International Monetary Fund

Burkina Faso and the IMF

Press Release:
IMF Executive Board Completes Sixth Review Under Burkina Faso's PRGF Arrangement, Request for Waivers of Performance Criteria, Augmentation of Access and Approves US$14.0 Million Disbursement
September 8, 2005

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Burkina Faso: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

August 25, 2006

Ouagadougou
August 25, 2006

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
700 19th Street NW
Washington, DC 20431
USA

Mr. de Rato:

1. The government of Burkina Faso has successfully implemented the measures contained in its economic program implemented with the support of the International Monetary Fund through its Poverty Reduction and Growth Facility. The program, which was approved by the IMF Board on June 11, 2003 for an amount equivalent to SDR 24.08 million (40 percent of quota), runs through September 2006.

2. The attached memorandum of economic and financial policies (MEFP) supplements the one attached to my letter to you dated February 27, 2006. The MEFP attached to that letter established quantitative performance criteria (for end-March 2006) and structural performance criteria (through mid-May 2006) for the completion of the sixth and final review under the PRGF arrangement.

3. All quantitative performance criteria for the completion of the sixth review were observed. We met one of the three structural performance criteria, and requisite actions for a second structural performance criterion were implemented with a delay. The third structural performance criterion, the completion of the taxpayer census in Ouagadougou and Bobo-Dioulasso and the submission to the Minister of Finance of the implementation report, was not observed, and completion of these measures constitutes a prior action for the completion of the sixth review under the PRGF arrangement. In addition, the increase in electricity tariffs by 12.5 percent constitutes a second prior action for completion of the sixth review. On the basis of this performance, and on the strength of the policies set forth in the attached memorandum, we request waivers for the nonobservance of two structural performance criteria, and that the IMF complete the sixth review under the PRGF and disburse the seventh loan in the amount of SDR 3.44 million.

4. In addition, the deterioration in Burkina Faso's terms of trade caused by higher world oil prices has considerably weakened our external position. The Government of Burkina Faso is determined to forcefully address these challenges and, to facilitate the adjustment and address the temporary additional balance of payments needs, requests an augmentation of access under the PRGF arrangement in an amount equivalent to SDR 6.02 million (10 percent of quota).

Sincerely yours,

/s/

Jean-Baptiste Compaoré
Minister of Finance and Budget
Officer of the National Order
Ouagadougou, Burkina Faso

MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES OF THE GOVERNMENT OF BURKINA FASO

August 25, 2006

I. MAIN ECONOMIC AND FISCAL DEVELOPMENTS IN 2005

1. Burkina Faso faced substantial economic challenges in 2005. A sharp decline in world cotton prices and a surge in world oil prices led to a near 25 percent deterioration in the external terms of trade and contributed to a balance of payments deficit. The relatively poor cereal harvest late in the previous year, along with rising world oil prices, pushed average inflation to 6.4 percent in 2005. However, conditions improved somewhat in the second half of the year. Strong agricultural growth offset a slowdown in other sectors, pushing real GDP growth to an estimated 7.1 percent in 2005, and inflationary pressures eased late in the year as food prices fell. Nonetheless, rising world oil prices continue to put upward pressure on transport costs and downward pressure on non-agricultural growth prospects. In the context of the deteriorating external environment, enterprises, notably in the cotton sector, increased their recourse to bank credit, driving the growth in credit to the economy to some 24 percent for the year as a whole. Nonetheless, the quality of commercial bank balance sheets remained satisfactory as adequate provisioning has been made to manage increased credit risk.

2. The overall fiscal deficit in 2005 (on a cash basis, excluding grants) was smaller than programmed (8.4 percent of GDP), despite a shortfall in revenue. As many expenditure authorizations were used to rebuild account balances of autonomous and semi-autonomous agencies (*comptes de trésor*), the indicative target on domestic financing was observed by a comfortable margin.

II. MACROECONOMIC FRAMEWORK FOR 2006 AND PROGRAM IMPLEMENTATION THROUGH MARCH

3. The projection for real GDP growth in 2006 has been revised upward to 5.6 percent to reflect early signs of a good cereal harvest, which is expected to offset the negative impact of a further deterioration in terms of trade on non-agricultural sectors. Inflation eased to 3 percent for the 12 months ending April 2006, owing to the continued impact of declining food prices. The external outlook has deteriorated since the 2006 program was designed, with the terms of trade projected to fall by another 2.7 percent on the basis of rising world oil prices. While the overall balance of payments is projected to register a surplus on account of the impact of reduction of debt under the multilateral debt relief initiative (MDRI), the generally weaker external environment is expected to result in a further, but more moderate, loss of international reserves. Monetary and exchange rate policy will continue to conducted a the regional level by the BCEAO with the objective of maintaining inflation to 2-3 percent .

4. Despite these adverse developments, macroeconomic policy implementation through March 2006 was satisfactory and all quantitative performance criteria were observed. A

continued high implementation rate of the public investment program, financed by project grants, and higher spending on priority social programs resulted in a moderately higher fiscal deficit than projected. Progress regarding structural reforms was mixed. The Joint Brigade of the Tax and Customs Directorates (JBTCD) was established before the end-December 2005 target date, thereby meeting one of three structural performance criteria under the program. The other two structural criteria were not observed. The JBTCD completed the targeted number of audits by end-March 2006, but the submission of the report to the Minister of Finance was delayed owing to personnel changes at the Directorate of Tax Administration. The completion of the taxpayer census and the submission of the report to the Minister of Finance was not completed as scheduled because of delays in settling contract disputes with census workers. All structural benchmarks were observed.

III. Policies for the Remainder of 2006

5. Fiscal policy will be somewhat more expansionary in 2006 than previously programmed. The revenue target of CFAF 432 billion (13.3 percent of GDP) remains achievable, but additional expenditure needs will require an increase in total non-interest outlays, including net lending, by about CFAF 36.1 billion (1.1 percent of GDP). The additional expenditures comprise a larger fuel subsidy to SONABEL (CFAF 5 billion); retroactive payments for civil service advancements that had been frozen since 2003 (CFAF 6 billion); higher utility bills linked to the decentralization of government and the establishment of new structures (CFAF 5 billion); VAT reimbursements (CFAF 6 billion); the *fonds de lissage* (CFAF 12.3 billion); and food security (CFAF 0.6 billion). To partially offset these additional expenditures, outlays in non-priority sectors will be reduced by CFAF 5.5 billion. In addition to the spending needs identified above (some of which are in priority sectors), another CFAF 6.6 billion is available for increasing spending in priority sectors. Any increase in the subsidy to SONABEL in 2006 beyond the CFAF 5 billion currently envisaged will be fully offset by reductions in non-priority sector outlays.

6. Against this background, total expenditure and net lending is projected to be on the order of CFAF 759 billion (23.3 percent of GDP) and the overall fiscal deficit (excluding grants) would be about 10 percent of GDP. Total spending in priority sectors would be CFAF 199.4 billion (6.1 percent of GDP). After taking into account the portion of recently obtained donor budget support and resources freed up in 2006 under the MDRI that could be used for these outlays (applied only to priority social sectors), additional domestic financing (excluding the onlending of IMF resources), a financing gap of about CFAF 15.2 billion remains. Given identified possible financing from donors, the remaining gap could be closed with the support of the requested augmentation from the IMF in the amount of 10 percent of quota (about CFAF 4.8 billion).

7. The CFAF 5 billion in additional provisions for SONABEL is the amount that will be needed after the increase in electricity tariffs of 12.5 percent. SONABEL is also taking measures to reduce internal costs by changing the fuel mix, and SONABHY (the petroleum importing company) is also implementing measures to reduce the cost of delivering fuels. We

are also working to accelerate the extension of the Côte d'Ivoire interconnection to Ouagadougou, which will further reduce costs and the need for subsidy. Finally, we also intend to implement a tariff setting mechanism that will link tariffs to costs, while providing incentives for improving efficiency in electricity generation. We are working closely with the World Bank in these areas, but substantial savings from these innovations are not expected before 2007.

8. Concerning the payments for retro-active public service advancements, the government estimates that the total cost of these advancements would be CFAF 18 billion. However, while formal advancements of public servants have not been implemented since 2003, salaries and indemnities have been raised on an ad-hoc basis during this period. These increases will be taken into account in assessing the government's additional financial obligation in this area. Should the government determine that it is legally obligated to pay the full CFAF 18 billion, it will spread the payment over a number of years, with a maximum of CFAF 6 billion to be paid in 2006.

9. The proposed *fonds de lissage* will help manage the risk associated with volatile world cotton prices and promote a more flexible response to changing world market conditions. The basic principles of the new fund and the associate automatic mechanism for establishing the cotton producer price have been adopted by the Interprofessional Association of Cotton Producers of Burkina Faso (AICB). Further work is needed to finalize the parameters of the new price-setting mechanism, the regulations governing the use of the fund, and the establishment of an adequate financial oversight system. Resources obtained for the *fonds de lissage* will be disbursed only after this work has been completed to the satisfaction of all stakeholders. Any resources provided to the fund by the government (which includes all donor contributions) would be made in the form of an interest-free loan to be repaid after the balance in the *fonds de lissage* reaches a sufficiently high level. In addition, the government is suggesting that all shareholders of cotton companies consider augmenting their capital. In that regard, the government has opened a dialogue with development partners to see if they could make resources available to help producers with their contribution.

10. Recent bills by utility companies indicate that total additional charges could total CFAF 11 billion in 2006. These additional charges come in the context of the decentralization of government, the establishment of new municipal and regional structures, and the expansion of health and education facilities. The provisioned CFAF 5 billion represents a good faith down payment by government that will be made only after the utility companies have provided all information necessary to validate the additional charges. Should the validity of the additional charges be verified, the balance will be paid in the context of the 2007 budget.

11. The government will continue to push ahead with the fiscal reforms outlined in its previous memorandum, and will implement additional measures in 2006 to strengthen tax and customs administrations. The Minister of Finance will validate updated multi-year plans to strengthen tax and customs administration by September 2006, and appoint a director of a steering committee to supervise working groups to implement the reform plans and to

coordinate technical assistance made available by donors. In addition, the Council of Ministers will approve a new investment code before the end of the year, which will enhance investment incentives while reducing revenue losses through exonerations. Key measures to strengthen tax and customs administration in the second half of the year include:

Tax Administration

- Install the tax management system (Sintax) at the two Directorates of Small and Medium Entreprises (*DPME, Direction des Petites et Moyennes Entreprises*);
- Generate automatically the list of nonfilers at the DPME each month;
- Reorganize tax files and teams at the DPME by sectoral activity;
- Produce an evaluation report of the program of ad hoc VAT audits, and assign objectives for ad hoc audits for 2007;
- Finish assigning Unique Taxpayer Numbers (*IFU, Identifiant Financier Unique*) to all firms in the DGE and the DPME, and update the taxpayer file;
- Link the Unique Taxpayer Number database to the tax management system (Sintax) at the DGE and the DPME;
- Improve management of the Remaining Balances (*RAR, Restes à Recouvrer*) by classifying the files in order of recoverability and amounts involved; and
- Put in place a mechanism to accelerate VAT refunds with a view to paying reimbursements within 60 days.

Customs Administration

- Start implementing the Unique Customs Declaration Form (*DDU, Déclaration en Douane Unique*);
- Implement monthly reconciliation of customs declaration data with Cotecna, and produce statistics; and
- Set up computerized database for customs valuation (*valeur en douane*).

12. The structural reforms for the energy sector, set forth in the government's previous MEFP (paragraph 8), will be implemented following the completion of the comprehensive energy sector reform strategy. Tenders for the selection of a private operator for the management of SONABEL and for private sector participation in SONABHY are unlikely to be realized this year. However, we are on schedule for selling a majority stake in ONATEL before the end of the year.

13. As noted in the government's previous letter of intent, we will continue to improve the business environment by streamlining procedures and costs for the transfer of property and the licensing of businesses, enhance labor market flexibility. The government's National Action Plan for the Reform of Justice (PANJR) is a key element of its efforts to fight corruption and to improve governance and the business climate. The General Inspectorate of Judicial Services has been given more autonomy. As a result, the Higher Judicial Council has recently applied disciplinary actions against magistrates (including arrest) accused of unethical or illegal activities. The government will increase the number of high tribunals from 13 to 20, increase the number of courts specializing in commercial and financial cases, and provide additional training for magistrates in the area of financial and commercial law. It will also enhance the independence of magistrates in the Auditor General Office (*Cour des Comptes*) by conferring them the same status as other judicial officers.

IV. Post Program Relations with the Fund

14. The government would like to maintain a close policy dialogue with the IMF with an arrangement either under the Poverty Reduction and Growth Facility or the Policy Support Instrument. We will shortly inform the IMF of our preference, and will request that a mission return to Burkina Faso in September-October to hold negotiations on the next arrangement.

Appendix 1. Attachment 1. Table 1. Burkina Faso: Quantitative Performance Criteria and Indicative Targets for the Program Under the Poverty Reduction and Growth Facility Arrangement, 2005

(In billions of CFA francs; cumulative from beginning of year)

	2004	2005		
	Dec.	End-Dec.		
	Actual	Prog. 1/	Prog. 1/ Adj. 2/	Actual
Performance criteria and indicative targets 3/				
Ceiling on cumulative change in net domestic financing to government 3/	-9.7	17.3	8.9	-14.5
Ceiling on the cumulative amount of new nonconcessional external debt				
contracted or guaranteed by the government 4/ 5/	0.0	0.0	0.0	0.0
Of which: less than one year's maturity 4/ 5/	0.0	0.0	0.0	0.0
Accumulation of domestic payments arrears 5/	0.0	0.0	0.0	0.0
Accumulation of external payments arrears 5/	0.0	0.0	0.0	0.0
Indicative targets				
Government revenue	344.5	377.9	377.9	365.2
Current expenditure	284.5	342.4	342.4	332.4
Expenditure on wages and salaries	119.0	140.7	140.7	141.4
Basic balance 6/ 7/	-82.0	-92.5	-92.5	-102.3
Change in the stock of expenditure authorized but without payment orders 7/	7.4	3.0	3.0	3.6
Adjustment factors				
Balance of payments assistance	89.8	99.2	...	98.8
Adjustment lending	42.8	40.5	...	41.0
Adjustment grants	47.1	58.7	...	57.8
Debt service after HIPC relief	14.2	21.0	...	12.2
Memorandum item:				
Social spending	145.0	160.5	160.5	166.2

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

1/ IMF Country Report No. 05/354, September 30, 2005.

2/ Target on net domestic financing adjusted to reflect the excess or shortfall in balance of payments assistance and deviations in external debt service compared to program projections.

3/ For 2005, the ceiling on the cumulative change in net domestic financing is to be adjusted upward (downward) by the amount of shortfall (surplus) in balance of payments assistance. The downward adjustment does not apply to the first CFAF 25 billion in excess balance of payments support, provided that additional spending is for priority social programs. At end-December 2005, the adjustment is limited to a maximum of CFAF 50 billion.

4/ Excluding treasury notes and bonds issued in CFA francs on the regional West African and Economic Monetary Union (WAEMU) market. This ceiling excludes supplier credits with a maturity of one year or less.

5/ To be observed on a continuous basis.

6/ Revenue (excluding grants) minus expenditure, excluding foreign-financed investment outlays and net lending.

7/ Including HIPC Initiative expenditure.

Appendix 1. Attachment 1. Table 2. Burkina Faso: Quantitative Performance Criteria and Indicative Targets for the Program Under the Poverty Reduction and Growth Facility Arrangement, 2006

(In billions of CFA francs; cumulative from beginning of year)

	2005	2006						
	Dec.	End-Mar.			End-June	End-Sep.	End-Dec.	
	Actual	Prog. 1/	Progr. Adj.	Actual	Rev. Proj.	Rev. Proj.	Proj. 2/	Rev. Proj.
Performance criteria and indicative targets 3/								
Ceiling on cumulative change in net domestic financing to government 4/	-14.5	14.8	-31.3	-50.3	-51.7	-45.5	12.8	-31.0
Ceiling on the cumulative amount of new nonconcessional external debt								
contracted or guaranteed by the government 5/ 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: less than one year's maturity 5/ 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Accumulation of domestic payments arrears 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Accumulation of external payments arrears 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Indicative targets								
Government revenue	365.2	87.7	87.7	87.9	213.4	314.8	432.3	432.3
Current expenditure	332.4	91.2	91.2	94.4	199.9	302.8	384.9	403.8
Expenditure on wages and salaries	141.4	37.1	37.1	38.6	78.1	118.4	151.8	157.8
Basic balance 7/ 8/	-102.3	-23.7	-23.7	-22.9	-54.3	-98.8	-97.1	-131.2
Change in the stock of expenditure authorized but without payment orders 8/	3.6	-7.0	-7.0	-9.1	-2.0	1.0	3.0	0.0
Adjustment factors								
IMF MDRI relief on principal due after 2006	...	0.0	...	45.3	45.3	45.3	...	45.3
Balance of payments assistance 9/	98.8	24.0	...	22.4	63.5	109.3	103.1	111.0
Adjustment lending	41.0	2.7	...	2.7	14.5	55.0	49.2	55.0
Adjustment grants	57.8	21.3	...	19.7	49.0	54.4	53.9	56.0
Debt service after HIPC relief	12.2	6.0	...	3.7	8.5	667.0	20.1	671.3
Memorandum item:								
Social spending	166.2	35.1	...	30.4	91.4	145.0	181.1	199.4

Sources: Burkinabè authorities; and staff estimates and projections.

1/ IMF Country Report No. 05/354, September 30, 2005.
2/ IMF Country Report No. 06/107, March 13, 2006.
3/ Performance criteria at end-March 2006.
4/ The ceiling on the cumulative change in net domestic financing is to be adjusted in line with the specifications set out in paragraph 7 of the TMU of IMF Country Report No. 06/107, March 13, 2006.
6/ To be observed on a continuous basis.
7/ Revenue (excluding grants) minus expenditure, excluding foreign-financed investment outlays and net lending.
8/ Including HIPC Initiative expenditure.
9/ Includes identified financing only.

Table 3. Burkina Faso: Structural Performance Criteria and Benchmarks and Prior Actions for the Sixth PRGF Review in 2005–06

	Measures	Dates	Measures
1.	Production by the Tax Directorate of monthly outcomes and quarterly progress reports on the 10 management indicators for three computerized offices (DGE, Kadiogo I, Houet I).	From end-March 2005	Observed
2.	Launch by the Tax Directorate of a comprehensive census of large and medium-sized enterprises in Ouagadougou and Bobo-Dioulasso and publication of a report on the status of its implementation.	End-December 2005	Observed
3.	Establishment of a fully operational Joint Brigade of the Tax and Customs Directorates with an annual work program for 2006. 1/	End-December 2005	Observed
4.	Submission to the Minister of Finance of a report on the six joint audits of the Joint Brigade of the Tax and Customs Directorates. 1/	End-March 2006	Not observed; done in April 2006
5.	Completion of the taxpayer census in Ouagadougou and Bobo-Dioulasso, and submission to the Minister of Finance of an implementation report. 1/	15 May, 2006	Not observed; prior action for the completion of the sixth review
6.	Implementation of the automatic price structure adjustment mechanism for petroleum products in relation to costs.	Continuous	Observed
7.	Increase electricity tariffs by 12.5 percent.		Prior action for the completion of the sixth review

[1] Performance criterion.