCM mission on banking supervision
June 2009	FIN mission on safeguards assessment
May 2009	FAD mission on public financial management

RELATIONS WITH THE WORLD BANK GROUP

Joint Managerial Action Plan (JMAP) for São Tomé and Príncipe

(As of November 30, 2016)

1. The IMF and World Bank São Tomé and Príncipe teams held regular meetings to discuss their respective work programs and macro critical structural reforms for São Tomé and Príncipe. The two institutions' teams met in the context of the preparations for the current ECF-supported program that discusses policies and financing during the prospective program period 2015–18, and for the prospective financial sector development plan (a World Bank initiative).

2. The World Bank's work program is guided by a Country Partnership Strategy for the fiscal years 2014 to 2018 approved in 2014 that focuses on supporting growth and job creation through two broad themes: macroeconomic stability and national competitiveness, and reducing vulnerability and strengthening human capacity. Gender, partnership, and capacity building are elements that cut across all the proposed engagements. A Debt Management and Performance Assessment (DeMPA) report was completed in October 2011, and an accompanying reform plan to improve debt management was completed in March 2012. A follow-up DeMPA and reform plan update mission is scheduled for November 2016.

3. The IMF's work program includes the Executive Board's consideration of the second review under the ECF-supported program in December 2016, third and fourth review missions in March and June 2017 respectively, the Executive Board's consideration of the third and fourth reviews under the ECF-supported program in June and December 2017 respectively, and future assistance in capacity development in the areas of public financial management, revenue administration, bank resolution and liquidation, and national accounts statistics.

4. The Bank and the Fund continue to provide complementary support to help São Tomé and Príncipe strengthen public financial management and make progress toward debt sustainability. Regarding the latter, the teams prepared a Joint IMF-World Bank Debt Sustainability Analysis (DSA) update in collaboration with the authorities of São Tomé and Príncipe in May 2016; the analysis updated the previous Joint DSA dated June 24, 2015 (IMF Country Report No. 15/196, Supplement 2).

Work Program for Period 2016–17			
Title	*Products*	*Provisional timing of missions*	*Expected delivery date*
A. Mutual information on relevant work programs			
World Bank work program in the next 12 months	• STP Power Sector Recovery Project • STP New Programmatic DPO Series • DeMPA and reform plan • Public expenditure review • Support to the new household survey • Payment system and financial inclusion • Bank resolution • Support to business environment reforms • Transport Sector Development Project • Quality Education for All	October 2016 November 2016 November 2016 November 2016 November 2016 October 2016 November 2016 December 2016 November 2016 October 2016 and March 2017	FY2017 FY2017 FY2017 FY2017 FY2017 FY2017 FY2017 FY2017 FY2018 FY2019 (new project)
IMF work program in the next 12 months	• ECF second review • ECF third review • ECF fourth review • TA from FAD: o Tax policy (VAT) o Public financial management • TA from MCM: o Bank resolution and liquidation • TA from STA: o National accounts	September 2016 March 2017 September 2017 TBD TBD November 2016 January 2017	December 2016 June 2017 December 2017 FY2017 FY2017 November 2016 January 2017
B. Requests for work program inputs			
Fund request to Bank	• Information on Bank budget support operations and disbursement schedule	To support the 2016 –17 fiscal program	October 2016
Bank request to Fund	• Collaboration on providing full set of macroeconomic framework and tables		Ongoing

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of November 30, 2016)

1. São Tomé and Príncipe (STP) became a member of the African Development Bank Group (AfDB) in 1976. To date, the AfDB has financed 40 operations in the country. This comprises 30 projects, including institutional support, and 10 studies, for a total net commitment of UA 134 million under the African Development Fund (ADF) (98.9 percent), and one special support operation of UA 1 million under the Nigeria Trust Fund (NTF). The vast majority of these operations (94 percent) were financed through loans with the remaining 6 percent through grants.

2. As of November 30, 2016, the AfDB's ongoing portfolio comprised seven active projects for a total commitment of UA 26.51 million. These are the Infrastructure Rehabilitation for Food Security (PRIASA I); the Infrastructure Rehabilitation for Food Security (PRIASA II); the Public Finance Management Project (PAGEF); the National Planning Scheme Study; the Study on Water Supply and Sanitation Programme Rural; the Trade Facilitation Project (second phase of ASYCUDA); and the Payment System; (Table 1). The portfolio is relatively young. The average age of the ongoing portfolio is 2.6 years against 5.4 years recorded in 2011. Such improvement is mainly linked to new projects approved in the first quarter of 2013 and 2015. The portfolio's average disbursement rate stands at 29.5 percent, lower than the 31.7 percent reported in the last portfolio review conducted in 2014. In terms of sector distribution, agriculture contributes a substantial proportion, representing 63 percent of the total value of the portfolio, followed by multi-sector (34 percent) and water and sanitation (3 percent). There are no ongoing private sector or multinational projects.

3. The AfDB current involvement in STP is guided by the Country Strategy Paper (CSP) 2012–16, approved in July 2012. The CSP's main objective is to prepare the authorities for the forthcoming oil production era and the associated challenges and risks to the country's socio-economic development. A mid-term review of the strategy was concluded in 2014. During the review process the AfDB and the government agreed to add a second pillar in order to respond to the country's development needs. Therefore, the revised AfDB's strategy focuses on **Pillar I**—Strengthening Governance; and **Pillar II**—Promotion of Agriculture Infrastructure. Both pillars are consistent with the authorities' priorities as well as with the AfDB's priorities outlined in the 2013–2022 strategy, and the High 5 agenda. More specifically, the strategy aims at improving the capacity of key public administration institutions, including human resource development, country systems, and strategic legal and regulatory frameworks by the time the oil era begins. In addition, it will also help to address the issues of food security, job creation, transformation of local products and global value chains.

4. As part of its strategy and knowledge products, the AfDB also envisages to undertake the following economic and sector works: (i) the study on irrigation transformation; and (ii) the study on national planning scheme. The AfDB also concluded the private sector strategy 2015–2024 for STP. At the project level, the AfDB has completed the study on the cartography and selectivity of energy,

including network protection of EMAE, the electricity and water company); the study on the implementation of the EITI initiative in the fishery sector, the study on corruption in STP; and the study on the accreditation of the Technology and Agronomic Centre (CIAT) for STP. Conversely, the AfDB is also in the process of preparing/finalizing the following studies: (i) study on fiscal decentralization, introduction of VAT and fiscal revenue; and (ii) the study on telecommunication tariffs in STP. STP reached the Highly Indebted Poor Countries (HIPC) decision and completion points in 2000 and 2007, respectively. To this effect, the country became eligible for the MDRI with an estimated US$99.56 million in debt service according to the terms of the MDRI. The AfDB's total assistance under HIPC and MDRI amounted to US$187.92 million in debt relief. At the end of December 2008, the AfDB provided US$13.33 million in debt relief under HIPC and US$99 million under MDRI.

Table 1. AfDB Ongoing Projects (Millions of UA)

Title of Projects	Window	Commitment	Disbursement Rate (Percent)
PRIASA I	ADF Grant	5.0	92.63
PRIASA II	ADF Loan	11.5	5.13
Study on Water Supply and Sanitation Programme	RWSSI Trust Fund	0.7	67.63
PAGEF	ADF+FSF Grants	7.0	49.5
National Planning Scheme	ADF Loan	2.0	NA
Trade Facilitation Project	Trust Fund	0.35	25.75
Payment System	ADF Loan	1.5	NA
Total		***28.1***	***29.5 (Average)***

Source: African Development Bank.

STATISTICAL ISSUES

(As of November 30, 2016)

I. Assessment of Data Adequacy for Surveillance
General: Economic data are broadly adequate for surveillance. At the same time, serious financial, human, and technological resource constraints have slowed down efforts to strengthen the statistical system.
National Accounts: Statistics on GDP/GNP are compiled on a yearly basis and provided at the time of the Article IV consultation and program review missions. Weak source data affect the quality of national accounts estimates. The INE has started working on a new base year (2008). A technical assistance mission is planned in January 2017 to (i) further help in the rebasing exercise; (ii) assist the authorities to improve the flash GDP estimates based on high frequency indicators; and (iii) migrate the GDP series to an improved statistical platform that better captures survey and market information and includes estimates of the informal sector. The current GDP series (base year 2001) became available in mid–2011. Compared with the previous series, the revised ones reflect more accurately recent economic developments. While the revision of the GDP series represented a significant improvement, a number of shortcomings remain. Further improvements would require input from available administrative data sources, the recently completed household expenditure survey (rather than living conditions survey), using producer prices, and better estimates for agricultural production.
Consumer Price Statistics: The INE began to disseminate a new CPI (base: 2014 = 100) from January 2016. With the assistance of AFRISTAT, the product mix was changed and the weights were updated, using the results of a household expenditure survey conducted in 2010. Due to financial constraints, the new CPI only covers the capital city.
Government Finance Statistics: Detailed revenue and expenditure data are compiled and reported to AFR. The main areas that need to be strengthened are (i) monitoring of expenditures on projects financed by donors; and (ii) financing operations. All project loans financed by donors are programmed in the budget, but some are executed independently. The government has requested development partners to help in recording all external financing in the budget. The recording of financing operations and stocks is expected to improve since the debt data management capacity is expected to be strengthened. The 2010 government accounts were finalized and presented to the Court of Audit in June 2013 (the first time in over two decades that government accounts have been prepared and submitted). The authorities are working on the 2011 and 2012 government accounts, but preparing the latter using the accounting feature of SAFE-e has taken longer than expected, highlighting the need for additional technical assistance and training in this area.

Technical assistance in government finance statistics (GFS) was last provided through missions in 2004 and 2007, but there has been no TA in this area since then. These two missions helped the Ministry of Finance to compile and disseminate GFS for the budgetary central government in accordance with the *Government Finance Statistics Manual 2001 (GFSM 2001)*. The mission prepared bridge tables between national budget classification and GFSM 2001 classifications to be used to compile GFS for reporting to STA and AFR, as well as in Ministry of Finance policy work. The authorities have recently resumed reporting GFS data to STA and submitted a time series of summary annual GFS for 2002–2015, on a consistent basis. However, the data include significant statistical discrepancies between above-the-line and below-the-line data and there are discrepancies between GFS data reported to STA and fiscal data provided to AFR. Faster statistical progress is hampered by an inadequate accounting system; successive FAD missions aimed at improving public accounting have begun to address this issue.
Monetary and Financial Statistics: STA missions provided technical assistance on monetary statistics in December 2004, April/May 2006, June 2007 and September 2010. As a result, the accuracy and timeliness of the monetary data reported in the standardized report forms (SRF) for the central bank and the other depository corporations' data improved significantly. The BCSTP has resumed reporting monthly data to STA for the central bank and other depository corporations (ODCs) on a regular basis. The BCSTP monthly trial balance sheet is broadly adequate to compile monetary statistics in line with the *Monetary and Financial Statistics Manual and Compilation Guide (MFSMCG).* A new plan of accounts for ODCs was introduced in January 2010. The September 2010 mission reviewed the new plan of accounts for the financial system, and found it adequate for a proper classification, sectorization, and valuation of financial instruments, and in line with the methodology of the *MFSMCG*. However, the mission detected serious shortcomings in the information reported by some banks and an inconsistent approach in the way banks report to the BCSTP. Following the mission's recommendations, the BCSTP worked towards eliminating those problems. The central bank has begun to collect data from insurance companies that opened in the past few years. The asset sizes of insurance companies remain small enough not to warrant inclusion in monetary statistics at this time. The central bank produces a quarterly FSI table. MCM TA missions on banking supervision have helped expand the coverage of the table and improved the data quality. The additional information compiled could permit the beginning of stress testing exercises in the near future. STA contacted the BCSTP to receive FSI data on a regular basis according to the methodology of the *FSI Compilation Guide* for their posting on the IMF's website: after an initial exchange, the BCSTP stopped responding to STA's requests.

External Sector Statistics: The BCSTP compiles quarterly balance of payments (BOP) and international investment position (IIP) statistics consistent with the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)*. However, the data are submitted to STA on an annual basis.

The BCSTP conducts quarterly surveys to collect BOP and IIP data from the private nonfinancial sector and from the oil and gas sector. However, the response rates are low and the net errors and omissions figures are still very large.

There is room to improve the compilation of external sector statistics, particularly to improve timeliness and lower large errors and omissions. The BCSTP has worked to improve the compilation of financial transactions and IIP statistics. However, further work is needed to expand the coverage and ensure consistency between IIP and BOP data.

A June 2015 mission recommended improving coordination and data sharing among data-producing agencies, increasing staff dedicated to the compilation and collection of external sector statistics, and discussing with the Joint Development Authority the establishment of mechanisms for receiving regular data on production sharing agreement contracts. The National Petroleum Agency has started submitting regular data.

II. Data Standards and Quality

São Tomé and Príncipe has participated in the Fund's General Data Dissemination System (GDDS) since April 20, 2004. Currently, it is in its successor data dissemination initiative, eGDDS.

Democratic Republic of São Tomé and Príncipe: Table of Common Indicators Required for Surveillance

(As of November 30, 2016)

	Date of Latest Observation	Date Received	Frequency of Data[6]	Frequency of Reporting	Frequency of Publication
Exchange rates	Nov. 2016	Nov. 2016	D	D	D
International reserve assets and reserve liabilities of the monetary authorities[1]	Nov. 2016	Nov. 2016	D	D	D
International investment position	Jun. 2016	Oct. 2016	Q	Q	Q
Reserve/base money	Nov. 2016	Nov. 2016	D	D	D
Broad money	Sep. 2016	Nov. 2016	M	M	M
Central bank balance sheet	Oct. 2016	Nov. 2016	M	M	M
Consolidated balance sheet of the banking system	Sep. 2016	Nov. 2016	M	M	M
Interest rates[2]	Oct. 2016	Nov. 2016	M	M	M
Consumer Price Index	Oct. 2016	Nov. 2016	M	M	M
Revenue, expenditure, balance and composition of financing[3] – general government[4]	Oct. 2016	Nov. 2016	M	M	M
Revenue, expenditure, balance and composition of financing[3] – central government	Oct. 2016	Nov. 2016	M	M	M
Stocks of central government and central government-guaranteed debt[5]	Oct. 2016	Nov. 2016	Q	I	Q
External current account balance	2015	Sep. 2016	A	I	A
Exports and imports of goods	Oct. 2016	Nov. 2016	M	M	A
GDP/GNP[6]	2013	Mar. 2016	A	I	A
Gross external debt	Sep. 2016	Oct. 2016	Q	I	A

[1] Includes reserve asset pledged or otherwise encumbered as well as net derivative positions.
[2] Central bank's reference rate.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra-budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); not available (NA).

Statement by Mr. Sembene, Executive Director and Mr. Carvalho da Silveira, Advisor to the Executive Director on Democratic Republic of São Tomé and Príncipe

December 9, 2016

We thank staff for the productive policy dialogue maintained with the Sao Tomean authorities in the context of their economic program supported by the Extended Credit Facility (ECF).

Performance under the Program and Recent Economic Developments

São Tomé and Príncipe continues to make progress in the implementation of the ECF-supported program, thus strengthening further macroeconomic stability. Program performance, however, was uneven. On the one hand, two out of six performance criteria (PC) were missed, namely those related to the domestic primary balance and net international reserves. While the underperformance with regard to the domestic primary balance resulted primarily from expenditure overrun, the nonobservance of the PC on net international reserves was triggered by the delayed disbursement of external financing. On the other hand, indicative targets on new domestic arrears and tax revenue were met, while good progress was also made in the implementation of key structural reforms, with the completion of two out of three end-June 2016 structural benchmarks. The missed end-June structural benchmark on the automatic fuel price adjustment mechanism has now been implemented in November.

Despite the adverse external environment, economic activity remains broadly robust, helped by a strong performance of the tourist and cocoa sectors. In 2016, real GDP growth is projected to hover around 4 percent, slightly lower than initially forecasted due to the unanticipated shortfall in foreign-financed capital spending. Inflation is expected to remain around 5.5 percent, reflecting temporary food shortages and changes introduced to the CPI basket. The external position continues to be strong as gross international reserves remain adequate, as noted by staff.

In the fiscal sector, performance in the first half of 2016 was mixed. While domestic revenue mobilization was slightly stronger than projected, public expenditure overshot significantly program targets, so did the primary deficit. Nevertheless, the overall fiscal deficit was in line with program commitments on account of weaker privatization and externally-financed capital spending.

In the banking sector, capital adequacy ratios are broadly satisfactory. However, banks' profitability remained elusive as excess liquidity continued to be high and nonperforming loans on the rise, with Banco Equador accounting for a significant part. In this context, the central bank (BCSTP) took steps to overcome these structural impediments to the health of the banking system. In particular, it initiated the resolution of Banco Equador, cancelling its license and beginning court liquidation proceedings in line with the new banking resolution framework. In parallel, care was taken to protect small and non-connected depositors. The court has since officially ruled in favor of the liquidation and appointed a liquidator.

Economic Policies for the Rest of 2016 Onwards

Our Sao Tomean authorities remain fully committed to the objectives of the ECF-supported program. Going forward, they will focus on ensuring greater fiscal discipline, safeguarding financial sector stability, and advancing their ambitious structural reform program.

Fiscal Policy

To mitigate the impact of fiscal missteps that took place in the first half of 2016, the authorities will aim to ensure a more rigorous and disciplined budget execution, with a view to achieving the end-year program target for the domestic primary deficit and ensuring that public debt remains on a downward path. In this endeavor, stricter control will be exercised over spending on goods and services and treasury-financed capital.

At the same time, steps will be taken to strengthen public financial management. In this connection, the recently completed diagnostic study that was conducted with the assistance of AfDB will play a key role by helping include autonomous services and municipalities in the electronic information management system (SAFEe). The oversight has already been extended to the general inspection finance entity and they are working on extending oversight to the Court of Public Accounts. The authorities are also committed to the prompt implementation of a centralized framework for appraising and prioritizing capital expenditure projects (public investment management assessment framework—PIMA).

The authorities are determined to pursue their fiscal consolidation efforts, notably by boosting revenue mobilization. In this regard, they plan to submit the VAT legislation to the National Assembly while preparing changes to the income tax to maintain coherence in the tax system. In addition, the focus will be put on reforms aimed at developing human capital, improving working conditions, and strengthening fiscal operations.

The authorities of São Tomé and Príncipe reiterate their commitment to reduce fiscal risk and improve debt management. The introduction of the automatic fuel price adjustment mechanism will help to avoid accumulating domestic arrears. On debt management, the authorities will continue to pursue prudent debt management policies consistent with the need to preserve debt sustainability and upgrade the country's risk of debt distress rating from high to moderate risk. An updated medium term public debt management strategy has been submitted to the parliament together with the draft 2017 budget. Moreover, a new debt management performance assessment (DeMPA) was completed with the World Bank assistance.

Monetary Policy

To address excess liquidity in the banking system, the authorities agree with staff on the need to refine the liquidity forecasting and management tools. The central bank of São Tomé and Príncipe (BCSTP) will continue to closely cooperate with the treasury with a view to further

minimizing forecasting errors and improving the assessment of banks' liquidity needs.
To enhance liquidity management, the BCSTP is working towards developing the secondary market for government securities, creating conditions for long-term liquidity management, and promoting transparent public reporting of banks' audited financial statements.

Financial Sector Stability

Profitability in the banking sector continues to be challenging. Against this background, the BCSTP is taking steps to implement its strategy for reducing non-performing loans (NPLs). As a result, on-site supervision inspections were conducted, resulting in asset reclassifications and increases in provisions. Banks were also called for improving their credit risk evaluation and introduce asset quality reviews. Following these initiatives, the end-September financial sector indicators suggest that the NPLs ratio has slightly decreased relative to their recorded level at the beginning of the year although this is largely related to the exclusion of Banco Equador.

In order to strengthen the risk-based supervision practices, the BCSTP is implementing the policy recommendations drawn from MCM technical assistance and consistent with international best practices for supervision (Basel Core Principles). These include notably updating the legal and regulatory framework and adopting measures to establish an effective supervisory regime capable of maintaining a sound and secure banking system in São Tomé and Príncipe.
In addition, the BCSTP is working with the recently appointed Audit Board to ensure independent oversight of the audit mechanisms, internal controls, financial reporting, in line with the recommendations made by the September 2015 safeguards assessment.

Structural Reforms

The authorities are fully committed to operationalizing the 2030 Transformation Agenda, notably by prioritizing export diversification and cost competitiveness to support growth and external stability. The new 5–year National Development Plan is expected to be completed by end-December 2016 with support from the UNDP. The authorities are currently working with the World Bank to finalize a national export diversification strategy centered on sustainable tourism growth. In this context, in early October 2016, São Tomé and Príncipe hosted the forum of the Union of Exporters of the Community of Portuguese Speaking Countries (UE-CPLP). This event sought to identify business opportunities that could be explored through partnerships between economic agents in within Portuguese speaking communities. Likewise, the authorities will continue efforts to improve the supply and reduce the high cost of electricity, including through substitution to alternative and cheaper energy sources, reform of the state electricity company (EMAE), and move to a full cost recovery of electricity tariffs.

Concluding Remarks

Against the backdrop of a challenging environment, São Tomé continues to make inroads in advancing its reform agenda. With the election of new President who benefits from a strong majority in parliament, the authorities are now provided with an opportunity to accelerate their reform efforts. The recent introduction of the automatic fuel price adjustment mechanism, a politically difficult measure, is an illustration of their determination to reap the benefits of this welcome development.

In light of the above, we would greatly appreciate Directors' support for the second review under the ECF and the authorities' request for waivers for nonobservance and modifications of performance criteria.