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Guinea-Bissau: Letter of Intent, Memorandum of Economic and
Financial Policies, and Technical Memorandum of Understanding

November 16, 2010

The following item is a Letter of Intent of the government of Guinea-Bissau, which describes the policies that Guinea-Bissau intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Guinea-Bissau, is being made available on the IMF website by agreement with the member as a service to users of the [IMF](#) website.

LETTER OF INTENT

Bissau, November 16, 2010

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

Dear Mr. Strauss-Kahn,

1. This letter and the attached memorandum of economic and financial policies (MEFP) update and supplement our correspondence of March 11, 2010, describe performance under the government's economic program for 2010, and propose our economic program for 2011.
2. The government economic program, supported by a three-year Extended Credit Facility (ECF), is on track. All performance criteria through end-June 2010 have been observed, and structural benchmarks for the first review were met (see Tables 1 and 2 of the MEFP). Except for the indicative target on social and other priority spending, all quantitative targets for end-June have also been met. The government is determined to speed up implementation of its investment program and priority spending in line with available financing.
3. In view of this performance, the Government of Guinea-Bissau requests completion of the first review and the second disbursement under the ECF arrangement of SDR 2.414 million. Completion of the first review will help pave the way for Guinea-Bissau to reach the Heavily Indebted Poor Countries (HIPC) Initiative completion point in late 2010.
4. The attached MEFP articulates the economic policies the government intends to pursue during 2011, as well as the targets and objectives under the program (performance criteria and structural benchmarks are included in Tables 3 and 4 of the MEFP). The government's objectives continue to be achieving fiscal and external sustainability, reviving economic growth, reducing poverty, and making progress toward the Millennium Development Goals (MDGs). The policies elaborated in the MEFP are adequate to achieve the objectives of the ECF-supported program. However, if necessary, the government will adopt additional measures to achieve these objectives. It will consult with the Fund before adopting such measures or if there are changes in the policies contained in the MEFP, in accordance with the Fund's policies on such consultations.
5. In line with our commitment to transparency, we request the IMF to publish this letter of intent, the attached MEFP, the Technical Memorandum of Understanding, the staff report, and the HIPC completion point document.

Sincerely yours,

/s/

José Mario Vaz
Minister of Finance

ATTACHMENT I. MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES FOR 2011

I. INTRODUCTION

1. **This memorandum summarizes the progress achieved since the adoption of the ECF-supported program and describes the macroeconomic policies and structural reforms the government plans to implement in 2011.** The program objectives are unchanged: achieving fiscal and external sustainability, reviving economic growth, and making progress toward poverty alleviation and the Millennium Development Goals (MDGs). Policy priorities continue to focus on strengthening public finances; modernizing the public administration and rebuilding technical and policy implementation capacity; increasing access to social services and basic infrastructure; and developing the private sector.
2. **Program implementation has taken place against the background of the April 1 military incident.** Since then, the political situation has been stable. Spillovers to the functioning of the civilian government have been limited and the government ministries as well as the parliament are operating normally. Development partners continue to follow the resolution of the military incident closely, with implications for budget support.

II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE UNDER THE ECF-SUPPORTED PROGRAM

A. Recent Economic Developments

3. **Economic growth has been resilient.** Strong terms-of-trade gains more than offset a weather-related decline in cashew harvest. Higher exports had a positive impact on disposable income and domestic demand. Construction activity has been buoyant despite a delay in the government investment program. Overall, growth is expected to accelerate slightly to 3.5 percent in 2010, up from 3.0 percent in 2009.
4. **Shortfalls in budget support and uncertainty about its prospects led the government to contain spending below program levels, including social and other priority spending.** Guinea-Bissau received a quarter of the budget support expected during the first half of the year, resulting in a shortfall in financing of CFAF 8.4 billion. This shortfall was accommodated through a combination of higher revenues and lower expenditures, ultimately affecting social and capital spending. In July, the AfDB disbursed its budget support and the World Bank approved its budget support operation. For the year, the expected shortfall in budget support and financial assistance amounts to 3.2 percent of GDP (or CFAF 13.3 billion).
5. **Fiscal adjustment through June more than offset delays in donor support, reflecting strong revenue performance, lower current primary spending, and delays in investment spending.** End-June 2010 fiscal data show a domestic primary balance of 0.5 percent of GDP (about 2 percentage points of GDP higher than programmed).
 - **Revenues** were ½ percentage point of GDP above program driven by direct and indirect taxes, reflecting healthy economic activity and tighter controls at customs (DGA) and revenue administration (DGCI).

- **Expenditures** were kept below program. Spending in goods and services and capital investment were contained in light of delays in disbursement of donor support.
6. **Inflation is still projected to be within the WAEMU target of 3 percent for the region.** Private sector credit accelerated, reflecting the government's domestic arrears clearance with the commercial banks early in the year.
7. **The external current account excluding official transfers is expected to narrow moderately this year.** Exports benefited from sharp increases in the price of cashew, only partly offset by a drop in volume of cashew exports. Stable net remittances also helped contain balance of payments pressures.

B. Performance Under the ECF Program

8. **Fiscal performance has been satisfactory despite delays in the disbursement of external budget support, and all quantitative performance criteria (PCs) at end-June 2010 were met** (Table 1). Fiscal revenues were above target, with strong tax collection more than offsetting delays in the disbursement of fishing compensation (nontax revenue) by the EU. Except for the indicative target on social and priority spending, all quantitative targets for end-June have been met. Shortfalls in budget support and uncertainty about its prospects led the government to contain spending below program levels, including social and priority spending.
9. **All structural benchmarks have been met** (Table 2). The treasury committee became operational, and it is proving to be an effective tool in improving cash management. The committee includes the minister of finance, the secretary of state of the treasury, the secretary of state of fiscal affairs, the financial controller, and the general directors of the treasury and budget. The government has also approved and implemented norms that helped tighten the recourse to simplified spending procedures. As a result, the government managed to keep nonregularized expenditures (the so-called "DNTs") within program ceilings. In July, the data of the biometric census of the public administration was published. The Council of Ministers approved a law creating the legal framework for the "one-stop" shop. The treasury's accounting system under the government's financial management system (SIGFIP) became operational by end-August. The Automated System for Customs Data (ASYCUDA ++)) has been installed in Bissau with assistance from UNCTAD.
10. **Progress has been made implementing other structural reform measures.** To strengthen oversight and control over public procurement, the National Assembly passed a new procurement law in July establishing a central procurement unit and a public procurement regulatory authority. As part of government efforts to better disseminate information on budget execution, the government started publishing and releasing to parliament quarterly budget execution reports. On defense and security sector reform (SSR), laws governing reorganization of the armed forces, the police, and the national guard were approved by the National Assembly in June and published in September. The legal framework for a pension fund for the military and security forces was approved in June, with a view to be made operational once financing from development partners becomes available.

11. **The government is on track with the execution of its arrears clearance plan.** The plan includes addressing the 1974–99 arrears to the private sector, which have already been audited, and completing the audit of the 2000–07 arrears. In addition to the clearance of the arrears with the commercial banks at the beginning of the year, the government paid CFAF 3.5 billion (about 0.8 percent of GDP) in arrears clearance to the private sector in August 2010.

III. MACROECONOMIC OUTLOOK AND ECONOMIC POLICIES FOR 2011

A. Macroeconomic Outlook

12. **The government’s medium-term macroeconomic objectives are unchanged under the ECF-supported program:** (i) raise real growth to 4½ percent by program end, (ii) contain annual inflation below the WAEMU convergence norm of 3 percent, (iii) narrow the external current account gradually (excluding official transfers), and (iv) keep the domestic primary budget deficit below 4 percent of GDP annually through 2012.

13. **The 2011 macroeconomic outlook is projected to improve.** Economic growth is expected to accelerate to 4.3 percent, driven by a rebound in cashew production, increased activity in cashew nut processing, and rebuilding of infrastructure, especially roads, ports, electricity, and water. Stable cashew prices and remittances, stemming from an improved global environment, should help support domestic demand and a further narrowing of the external current account deficit.

14. **Inflation is expected to remain below the WAEMU convergence norm, supported by the CFA peg to the euro.** Monetary and exchange rate policy will continue to be pursued within the WAEMU framework.

B. Fiscal Policy

15. **The medium-term fiscal program will continue to aim at strengthening fiscal policy and achieving debt sustainability.** The strategy seeks to reinforce revenue collection—low by regional standards—and make space for priority spending. The government will continue to address domestic arrears in line with available resources. The fiscal program reduces the domestic primary deficit gradually. This, combined with HIPC/MDRI debt relief, will improve fiscal and debt sustainability while limiting reliance on external budget support.

16. **The government is adjusting its fiscal plans for 2010 to address the expected shortfall in budget support** (3.2 percent of GDP). The adjustment is driven by several considerations: budget execution through August 2010 and preservation of priority spending and deposits at the BCEAO. Measures consist of higher revenues and lower spending in goods and services (by about 1 percentage point of GDP); underexecuting the budget for domestically financed capital spending by about 1½ percentage points of GDP; and drawing on government deposits at the BCEAO to raise domestic financing (by about ¾ percentage point of GDP). If budget support is higher than envisaged in the program, the government is

committed to using resources to restore spending in the priority areas of infrastructure, agriculture, health, and education, as well as rebuilding deposits at the BCEAO.

17. **The 2011 budget will implement strong measures and will be consistent with available financing.** It will target a domestic primary budget deficit of 1.7 percent of GDP, consistent with domestic primary spending of CFAF 55.3 billion and budget support of about CFAF 7.5 billion, without adding to Guinea-Bissau's debt problem. On the revenue side, the government will raise the reference price for cashew exports to US\$ 750 per ton and for imports that need valuation adjustments (rice to CFAF 6000, sugar to CFAF 8500, and flour to CFAF 8500) and increase the tax rate on advance payment of profit tax (ACI) from 3 to 5 percent for the informal sector. On the spending side, the government will freeze wages while incorporating contractual workers in the health and education sector in the wage bill. Budget support is expected from the AfDB and the World Bank. The residual financing gap of CFAF 3.5 billion is expected to be filled by the ECF. The government will submit the 2011 budget to the National Assembly consistent with these parameters. In the event that budget support is higher, the government will restore its public investment program (PIP) and increase other priority spending.

18. **The government will continue to address domestic arrears in line with the medium-term strategy under the ECF.** For 2011, it will carefully monitor budget execution and available resources before carrying out its plan of paying a total of CFAF 1.85 billion. The government will also complete the audit of the arrears of 2000–07.

C. Structural Reforms

19. **The government's program will continue to center on strengthening revenue collection; improving public financial management; modernizing the public administration and creating space for priority spending; removing impediments to private sector development; improving access to social services; and reinforcing debt management.**

(i) Strengthening Revenue Collection

20. **A major source of fiscal imbalances in Guinea-Bissau is the low level of revenue compared with other Sub-Saharan African countries, including countries in WAEMU.** Revenue depends heavily on tax collection at customs (export and import duties, as well as sales taxes on imports). Measures to mobilize revenue focus partly on improving customs administration, especially import processing and customs clearance, and the tax base also needs broadening.

21. **To achieve its revenue collection targets, the government will modify customs and tax policy to enhance revenue collection and broaden the tax base.** The government plans to (i) start raising the reference prices for customs purposes of certain imports toward market values in the 2011 budget; (ii) raise the reference price for cashew exports; (iii) increase the tax rate on the advance payment of the profit tax collected at customs (anticipation of industrial contribution); and (iv) start preparing for a transition from the general sales tax to the VAT, similar to other WAEMU countries. The government will

request technical assistance from development partners on tax policy, possibly through a resident advisor.

22. To continue modernizing and improving customs and tax administration, the government will

- On customs, (i) reintroduce seals on alcoholic beverages and tobacco to combat smuggling (by January); (ii) customize and test the system of ASYCUDA ++ with the parameters for Guinea-Bissau and train staff with the help of UNCTAD (by August); and (iii) conduct a comprehensive review of all customs exemptions to further broaden the customs revenue base, submitting a report to Council of Ministers (by June).
- On tax administration, (i) revise taxpayer segmentation based on turnover criteria, with thresholds for small and large taxpayers at CFAF 10 and 40 million, respectively (by June); (ii) cross-check ASYCUDA ++ data with tax returns for 300 largest importers in 2009-10 (by June); (iii) audit importers underreporting tax liabilities, beginning with largest gaps (by December); (iv) increase to 90 percent large taxpayers filing rate for the general sales tax; and (v) continue to reinforce the large taxpayer unit in the Ministry of Finance to ensure compliance with tax declarations. Measures (i), (ii), and (iii) are prerequisites for preparing an action plan for the VAT in line with recommendations from the Fund's fiscal affairs department (FAD).

(ii) Improving Public Expenditure and Financial Management

23. The government will continue to implement its public financial management (PFM) action plan. Measures will focus on bettering budget planning, improving predictability and control in budget execution, strengthening reporting procedures, and reinforcing internal and external controls.

Bettering budget planning

- The government will review the legal framework that regulates revenue sharing agreements ("restitutions") to increase the share of non earmarked revenues in the budget, and will submit a proposal to the Council of Ministers (by December 2011). The review will include all restitutions between the collecting ministries (including allocated revenue from fishing, mining, and forestry; and administrative revenue such as revenue from passports) and the treasury.
- The government will seek technical assistance from development partners to reinforce budget preparation procedures.

Improving predictability and control in budget execution

- To ensure adequate cash management, the treasury committee in the Ministry of Finance will prepare and regularly update the treasury plan for the 2011 budget.
- To improve financial management the government will establish an operational link form budget/treasury under the SIGFIP to the customs and tax administration (by March 2011).

Strengthening reporting procedures

- The government will continue publishing quarterly budget execution reports, and send detailed budget execution reports to all sovereign institutions.

Reinforcing internal and external controls

- The government will modify the organic law for the Audit Court to harmonize it with the WAEMU directives. It will submit to the Court of Accounts the budgetary execution accounts of 2010 (by September 2011).

(iii) Modernizing the Public Administration and Creating Space for Priority Spending

24. **The government will launch a gradual civil service reform program to achieve a more modern, efficient civil service.** The minister of labor and public administration is preparing a plan to submit to the Council of Ministers by January 2011. The plan will (i) include a medium-term schedule with annual targets to gradually downsize the civil service through mandatory retirement and removal of redundant workers and (ii) increase the efficiency of public administration by upgrading the qualifications and working conditions for civil servants. The government will use savings in the wage bill to help cover the cost of severance payments.

25. **The government is working to implement stricter payroll controls and establish a more comprehensive payroll database.** This will allow for adequate control, regular updating, and verification of civil service employment. By January 2011, the government will start using the computerized and unified payroll and personnel management system in the Ministries of Finance and Labor and Public Administration. The system will be extended to all ministries by August 2011.

26. **The government continues to work with development partners to modernize defense and security sectors.** The government is preparing an operational plan with a list of potential retirees and projects for the construction of military and security installations. The government will facilitate donor coordination with the participation of ECOWAS, CPLP, the UN, and other development partners. Financing will be needed for the pension fund.

(iv) Removing Impediments to Private Sector Development

27. **The government program to remove impediments to private sector development has three main objectives:** (i) improve the business environment; (ii) restore and develop basic power, transportation, and communication infrastructures; and (iii) start managing the country's natural resources.

28. **To improve the business and investment environment, the government will**

- Adopt the implementing regulations of the new investment code, which removes the multiplicity of investment regimes, eliminates the discretion of granting incentives under the old law, and provides a level playing field for private investors.

- Prepare an action plan to further identify and remove impediments to private sector development and improve the ease of doing business in Guinea-Bissau (by August).

29. **As part of its new strategy for growth and poverty reduction, the government identified areas where investments are most promising in terms of medium-term growth.** These consist of sectors where the country has comparative advantage, such as agriculture and fishery, or sectors that constitute a significant constraint on growth, energy, transport and the port. The government is working with the World Bank to reactivate electricity generation and distribution installations in Bissau and will develop a sectoral strategy to promote alternative domestic energy sources. The government will coordinate closely with the BOAD and other development partners, with a view to improve roads connecting Bissau to neighboring countries and provide access to production areas. The construction of a fishing port should be ready by 2011.

30. **The government wants to exploit mineral deposits and other natural resources over the medium term.** Such resources could contribute to foreign exchange earnings and tax revenues, and enhance the country's overall financial position, thus helping reduce poverty. The government will prepare a plan to manage the country's natural resources by December 2011. This plan will help ensure that as preparatory work are undertaken in these areas, transparent and accountable practice will be followed in the mining, oil, and gas sectors, including dealing with the environmental impact of the development of mineral deposits. The plan would also include the feasibility studies of needed infrastructure such as the deep water port for developing bauxite deposits and roads for the phosphate deposits.

(v) Improving Access to Social Services

31. **The government aims to make further progress toward addressing high rates of poverty.** The government will adopt a new five-year poverty reduction strategy (PRS) that incorporates the lessons learned in implementing the 2007 PRS (by December 2010). Increasing per capita income and reducing the incidence of poverty will require efforts on several fronts, including improving access to basic services (health and education) and agricultural development because most of the poor live in rural areas and practice subsistence agriculture.

(vi) Reinforcing Debt Management

32. **The government plans to improve debt management by**

- Strengthening the unit of public debt management;
- Producing quarterly electronic reports on public debt (external and domestic) no later than three months after each quarter, in a manner consistent with the BCEAO reporting requirements, with the first report to be published by June 2011; and
- Using the Debt Management Financial and Analysis System (DMFAS; SYGADE in French) to record, monitor, and manage all public debt (external and domestic) by December 2011.

33. **The government will pursue a prudent debt management strategy.** The government will not contract or guarantee any nonconcessional or short-term external debt, as defined in the Technical Memorandum of Understanding (TMU). Moreover, any government or government-guaranteed borrowing (external or domestic) will be subject to prior approval by the finance minister.

D. Financial Sector and Monetary Policies

34. **Monetary policy will continue to be pursued within the WAEMU framework.** This arrangement has enabled the country to contain inflation and maintain a stable exchange rate.

35. **Access to credit is still low.** Much work is still needed in the area of contract enforcement. To strengthen legal rights the government will provide resources to allow the commercial tribunal to function. The government will seek donor support for setting up a credit bureau and a collateral registry. The government's arrears clearance strategy will continue to improve the liquidity of the private sector.

E. Reaching the HIPC Completion Point

36. **The government is committed to reach the HIPC completion point by end-2010.** The government has implemented all but one completion point trigger and is requesting a waiver for lack of continuous implementation of one trigger. The triggers that have been implemented are (i) a track record of satisfactory macroeconomic performance lasting at least six months, which will coincide with the first review of performance under the ECF; (ii) a satisfactory record of PRS implementation for at least one year, as shown by a joint WB-IMF staff assessment of the country's annual progress report (APR); (iii) better outcomes in the areas of health, education, and demobilization; and (iv) reforms in the area of governance, including the external audit of the 1997–99 budget outturns and the reform of the public procurement system. The government is requesting a waiver for lack of continuous publication of comprehensive budget execution reports since 2001. In 2010, the government started publishing quarterly budget execution reports and submitted the general administrative accounts for FY2009 to the Court of Accounts by end-September 2010.

37. **The government is seeking to normalize relations with all creditors in a manner consistent with the country's debt service capacity and consistent with the HIPC initiative.** The government has already received HIPC financing assurances from creditors representing over 80 percent of HIPC eligible debt and will continue to seek maximum participation in the HIPC initiative beyond the minimum threshold of 80 percent.

F. Statistics

38. **The government plans to better disseminate data.** It will publish national account data for 2009 this year, based on the SNA93, and will continue to publish WAEMU harmonized consumer price index.

G. Capacity Building and Technical Assistance

39. **Capacity building will be needed to ensure effectiveness and sustainability of fiscal reforms.** In the Ministry of Finance, the highest priorities are: customs, treasury, budget, and tax and financial control departments. The IMF is providing technical support, including technical assistance from FAD and West AFRITAC, in public financial management, revenue administration, and national accounts statistics.

H. Program Monitoring

40. **While the underlying objectives of the program remain unchanged, it has become necessary to modify the indicative target on social and priority spending for end-December 2010 because of a shortfall in budget support** (Table 1). All other quantitative indicators and all performance criteria remain unchanged.

41. **The second year of the program covers the 12 months from January 1, 2011, to December 31, 2011.** The program will be monitored using quarterly quantitative indicators and structural benchmarks, as well as semiannual reviews and the quantitative performance criteria presented in Table 3. Tables 4 and 5 contain a list of structural measures identified by the government. The definitions of quantitative performance criteria and benchmarks are in the attached TMU. We expect the second review to take place in May 2011 and the third review in November 2011.

Table 1. Guinea-Bissau: Quantitative Indicators for the ECF Program for 2010

Quarterly Targets ¹
(Cumulative, CFAF millions)

	End-March			End-June			End-Sept.	End-Dec.
	Prog.	Prog. ²	Actual	Prog.	Prog. ²	Actual	Prog.	Prog.
Performance criteria³								
1. Domestic financing of the budget	7,165	10,618	5,975	-1,411	8,627	302	3,430	231
2. New domestic arrears	0	0	0	0	0	0	0	0
3. External nonconcessional public borrowing, maturity > 1 year	0	0	0	0	0	0	0	0
4. External short term public borrowing	0	0	0	0	0	0	0	0
5. New external payment arrears	0	0	0	0	0	0	0	0
Indicative targets								
6. Government tax revenues	5,420	5,420	6,392	15,148	15,148	17,539	24,218	30,101
7. Domestic primary balance (commitment basis)	-7,789	-7,789	-1,497	-6,779	-8,386	1,895	-11,030	-16,333
8. Nonregularized expenditures (DNTs)	200	200	67	200	200	123	200	200
9. Social and priority spending	4,062	4,062	1,989	8,123	8,123	4,223	12,185	8,647 ⁴

¹ Cumulative from January 1. The definition of the aggregates and adjustors is provided in the Technical Memorandum of Understanding (TMU).

² Adjusted target under the program.

³ Performance criteria (PC) are defined for June and December. March and September are indicative. All performance criteria (PC) are ceilings and PC 3, 4 and 5 apply continuously.

⁴ Indicative target for social and priority spending is adjusted from CFAF 16,246 to CFAF 8,647.

Table 2. Guinea-Bissau: Structural Benchmarks Under the ECF
January 1, 2010–December, 31, 2010

Category	Structural Benchmarks	Macro Rationale	Actual Delivery Date	Ministry	Status of Implementation
First Review					
Fiscal management	1 Prepare quarterly and monthly treasury plans and make the treasury committee operational within the Ministry of Finance.	To improve budget planning	June 2010	MoF ¹	Met
	2 Implement norms tightening the recourse to simplified spending procedures.	Greater control in budget execution	May 2010	MoF	Met
	3 Make the accounting system operational at the treasury under the SIGFIP.)	Greater control in budget execution	August 2010	MoF	Met
Tax reform and strengthening revenue collection	4 Put into operation ASYCUDA ++ in three customs posts (Bissau, airport, Safim).	To strengthen revenue collection	Sep 2010	MoF	Met
Expenditure reforms	5 Publish the verified data of the biometric census of public administration employees (civil servants and paramilitary).	To improve civil servant management	July 2010	MinLaPS ²	Met
Business environment	6 The Council of Ministers will approve a legal framework for the "one-stop" shop, streamlining procedures and reducing costs for licensing and registration of new businesses.	Improve the ease of doing business	March 2010	MinEcon ³	Met.

¹ Ministry of Finance

² Ministry of Labor and Public Administration

³ Ministry of Economy

Table 3. Guinea-Bissau: Quantitative Indicators for the ECF Program for 2011

Quarterly Targets ¹
(Cumulative, CFAF millions)

	End-March	End-June	End-Sept.	End-Dec.
	Prog.	Prog.	Prog.	Prog.
Performance criteria²				
1. Domestic financing of the budget	1,431	-520	-1,954	0
2. New domestic arrears	0	0	0	0
3. External nonconcessional public borrowing, maturity > 1 year	0	0	0	0
4. External short term public borrowing	0	0	0	0
5. New external payment arrears	0	0	0	0
Indicative targets				
6. Government tax revenues	6,437	17,988	28,759	35,745
7. Domestic primary balance (commitment basis)	-1,039	-449	-2,473	-7,579
8. Nonregularized expenditures (DNTs)	200	200	200	200
9. Social and priority spending	2,932	5,864	8,795	11,727

¹ Cumulative from January 1. The definition of the aggregates and adjustors is provided in the Technical Memorandum of Understanding (TMU).

² Performance criteria (PC) are defined for June and December. March and September are indicative. All performance criteria (PC) are ceilings and PC 3, 4 and 5 apply continuously.

Table 4. Guinea-Bissau: Structural Benchmarks Under the ECF
January 1, 2011–December 31, 2011

Category		Structural Benchmarks	Macro Rationale	Delivery Date	Ministry
Second Review					
Fiscal management	1	Establish an operational link from budget/treasury under the SIGFIP to the customs and tax administration.	Greater control in budget execution	March 2011	MoF ¹
Expenditure reforms	2	Submit to the Council of Ministers an action plan for public administration reform, with a medium-term schedule to downsize the civil service through retirement and removing redundant workers beginning in 2011.	To improve the efficiency of civil service	Jan 2011	MoF MinLaPS ²
	3	Start using the unified payroll and personnel management system and pilot it in the Ministries of Finance and Labor and Public Administration.	To modernize public administration	Jan 2011	MoF MinLaPS ²
Third Review					
Tax reform and strengthening revenue collection	1	Customize and test ASYCUDA ++, and provide training to staff.	To strengthen revenue collection	August 2011	MoF
	2	Conduct a comprehensive review of all customs exemptions to broaden the customs revenue base and submit report to Council of Ministers.	To strengthen revenue collection	June 2011	MoF
	3	Cross-check SYDONIA data with tax returns for 300 largest importers in 2009–10.	To strengthen revenue collection	June 2011	MoF
Expenditure reforms	4	Extend the computerized and unified payroll and personnel management system to all ministries.	To modernize public administration	August 2011	MoF MinLaPS ²
Business environment	5	Prepare an action plan to identify and remove further impediments to private sector development and improve the ease of doing business in Guinea-Bissau.	Improve the ease of doing business	August 2011	MinEcon ³
Public debt management	6	Start producing, on a quarterly basis, electronic reports on public debt (external and domestic).	Improve transparency	June 2011	MoF

¹ Ministry of Finance

² Ministry of Labor and Public Administration

³ Ministry of Economy

Table 4. Guinea-Bissau: Structural Benchmarks Under the ECF (concluded)
January 1, 2011–December 31, 2011

Fourth Review					
Public debt management	1	Use SYGADE to record, monitor, and manage all public debt (external and domestic)	Improve debt management	Dec 2011	MoF ¹
Tax reform and strengthening revenue collection	2	Audit those importers underreporting their tax liabilities, beginning with largest gaps.	To strengthen revenue collection	Dec 2011	MoF
	3	Review the legal framework that regulates revenue sharing agreements ("restitutions").	To strengthen revenue collection	Dec 2011	MoF
Business environment	4	Prepare a plan to manage the country's natural resources.	Improve the ease of doing business	Dec 2011	MinEcon ²

¹ Ministry of Finance

² Ministry of Economy

Table 5. Guinea-Bissau: Structural Measures for 2011

Category	Measures	Delivery Date
Tax reform & strengthening revenue collection	1 Raise reference price for cashew exports to US\$750 per ton. (¶17)	2011
	2 Raise the reference price for staple imports (rice to CFAF 6000, sugar to CFAF 8500, and flour to CFAF 8500). (¶17)	2011
	3 Increase the tax rate on advance payment of the profit tax collected at customs (anticipation of industrial contribution) from 3 to 5 percent for the informal sector. (¶17)	2011
	4 Reintroduce seals on alcoholic beverages and tobacco. (¶22)	Jan 2011
	5 Customize and test the system of ASYCUDA ++ with the parameters for Guinea-Bissau (including the specific exemptions and tariffs), and train staff. (¶22)	Aug 2011
	6 Conduct a comprehensive review of all customs exemptions. (¶22)	Jun 2011
	7 Revise taxpayer segmentation based on turnover criteria, with threshold for small and large taxpayers at CFAF 10 and CFAF 40 million, respectively. (¶22)	Jun 2011
	8 Cross-check SYDONIA data with tax returns for 300 largest importers in 2009–10. (¶22)	Jun 2011
	9 Audit importers underreporting tax liabilities, beginning with largest gaps. (¶22)	Dec 2011
	10 Increase to 90 percent large taxpayers filing rate for the general sales tax. (¶22)	2011
	11 Continue to reinforce the large taxpayer unit in the Ministry of Finance. (¶22)	2011
Fiscal management	12 Review the legal framework that regulates revenue sharing agreements (“restitutions”) to increase the share of non earmarked revenues in the budget. (¶23)	Dec 2011
	13 Seek technical assistance to reinforce budget preparation procedures. (¶23)	Jun 2012
	14 Prepare and regularly update the treasury plan for the 2011 budget. (¶23)	2011
	15 Establish an operational link form budget/treasury under the SIGFIP to the customs and tax administration. (¶23)	Mar 2011
	16 Continue publishing quarterly budget execution reports. (¶23)	2011
	17 Modify the organic laws for the Audit Court. (¶23)	2011
	18 Submit to the Court of Accounts the budgetary execution accounts for 2010. (¶23)	Sep 2011
Civil service reform	19 Submit to the Council of Ministers an action plan for public administration reform, with a medium-term schedule to downsize the civil service through retirement and removing redundant workers beginning in 2011. (¶24)	Jan 2011

	20 Start using the computerized and unified payroll and personnel management system in the Ministries of Finance and Labor and Public Administration. (¶25)	Jan 2011
	21 Extend the computerized and unified payroll and personnel management system to all ministries. (¶25)	Aug 2011
Defense and security sector reform	22 Prepare an operational plan with a list of potential retirees and projects for the construction of military and security installations. (¶26)	2011
Arrears clearance	23 Complete the audit of 2000–07 private sector arrears. (¶18)	2011
Business environment	24 Adopt the implementing regulations of the new investment code. (¶28)	2011
	25 Prepare an action plan to further identify and remove impediments to private sector development and improve the ease of doing business in Guinea-Bissau. (¶28)	Aug 2011
	26 Prepare a plan to manage the country's natural resources. (¶30)	Dec 2011
Social services	27 Adopt a new five-year poverty reduction strategy (PRS). (¶31)	Dec 2010
Public debt management	28 Strengthen the unit of public debt management. (¶32)	2011
	29 Produce quarterly electronic reports on public debt no later than three months after each quarter, in a manner consistent with BCEAO reporting requirements. (¶32)	Jun 2011
	30 Use SYGADE to record, monitor, and manage all public debt. (¶32)	Dec 2011

ATTACHMENT II. TECHNICAL MEMORANDUM OF UNDERSTANDING

Bissau

November 16, 2010

1. **This memorandum describes the definitions of the quantitative and structural performance criteria, indicative targets, and structural benchmarks to monitor the program supported by an arrangement under the Extended Credit Facility (ECF).** It also specifies the agreed periodicity and deadlines for transmission of data to IMF staff for program monitoring.

Quantitative Indicators and Adjustors

A. Quantitative Indicators

2. **The quantitative indicators are as follows:**
- a. Cumulative floors on government tax revenue
 - b. Cumulative ceilings on the domestic primary fiscal deficit (on a commitment basis)
 - c. Cumulative ceiling on the amount of nonregularized expenditures (DNTs).
 - d. Cumulative floor on social and other priority spending
 - e. Cumulative ceilings on the change in net domestic financing of the budget
 - f. Cumulative ceiling on new domestic arrears of the government, including wage arrears
 - g. Cumulative ceilings on new nonconcessional external debt contracted or guaranteed by the government
 - h. Cumulative ceiling on new external short term debt
 - i. Cumulative ceiling on new external payment arrears.

Quantitative indicators are set for end-March, end-June, end-September, and end-December. Quantitative performance criteria are proposed for end-June and end-December 2011 for indicators (e) through (i). Indicators for new nonconcessional external debt, new external short-term debt, and new external payment arrears are continuous.

Definitions and computation

3. **For program purposes the government is defined as the central government of Guinea-Bissau.** This definition excludes public entities whose budget is not included in the central government budget.
4. **The targeted floor on government tax revenues** includes direct and indirect taxes, as well as recovery of tax arrears and additional revenue efforts (Table 1).

Table 1. Quarterly Floors for Government Tax Revenues, 2011
(Cumulative, CFAF millions)

	March Prog.	June Prog.	Sept. Prog.	Dec. Prog.
Tax revenues	6,437	17,988	28,759	35,745

5. **The domestic primary fiscal deficit on a commitment basis** is calculated as the difference between government revenue and domestic primary expenditure on a commitment basis (Table 2). Government revenue includes all tax and nontax receipts and excludes external grants. Domestic primary expenditure consists of current expenditure plus domestically financed capital expenditure, excluding all interest payments. Government commitments include all expenditure for which commitment vouchers have been approved by the Ministry of Finance; automatic expenditure (such as wages and salaries, pensions, utilities, and other expenditure for which payment is centralized); and expenditure by means of offsetting operations.

Table 2. Quarterly Domestic Primary Balance, New Domestic Arrears,
and Nonregularized Expenditures, 2011
(Cumulative, CFAF millions)

	March Prog.	June Prog.	Sept. Prog.	Dec. Prog.
Total domestic primary deficit	-1,039	-449	-2,473	-7,579
Revenue	8,161	21,436	38,978	47,688
Domestic primary expenditure	9,199	21,886	41,450	55,267
New domestic arrears	0	0	0	0
Nonregularized expenditures (DNTs)	200	200	200	200

6. **New domestic arrears of the government** are defined as accounts payable (rest-a-payer) accumulated during the year, still outstanding one month after the quarter for wages and salaries (including pensions), and three months after for goods and services and transfers, at end-March, end-June, end-September, and end-December 2011.

7. **Nonregularized expenditures** are defined as any treasury outlay not classified in the expenditure tables presented by the National Budget Directorate.

8. **Net domestic financing consists of bank and nonbank financing** (Table 3). Bank financing consists of net changes in the balances of the treasury accounts at the BCEAO (excluding net disbursement from the IMF) and commercial banks (excluding balances in those accounts that are not available for budget financing, such as accounts held under double signature arrangements with donors) and in the outstanding amounts of loans, including T-bills, from the BCEAO and commercial banks, local and regional. Nonbank financing encompasses privatization receipts and any other financial debt held outside the banking system other than new domestic arrears.

Table 3. Domestic Financing by Quarter, 2011
(Cumulative, CFAF millions)

	March	June	Sept.	Dec.
	Prog.	Prog.	Prog.	Prog.
Domestic financing	1,431	-520	-1,954	0
Bank financing	1,431	-520	-1,954	0
BCEAO	1,431	-520	-1,954	0
Commercial banks (including regional)	0	0	0	0
Regional commercial banks and Treasury bills	0	0	0	0
Nonbank financing	0	0	0	0

9. **The cumulative ceilings on new nonconcessional external debt apply to debt contracted or guaranteed by the government.** External debt is defined as debt held by creditors outside the WAEMU region. For ECF purposes, the definitions of “debt” and “concessional borrowing” are as follows:

- a. **The indicator for external borrowing** applies to debt including commitments contracted or guaranteed for which value has not been received. The term “debt” is understood to mean a current liability, not contingent, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services that requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s); these payments will discharge the principal and interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being (i) loans, that is, advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers credits) and temporary exchanges of assets equivalent to fully collateralized loans, under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers’ credits, that is, contracts where the supplier permits the obligor to defer payments until a time after the date on which the goods are delivered or services are provided; and (iii) leases, that is, arrangements under which property is provided that the lessee has the right to use for one or more specified periods, usually shorter than the total expected service life of the property, while the lessor retains the title to the property. The debt is the present value at the inception of the lease of all lease payments expected to be made during the period of the agreement, excluding those that cover the operation, repair, or maintenance of the property. Under this definition of debt, arrears, penalties, and judicially awarded damages arising from failure to make payment on a contractual obligation that constitutes debt are also debt. Failure to make payment on an obligation that is not considered debt under this definition (for example, payment on delivery) will not give rise to debt. For monitoring the ECF, arrangements to pay over time obligations arising from

judicial awards to external creditors do not constitute nonconcessional external borrowing.

- b. **Debt concessionality**, for program purposes, is assessed based on its calculated grant elements. A debt is concessional if it includes a grant element of at least 50 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rates used for this purpose are the currency specific commercial interest reference rates (CIRRs), published by the Organisation for Economic Cooperation Development (OECD). For debt with a maturity of at least 15 years, the 10-year-average CIRR is used to calculate the PV of debt and hence, its grant element. For debt with a maturity of less than 15 years, the six-month average CIRR is used. To both the 10-year and six-month averages, the same margins for differing repayment periods as those used by the OECD need to be added (0.75 percent for repayment periods of less than 15 years, 1 percent for 15 to 19 years, 1.15 percent for 20 to 29 years, and 1.25 percent for 30 years or more).

10. **Ceiling on short-term external debt newly contracted or guaranteed by the government.** Short-term external debt is debt with the contractual term of less than one year. Debt-relief operations and treasury bills issued in CFA francs on the WAEMU regional market are excluded from this performance criterion. In the context of the program, the government and public enterprises will not contract, or guarantee, short-term external debt. This performance criterion is monitored on a continuous basis.

11. **Ceiling on new external payment arrears.** External payment arrears are defined as external payments due but not paid on the due date. In cases where a creditor has granted a grace period after the contractual due date, arrears are incurred following the expiration of the grace period. Under the program, the government undertakes not to accumulate arrears on its external debt, except those arising from government debt that is being renegotiated with creditors, including non-Paris Club bilateral creditors. This performance criterion is monitored on a continuous basis.

12. **The concept of government for the external debt is broader than the one used for the budget aggregates;** it includes all debt that may ultimately be deemed to be a liability of the state. In addition to the central government, the definition includes administrative public institutions; public enterprises authorized to contract, guarantee, or accommodate nonconcessional borrowing; scientific and technical public institutions; professional public institutions; industrial and/or commercial public institutions; and local governments.

13. **Social and other priority spending** is defined as total current expenditures in the education, health, and agricultural sector, and domestically financed capital spending (Table 4).

Table 4. Social and Priority Spending¹ by Quarter, 2011
(Cumulative, CFAF millions)

	March	June	Sept.	Dec.
	Prog.	Prog.	Prog.	Prog.
Social and other priority spending	2,932	5,864	8,795	11,727
Education	1,649	3,299	4,948	6,598
Health	897	1,794	2,691	3,588
Agriculture	264	527	791	1,055
Infrastructure	122	244	365	487

¹ Current and domestically financed capital spending.

B. Adjustors

14. The following adjustors will be in effect:

- a. The ceiling on the domestic primary deficit (on a commitment basis) will be increased in case of lower than programmed disbursement of fishing compensation, by the amount of the shortfall up to a maximum of CFAF 3 billion. The program assumes the following amounts of fishing compensation (cumulative from January 1, 2011): zero by end-March; zero by end-June; by end-September CFAF 5 billion; and by end-December CFAF 5 billion.¹
- b. The ceiling on domestic financing will be increased for any shortfall in external budget support, and fishing compensation, by the amount of the shortfall up to a maximum of CFAF 3.5 billion. The program assumes the following amounts of external budget support, and fishing compensation (cumulative from January 1, 2011): zero by end-March; zero by end-June; by end-September CFAF 8.9 billion; and by end-December CFAF 12.5 billion.
- c. The ceiling on domestic financing for March, June, and September will be increased for payment of previous years arrears in excess of programmed amounts up to a maximum of CFAF 1.85 billion. The program assumes the following arrears payments from previous years (cumulative from January 1, 2011): zero by end-March; zero by end-June CFAF; zero by end-September; and by end-December CFAF 1.85 billion.

¹ For this TMU, the CFAF/euro exchange rate is 655.956 and the CFAF/US\$ exchange rate is 524.