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

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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.

Bissau, January 9, 2008

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

Dear Mr. Strauss-Kahn:

1. Guinea-Bissau is slowly recovering from a decade of conflict and political instability. Economic and social conditions have worsened in the post-conflict period; the country's physical infrastructure was destroyed, and its administrative capacity was severely weakened. The fiscal situation has become unsustainable and relations with the international community have suffered. A new government appointed in April 2007 has taken early measures to adopt an emergency program to restore fiscal stability and improve economic management. This government has taken firm action to control expenditures, increase revenue collection, and improve fiscal management, transparency, and governance. There are already encouraging signs of an improvement in fiscal performance in the second half of 2007, and donor support has resumed.
2. In order to build on these recent gains, the government has agreed on a program of economic and financial policies for 2008 that addresses the immediate post-conflict challenges of stabilizing the fiscal position, building capacity for policy implementation, and regularizing relations with the donor community. The program also includes structural measures that lay the ground work for meeting the country's medium-term objectives of reviving growth, reducing poverty, and achieving fiscal and external sustainability. The donor community has already indicated it will provide significant financial and technical support for the 2008 program. To help achieve its objectives and restore confidence in economic management, the government is requesting a first purchase of SDR 1.775 million (12.5 percent of quota) under the Fund's Emergency Post-Conflict Assistance (EPCA) program. A second request for an EPCA purchase will be made later in 2008..
3. The details of the program for 2008 are included in the attached Memorandum on Economic and Financial Policies (MEFP). The government believes that the policies and measures set forth in the MEFP are adequate for achieving the objectives of the program, but we will take any further measures that may become appropriate for that purpose. In such cases, as well as before implementing policies that could adversely affect the program, we will consult the Fund.

4. To assist the Fund in assessing progress on the program, we will provide information on a regular basis as detailed in the attached Technical Memorandum. Moreover, we invite the staff of the Fund to review performance under the program quarterly, on the basis of quantitative and structural indicators (Tables 2 and 3 of the MEFP) as well as on overall implementation of the program.

Sincerely yours,

/s/

Issufo Sanhá
Minister of Finance

Attachments:

- Memorandum on Economic and Financial Policies
- Technical Memorandum of Understanding

ATTACHMENT I

GUINEA-BISSAU: MEMORANDUM ON ECONOMIC AND FINANCIAL POLICIES FOR EMERGENCY
POST-CONFLICT ASSISTANCE FOR 2008

Bissau, January 9, 2008

I. INTRODUCTION

1. **Guinea-Bissau remains a fragile post-conflict country.** The conflicts and prolonged political instability have taken a toll on the country's physical infrastructure, weakened administrative and technical capacity, and left unsustainable fiscal balances. The country is heavily dependent on external assistance, but relations with the donor community have suffered. The government of Guinea-Bissau is determined to take the necessary actions to address the immediate post-conflict challenges of stabilizing the fiscal position, building capacity for policy implementation, improving economic confidence, and regularizing relations with donors. A new government appointed in April 2007 has already made progress on an emergency program¹ to restore fiscal stability and improve economic management. The new government has taken strong measures to control expenditures, increase revenue collection, and improve fiscal management, transparency, and governance. We have also vigorously pursued efforts to secure much-needed financing, including reaching out to new donors. There have been encouraging signs of improved fiscal performance in the second half of 2007, and donors have resumed disbursements on pledges from the 2006 donors conference.

2. **To build on these recent gains, the government has agreed on a program of economic and financial policies for 2008 that aims to achieve fiscal stability in the near term and lay the groundwork for meeting the country's medium-term objectives of reviving growth, reducing poverty and achieving fiscal and external sustainability.** The government is requesting a purchase from the Fund's Emergency Post-Conflict Assistance (EPCA) to achieve its objectives and restore confidence in its economic management.

3. **This memorandum describes economic developments in 2007 and outlines policies and measures planned for 2008.**

II. RECENT ECONOMIC DEVELOPMENTS

4. **Preliminary projections for 2007 point to real GDP growth of 2.7 percent,** slightly higher than in 2006. Despite a normalization in cashew marketing arrangements in 2007, when the government avoided intervention in the cashew market—the 2007 domestic

¹ *Minimum Program for Restoration of Fiscal Stability*, May 2007.

reference price of CFA 200/kilo for cashews was agreed by all major stakeholders—provisional data indicate that production and exports of cashews was slightly lower than expected. In addition, the production of rice and other cereals has been severely affected by late and inadequate rains. Inflation has remained subdued, as it has been elsewhere in the WAEMU area, although recent high food prices could push the inflation rate for the year to slightly above the 3 percent target. The current account deficit (excluding grants) is expected to narrow to 11 percent of GDP in 2007, from 25 percent in 2006, reflecting higher exports of cashews, including from last year's harvest.

5. **The fiscal stance deteriorated sharply in early 2007, reflecting a severe breakdown in controls since late 2006.** Tax revenues declined 13 percent in the first half of 2007 compared to the same period in 2006, as revenue administration weakened and imports fell in the wake of political uncertainties. Although resources were scarce, the former government repaid large stocks of (unaudited) domestic arrears of previous years and there were other unprogrammed and extra-budgetary expenditures; substantial arrears, among them four months of civil service salaries, accumulated.

6. **Faced with the extremely difficult fiscal situation and a large financing gap estimated for 2007, in April the new government undertook an emergency program to restore fiscal stability.** The government plan received widespread support from Parliament, donors, development partners, and the public. Strong measures were taken to increase revenues, restrain expenditures, improve financial management, enhance supervision and monitoring, and address financing weaknesses.

Revenue Measures:

- (i) Limited the granting of exemptions to only those situations foreseen in the law (NGOs, embassies, ex-combatants, projects).
- (ii) Abolished the tax compensation system for customs (DGA) and corporate tax payers (DGCI), and allowed only the Treasury to grant tax compensations.
- (iii) Returned tax rates to previous levels on 14 of 18 products on which rates were lowered in May 2006.
- (iv) Enforced collection of stamp tax (cigarettes, bank checks, credit cards, airline tickets, insurance companies).
- (v) Contracted with commercial banks to manage tax collection for the DGA and DGCI departments.
- (vi) Pursued collection of tax arrears.

Expenditure Measures:

- (i) Closed accounts of all ministries and public entities at the BCEAO and opened accounts at the Treasury. The Treasury now holds only one account, the Treasury Current Account, at the BCEAO (rather than having financial directorates of ministries and public

entities managing government accounts as before).² The Treasury is now in sole charge of managing all government revenue and expenditure accounts.

- (ii) Process all payment orders through the Budget Directorate (DGO).
- (iii) Restrict extrabudgetary expenditures (DNT) only to emergency situations and regularize them within 48 hours.³
- (iv) Standardize budget execution procedures
- (v) Require pre-approval by the Ministry of Finance's Financial Control Department for any purchase of goods and services.
- (vi) Cease Treasury issuance of checks in the names of finance managers of ministries to directly pay for goods and services.
- (vii) Computerize payment system at the Treasury.
- (viii) Placed a ceiling of CFAF 300,000 on expenditures that can be paid by cash.

Transparency and Financial Management

- (i) Improved the transparency of and public confidence in the Treasury Committee, which is in charge of implementing the Treasury's cash flow plan, by inviting members from civil society, the armed forces, the Ministry of Interior, and ex-combatants, in addition to donor representatives, to participate as observers.
- (ii) Dismantled internal nontariff barriers on transporting cashews within the country.
- (iii) Introduced a requirement that all government suppliers have taxpayer identification numbers and bank accounts for payment, and that payments are to be made only after goods or services have been verified.

7. **Fiscal performance has improved markedly in the period since the new government began implementing its emergency fiscal plan.** In July–October, tax revenues were some 28 percent higher than during the same period last year, an important reversal of the trend observed in the first half of the year. There have also been positive developments with respect to expenditure control: The new government has ceased to pay domestic arrears from previous years, the amount of extrabudgetary expenditures (DNT) was reduced, and wages and other discretionary expenditures have been kept within budget.

8. **Despite these improvements in fiscal management, the fiscal stance is expected to deteriorate in 2007; the overall balance (excluding grants) is expected to widen to about 25 percent of GDP, from 22 percent in 2006.** Despite the improvement in revenue, it will not be possible to make up for the delay in disbursement of sizable annual fishing

² A special account used to honor outstanding debt service is also held at the BCEAO.

³ Such expenditures were at the heart of the fiscal deterioration observed at the end of 2006 and the beginning of 2007.

compensation from the E.U., which is now planned for early 2008.⁴ Total revenues are currently projected to decline to 16 percent of GDP, some 3.5 percent of GDP lower than in 2006. On the other hand, current expenditures are expected to be lower in 2007, down to 27 percent of GDP from 29 percent in 2006, reflecting improved expenditure control.

9. **Donor disbursements resumed in 2007, among them outstanding pledges from the November 2006 donor meeting.** External budget support for 2007 amounted to CFAF 17 billion (US\$34 million) from the European Union, regional partners (WAEMU and ECOWAS), bilateral partners (Spain, Portugal, France and China), and such nontraditional partners as Angola. Expected budget support of US\$10 million for 2007 from the World Bank was delayed and will be disbursed in early 2008. Budget support expected from the African Development Bank in 2007 (US\$1.7 million) has also been delayed until early 2008.

10. **On the financing side, the government rescheduled the domestic commercial debt it owed in 2007, in order to avoid substantial accumulation of domestic arrears:**

- (i) CFAF 3 billion (US\$5.7 million) in debt service owed in 2007 on commercial bank loans, as well as CFAF 1.5 billion (US\$3 million) in debt payments owed to the BCEAO, and
- (ii) CFAF 6.7 billion (US\$13.5 million) in Treasury bills that were due in February 2007

11. **Despite the government's efforts, some accumulation of domestic arrears (about CFAF 6.6 billion, 3.8 percent of GDP) was unavoidable in 2007, largely because of the delayed budget support in 2007.** A portion of the domestic arrears (about CFAF 3.6 billion related to medical and education supplies) will be paid with the World Bank disbursement expected in early 2008, and the remaining 2007 arrears will be included in an E.U.-financed audit of domestic arrears and repaid over time as financing becomes available (see below).

III. OUTLOOK, OBJECTIVES, AND POLICIES FOR 2008 AND THE MEDIUM TERM

12. **Real GDP growth is projected to increase to 3.3 percent in 2008, slightly higher than the average for the past four years.** The projections assume (i) an increase in cereal production to levels observed in previous years; (ii) an increase in cashew production from crop maturing; (iii) a slight pickup in public investment as the government continues to gather external donor support. Inflation is expected to converge to moderate levels below 3 percent, in line with WAEMU convergence criteria. The current account deficit (excluding grants) is expected to widen slightly to 12 percent of GDP in 2008, reflecting a lower export volume of cashews compared to 2007 (which included stocks from the previous year) and higher expected prices for rice and oil imports.

⁴ Owing to delays in concluding a new fishing agreement, the E.U. will not disburse the annual compensation (amounting to CFAF 4.5 billion or US\$9 million) expected in 2007 until early 2008.

13. **The fiscal stance is expected to improve in 2008 as the government continues to implement its fiscal adjustment plan.** For the year as a whole government revenues are projected to increase by some 5 percent of GDP to about 21 percent of GDP. Nontax revenues are expected to be above normal in 2008 because of two disbursements from the E.U. for fishing compensation (corresponding to the 2008 annual compensation and the delayed 2007 compensation). Tax revenues are projected to remain roughly constant as a share of GDP, but efforts will be made to bring in more revenues by year-end. Current expenditures are expected to decline by about 1 percent of GDP in 2008, reflecting a nominal freeze of current expenditures, including the wage bill, and strict control of nonwage discretionary outlays. While it is recognized that the expenditure framework is tight and encompasses only minimum spending requirements, the government is committed to maintaining domestic expenditures within available resources, both domestic and external. The overall balance (excluding grants) is expected to decline to about 21 percent of GDP, lower than in previous years.

14. **Financing needs will continue to be large in 2008,** amounting to CFAF 45 billion (US\$92 million or 27 percent of GDP). The 2008 financing needs include the rescheduling of Treasury bills and domestic debt owed to commercial banks and the BCEAO that are now expected to be repaid in 2008, as well as repayment in 2008 of domestic arrears that arose in 2007. The authorities have already secured the following sources of financing for 2008:

- (i) budget support from traditional and nontraditional donors (CFAF 24.8 billion or US\$50 million)⁵
- (ii) an extension of interim debt relief from the World Bank to cover US\$8.5 million (CFAF 4.2 billion) in 2008 external debt service obligations
- (iii) additional recovery of tax arrears (CFAF 0.7 billion)
- (iv) partial rescheduling (about CFAF 3.6 billion or US\$6 million) of domestic commercial debt owed in 2008
- (v) further accumulation of arrears on external debt (CFAF 9.7 billion or US\$20 million).

15. **These measures, along with two EPCA purchases (US\$5.6 million or CFAF 2.8 billion), should fully cover the financing gap and avoid accumulation of domestic arrears for 2008 as a whole, a key fiscal objective.** To the extent of any shortfalls in external financing in 2008, the government is committed to making further efforts to reschedule its domestic debts, to the extent possible. In 2008 the government also intends to hold a meeting following up on the November 2006 Round Table Conference to present its

⁵ Including World Bank (US\$16 million), European Union (US\$7 million), WAEMU (US\$3 million), and the African Development Bank (US\$1.7 million). The World Bank figure includes US\$6 million delayed from 2007, as is the African Development Bank disbursement. The total also includes South Africa (US\$10 million), Japan (US\$4 million), Portugal (US\$3 million), and Spain (US\$3 million).

2008 program and mobilize partners to support its development program, especially security sector and civil service reforms. If donor budget grants exceed the amount needed to finance the fiscal gap, priority will be given to using the resources to fully repay outstanding commercial debts and audited domestic arrears, and increase priority spending in social sectors above budgeted levels, in consultation with the Fund.

16. The government in 2008 will also implement policy measures to address remaining structural weaknesses in revenue collection and expenditure management.

These will:

- (i) Improve accounting and information flows of all Treasury transactions, including nonregularized expenditures and bank financing.
- (ii) Conduct a comprehensive audit of outstanding domestic arrears for 2000–06 and a portion of new 2007 arrears.⁶
- (iii) Avoid payment of audited arrears until the audit is completed and specific external financing for their clearance is obtained.
- (iv) As a first priority, avoid the accumulation of new domestic arrears in 2008.
- (v) Implement an integrated management information system, linking data flows between the customs (DGA) and tax department (DGCI), the budget office (DGO), and the Treasury.
- (vi) Strengthen the inspection capabilities of the General Audit Department of the Ministry of Finance and the Financial Control Unit of the Budget Office (DGO) through human and technological capacity building.
- (vii) Approve and have the Council of Ministers adopt a new state budget classification system in line with WAEMU regulations and implement it for the 2009 budget process.
- (viii) Finalize the merger of the payroll databases of the Ministry of Finance and the Ministry of Public Administration.

17. Beyond 2008 the fiscal position should steadily improve as controls are restored and nonpriority expenditures are reined in. Continued commitment to policy reform will enable the government to implement stronger Fund-supported reform programs and achieve sustained donor support. The government will in particular pursue efforts to contain the wage bill through civil and security sector reform. The overall fiscal balance (excluding grants) is projected to decline to below 20 percent of GDP in 2010, to levels that are more manageable given domestic resources and sustainable levels of external budget support.

18. The authorities intend to avoid introducing or intensifying exchange and trade restrictions in 2008 and beyond.

⁶ This audit will be conducted by a reputable international firm and financed by the E.U. The audit is expected to be launched before May 2008 and completed later in 2008.

IV. CAPACITY-BUILDING AND TECHNICAL ASSISTANCE

19. **Capacity-building is a key complement to fiscal reform in order to ensure that reform is effective and sustainable.** The recent missions from the World Bank and the IMF—including its regional technical assistance center West AFRITAC—identified technical assistance needs in all areas of public financial management as well as macroeconomic statistics (Table 1). The highest priority is assistance to the Customs, Treasury, and Tax Departments and the debt unit. The IMF West AFRITAC and AFRISTAT are providing technical support to strengthen public financial management and tax collection, as well as improve the statistics. The World Bank is also assisting with these reforms through its support to low-income countries under stress (LICUS), including financing a long-term resident fiscal advisor.

V. PROGRAM MONITORING

20. **The monitoring of progress on the program outlined will be based on the quantitative and structural indicators provided in Tables 2 and 3.** The quantitative indicators are (i) a floor on government revenue (tax and nontax); (ii) a ceiling on the domestic primary deficit; (iii) a ceiling on domestic financing of the budget; (iv) no new domestic arrears; and (v) a ceiling on payment of previous arrears; and (vi) no short- or long-term nonconcessional external borrowing. The quantitative indicators are based on the monthly treasury cash flow plan for 2008 (Table 4).⁷ Specific definitions and explanations are contained in the annexed Technical Memorandum of Understanding (TMU). The government will provide, on a timely basis, all necessary data to monitor the program as indicated in the technical memorandum of understanding. A second EPCA purchase will take place in July 2008.

21. **To ensure the success of the program, and as prior actions, the government has** (i) submitted to parliament its 2008 government budget consistent with the agreement in this Memorandum; and (ii) sought firm assurances from donors to fully cover the 2008 fiscal financing requirements. The authorities have received assurances that there are no objections to EPCA from official Paris Club creditors to whom Guinea-Bissau is currently in arrears. They have also informed non-Paris Club creditors that they will continue to have difficulties servicing their external debt service obligations, including during the EPCA program period.

⁷ The monthly cash flow also serves as an informal indicative monthly framework for regular assessments of performance under the EPCA.

Table 1. Technical Assistance Needs of the Ministry of Finance

Department	Area	Long term	Short term	(Possible) provider
Minister's Cabinet	Macrofiscal advisor	X ¹		(WB LICUS/IMF) ²
Budget	Expert public finance	X		(E.U.)
	Expert computer systems	X		(E.U.)
	Computerization expenditure accounts	X ²		E.U.
	Public financial management		X	IMF/FAD
Treasury	Advisor to the Treasurer	X		WB LICUS ²
	Accounting system	X		(France)
Tax Department	Expert on tax code		X	(Portugal/IDB)
	Computerization of revenue accounting	X		
	Advisor Directorate of Large Enterprises		X (6 months)	(West AFRITAC)
Customs	Expert to review organic law of customs	X		IDB/WB LICUS ²
	Customs advisor	X		
	Advisor implementing ASYCUDA ++			AfDB
External debt	Debt management		X ³	DRI/IDB/West-AFRITAC
Microfinance	Advisor		X	(West-AFRITAC)
Conjuncture	Advisor, fiscal analysis	X		
Planning	National accounts advisor	X		
	Implementation System of National Accounts 1993		X	IMF/AFRISTAT

¹ TA requested and under consideration.

² TA in place.

³ First mission conducted in January 2005.

Table 2: Guinea-Bissau: Quantitative Indicators under the Emergency Post-Conflict Assistance for 2008
 Quarterly Targets 1/
 (Cumulative, in millions of CFAF)

	2008			
	End-Mar. Prog	End-Jun. Prog	End-Sep. Prog	End-Dec. Prog
1. Government Revenues 2/	4,226.6	10,413.9	17,824.3	23,130.4
2. Domestic primary deficit (commitment basis) 3/	-5,050.0	-4,861.7	-3,522.1	-7,463.7
3. Domestic financing of the budget 4/	-238.7	-7445.7	-7684.3	-17331.6
4. New domestic arrears 5/	0.0	0.0	0.0	0.0
5. Payment of previous years arrears 6/	1772.0	3600.0	3600.0	3600.0
6. External non-concessional public borrowing, maturity > 1 year	0.0	0.0	0.0	0.0

1/ Cumulative from January 1 of the corresponding year. The definition of the aggregates is provided in the Technical Memorandum of Understanding (TMU).

2/ Floor. Defined as direct taxes (01.00.00) plus indirect taxes (02.00.00) plus fishing licenses (03.01.01).

3/ Ceiling. From TOFE. If the disbursed amounts of EU fishing compensation are lower (higher) than programmed, the ceiling will be increased (lowered). For the programmed quarterly amounts of EU fishing compensation for 2008 see the TMU (¶ 11).

4/ Ceiling. From TOFE. If the actual amount of external budgetary assistance (including EU fishing compensation) falls short of program forecasts, the ceiling will be increased for the full amount of the shortfall. For the programmed quarterly amounts of external assistance (including EU fishing compensation) in 2008 see the TMU (¶ 11).

5/ Ceiling. At end-March, end-June and end-September, stock of accounts payables (rest-a-payer); at end-December, accounts payables accumulated during the current year (2008) and still outstanding one month after the end of the year in the case of wages and other personnel expenditures (including pensions) and three months after the end of the year, in the case of non personnel expenditures. The ceiling on the accumulation of new domestic arrears will be adjusted in line with available domestic financing of the budget. In particular, if the government is not able to increase (decrease) the domestic financing of the budget by the full amount of the shortfall (excess) in external budget support, the ceiling in the accumulation of new domestic arrears will be adjusted upward (downward) by that difference.

6/ Ceiling. Includes arrears in wages, transfers, and goods and services previous to 2008 and outstanding as of January 1, 2008. If external financing specifically targeted to clear arrears is available, the ceiling will be increased for the full amount of the funds available.

Table 3. Guinea-Bissau: Prior Actions and Structural Indicators Under the
Emergency Post-Conflict Assistance
January 1, 2008—December 31, 2008

Prior Actions	Target date	Status
Submission to Parliament of the government budget fully consistent with the fiscal framework presented in this MEFP.	End-November 2007	Done
Secure financing assurances from donors to fully cover the 2008 fiscal financing requirements	End-November 2007	Done
Structural Indicators		
Approve and adopt by Council of Ministers legal framework for new state budget classification system in line with WAEMU regulations.	End-March 2008	
Create Information Technology (IT) Department in Ministry of Finance and start training staff	End-March 2008	
Launch financial audit, by a reputable international audit firm, of outstanding domestic arrears for 2000-2007. ⁸	End-April 2008	
Finalize merger of two payroll databases of Ministry of Finance and Ministry of Public Administration	End-June 2008	
Improve proper accounting and information flows of all Treasury transactions, including nonregularized expenditures and bank financing	End-June 2008	

⁸ Audit financed by E.U..

Table 4. Guinea-Bissau: Treasury Cash-Flow Plan 2008
(CFAF millions)

	Jan. Proj.	Feb. Proj.	Mar. Proj.	Apr. Proj.	May Proj.	Jun. Proj.	Jul. Proj.	Aug. Proj.	Sep. Proj.	Oct. Proj.	Nov. Proj.	Dec. Proj.	Jan-Dec Proj.	In percent of GDP
A. Revenue and grants	4,896	2,903	2,010	8,229	3,538	3,000	7,950	2,567	7,159	4,006	2,296	2,947	51,501	28.4
Revenue	1,926	2,061	2,010	6,425	2,038	3,000	3,000	2,567	7,159	2,202	2,296	2,947	37,631	20.8
Taxes	1,100	1,235	1,300	1,420	1,886	2,289	2,807	2,475	1,536	1,376	1,469	1,869	20,764	11.5
Nontax revenue	826	826	710	5,005	151	710	192	92	5,623	826	826	1,077	16,867	9.3
Expected budget support	2,970	842	0	1,804	1,500	0	4,950	0	0	1,804	0	0	13,869	7.7
B. Expenditure	4,022	3,824	3,748	3,879	3,936	4,105	3,988	3,936	3,861	3,990	3,935	4,106	47,331	26.1
Current expenditure	3,923	3,725	3,649	3,780	3,725	3,893	3,777	3,724	3,649	3,778	3,723	3,895	45,242	25.0
Wages and salaries	1,777	1,777	1,777	1,777	1,777	1,777	1,777	1,777	1,777	1,777	1,777	1,777	21,322	11.8
Goods and services	595	595	595	595	595	595	595	595	595	595	595	595	7,134	3.9
Transfers	935	935	935	935	935	935	935	935	935	935	935	935	11,224	6.2
Other current expenditure	277	277	277	277	277	277	277	277	277	277	277	277	3,327	1.8
<i>Of which: Restitutions + Incentives + Others</i>	203	203	203	203	203	203	203	203	203	203	203	203	2,432	
Interest on domestic and foreign debt	339	141	66	196	141	310	193	140	66	195	140	311	2,236	1.2
<i>Of which: World Bank</i>	29	84	8	104	83	252	28	83	8	102	82	253	1,116	0.6
Capital expenditure (domestically financed)	99	99	99	99	212	212	212	212	212	212	212	212	2,089	1.2
C. Extrabudgetary expenditures (DNT + tax compensations)													0	
D. Overall domestic balance: A - (B+C)	875	-921	-1,738	4,350	-399	-1,105	3,961	-1,369	3,298	16	-1,639	-1,159	4,170	2.3
E. Payment of domestic arrears and complimentary period	1,564	208	0	1,828	0	0	0	0	0	0	0	0	3,600	2.0
F. Overall domestic balance (cash basis) D-E	-689	-1,129	-1,738	2,522	-399	-1,105	3,961	-1,369	3,298	16	-1,639	-1,159	570	0.3
Financing	689	1,129	1,738	-2,522	399	1,105	-3,961	1,369	-3,298	-16	1,639	1,159	-570	-0.3
Domestic financing	0	0	-239	-5,244	0	-239	0	0	-239	-1,917	0	-990	-8,868	-4.9
Bank financing	0	0	-239	-5,244	0	-239	0	0	-239	-1,917	0	-990	-8,868	-4.9
BCEAO	0	0	-239	0	0	-239	0	0	-239	0	0	-990	-1,706	-0.9
Commercial banks	0	0	0	-5,244	0	0	0	0	0	-1,917	0	0	-7,161	-4.0
Nonbank financing (incl. privatization)	0	0	0	0	0	0	0	0	0	0	0	0	0	0.0
T-bills and regional commercial banks (net)	0	0	0	-1,724	0	0	0	0	0	-6,740	0	0	-8,464	-4.7
Amortization of external debt	-849	-135	-36	-533	-335	-763	-218	-135	-36	-548	-335	-999	-4,920	-2.7
Financing requirements (+ = financing needs flow)	1,538	1,264	2,013	4,979	733	2,107	-3,744	1,503	-3,024	9,188	1,974	3,149	21,682	12.0
Additional identified budget support		1,485	1,485	4,950	1,000	283	283	283	283	283	283	283	10,900	6.0
EPCA	1,386						1,386						2,772	
World Bank debt relief	94	150	40	591	372	847	94	150	40	591	372	847	4,188	
Authorities' measures	58	58	58	58	58	58	58	58	58	3,213	58	58	3,854	
Recovery of tax arrears (CFA 700 mill.)	58	58	58	58	58	58	58	58	58	58	58	58	700	
T-bills rescheduling	0	0	0	0	0	0	0	0	0	3,154	0	0	3,154	
Financing gap (flow) (+ = financing needs)	0	-429	429	-621	-697	919	-5,565	1,013	-3,405	5,102	1,261	1,993	0	0.0
Financing gap (accumulated stock) (+ = financing needs)	0	-430	0	-621	-1,318	-399	-5,964	-4,952	-8,356	-3,254	-1,993	0		

Source: Guinea-Bissau authorities, and IMF staff estimates and projections based on 2008 Budget.

ATTACHMENT II
TECHNICAL MEMORANDUM OF UNDERSTANDING FOR PROGRAM FOR 2008 TO BE
SUPPORTED UNDER EMERGENCY POST-CONFLICT ASSISTANCE

Bissau, January 9, 2008

1. This memorandum describes the definitions of the quantitative indicators for the Program for 2008 to be supported under Emergency Post-Conflict Assistance (EPCA) (Table 2) of the Memorandum on Economic and Financial Policies (MEFP) in accordance with the understandings reached between the authorities of Guinea-Bissau and the staff of the IMF. It also specifies the agreed periodicity and deadlines for transmission of data to the staff of the IMF for program monitoring purposes.

I. QUANTITATIVE INDICATORS AND ADJUSTORS

A. Quantitative Indicators

2. The quantitative indicators are the following:
- a. cumulative floors on government revenue;
 - b. cumulative ceilings on the domestic primary fiscal deficit (on a commitment basis);
 - c. cumulative ceilings on the change in net domestic financing of the budget;
 - d. cumulative ceiling on new domestic arrears of the government, including wage arrears;
 - e. ceiling on payments of previous years domestic arrears (before 2008);
 - f. cumulative ceilings on new nonconcessional external debt contracted or guaranteed by the government.

Quantitative indicators have been set for end-March, end-June, end-September and end-December 2008, and their values are cumulative from January 1, 2008. Indicative targets for new nonconcessional external debt are continuous.

Definitions and computation

3. **For the purposes of the EPCA, the government is defined as the central government of Guinea-Bissau.** This definition excludes public entities with autonomous legal personality whose own budget is not included in the central government budget.
4. For the targeted ceiling presented in Table 1 below, government revenues include direct taxes, indirect taxes, and fishing licenses. The cash-flow estimates are based on the tax revenues and fishing licenses estimated in the draft budget for 2008.

Table 1. Quarterly Targets for Government Revenues
and Other Current Expenditures, 2008
(Cumulative, in millions of CFAF)

	Mar.	Jun.	Sept.	Outturn Dec
1. Government revenues	4,226.6	10,413.9	17,824.3	23,130.4
Tax revenues (Direct and indirect taxes (01.00.00 and 02.00.00))	3,635.0	9,230.7	16,049.5	20,764.0
Fishing licenses (03.01.01)	591.6	1,183.2	1,774.8	2,366.4

Source: Budget 2008.

5. **The domestic primary fiscal deficit on a commitment basis is based on the cash-flow estimates provided in Table 4 of the MEFP.** It is calculated as the difference between government revenue and domestic primary expenditure on a commitment basis. Government revenue includes all tax and nontax receipts and excludes external grants. The domestic primary expenditure consists of current expenditure plus domestically-financed capital expenditure, excluding all interest payments and externally financed capital expenditures. 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. The estimated domestic primary balances for the program period are provided in Table 2 below.

Table 2. Estimates of the Quarterly Domestic Primary Balance, New Domestic Arrears, and Payment of previous years' arrears, 2008
(Cumulative, in millions of CFAF)

	Mar.	Jun.	Sept.	Outturn Dec
1. Total domestic primary deficit	-5,050	-4,862	-3,522	-7,464
Revenue	5,998	17,460	30,187	37,631
Current expenditure excluding interest	10,752	21,503	32,255	43,006
Domestically financed capital exp.	297	819	1,454	2,089
2. New domestic arrears	0.0	0.0	0.0	0.0
Wages and other expenditures on personnel (including pensions)	0.0	0.0	0.0	0.0
Nonpersonnel expenditures	0.0	0.0	0.0	0.0
3. Payment of previous years' domestic arrears	1,772	3,600	3,600	3,600

Source: Table 4, MEFP.

6. **New domestic arrears of the government are defined as follows:** (i) At end-March, end-June and end-September defined as the stock of account payables (rest-a-payer); (ii) At end-December, defined as accounts payables accumulated during 2008 and still outstanding one month after end-December in the case of wages and salaries (including pensions), and three months after end-December in the case of goods and services and transfers. The targets for the program period are presented in Table 2 above.

7. **Previous year's domestic arrears are defined as domestic arrears in wages, transfers, and goods and services** previous to 2008 and outstanding as of January 1, 2008. The targets for the program period are presented in Table 2 above. The program allows a partial payment of expenditure commitments related to 2007, that were not paid during that year and are still outstanding as of January 1, 2008, up to a maximum of CFAF 3.6 billion (see MEFP ¶ 14).

8. **Net domestic financing of the budget is defined on the basis of the cash-flow estimates in Table 4 of the MEFP.** Bank financing consists of the net changes in the balances of the treasury accounts at the BCEAO and at commercial bank(s)—excluding balances in those accounts that are not freely available for budget financing, such as accounts that are held under double signature arrangements with donors—as well as the outstanding amounts of loans, including T-bills, from the BCEAO and the commercial banks (local and regional). Domestic nonbank financing encompasses privatization receipts, as well as any other domestic financial debt held outside the banking sector, other than new domestic arrears as defined above, that may arise. Table 3 below provides the details.

Table 3. Estimates of Domestic Financing by Quarter, 2008
(Cumulative, in millions of CFAF)

	Mar.	Jun.	Sept.	Outturn Dec
Domestic financing	-239	-7,446	-7,684	-17,332
Bank financing	-239	-7,446	-7,684	-17,332
BCEAO	-239	-477	-716	-1,706
Commercial bank(s) (local banks)	0	-5,244	-5,244	-7,161
Regional Commercial banks and Treasury bills	0	-1,724	-1,724	-8,464
Nonbank financing	0	0	0	0

Source: Table 2, MEFP.

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

a. The indicator for external borrowing applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt, adopted by the Executive Board of the IMF on August 24, 2000 but also to commitments contracted or guaranteed for which value has not been received. For purposes of these guidelines, the term “debt” is understood to mean a current, that is, not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, 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 that are equivalent to fully collateralized loans, under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers’ credits, that is, contracts where the supplier permits the obligor to defer payments until some 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 period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement, excluding those payments that cover the operation, repair, or maintenance of the property. Under the definition of debt set out above, arrears,

penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g. payment on delivery) will not give rise to debt. For the purposes of monitoring the EPCA, arrangements to pay over time obligations arising from judicial awards to external creditors do not constitute nonconcessional external borrowing.

b. Loan concessionality is assessed on the basis of the commercial interest reference rates (CIRRs) established by the OECD. A loan is said to be on concessional terms if, on the initial date of contraction of the loan, the ratio of the present value of the loan, calculated on the basis of the reference interest rates, to its nominal value is less than 50 percent (that is, a grant element of at least 50 percent). For debts with a maturity exceeding 15 years, the ten-year reference interest rate published by the OECD is used to calculate the grant element. For shorter maturities, the six-month market reference rate is used. Purchases from the IMF are excluded from this limit.

10. **The concept of government for the purposes of the indicators on external debt is broader than the one used for the budget aggregates, including all debt that may ultimately be deemed to be a liability of the state.** In addition to the government as defined in paragraph 3, 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.

B. Adjusters

11. The following adjusters will be in effect:

The ceilings on domestic primary fiscal deficit will be adjusted upward (downward) for any shortfall (excess) in E.U. fishing compensation:¹

- **The ceiling on the domestic primary deficit (on a commitment basis) will be increased (lowered) in case of lower (higher) than programmed disbursement of E.U. fishing compensation, for the full amount of the shortfall (excess).** The program assumes the following amounts of E.U. fishing compensation (cumulative from January 1, 2008): by end-March CFAF 0 billions; by end-June CFAF 4.9 billions; by end-September CFAF 9.8 billions; and by end December CFAF 9.8 billion.

¹ For the purposes of the TMU, the CFAF/US\$ exchange rate is 495 and the CFAF/Euro exchange rate is 656.

The ceilings on domestic financing and on new domestic arrears will be adjusted upward (downward) for any shortfall (excess) in external budgetary assistance (including E.U. fishing compensation),

- **The ceiling on domestic financing will be adjusted in line with the amount of external budget support (including E.U. fishing compensation).** In particular, the ceiling will be increased (lowered) in the case of shortfall (excess) in external budget support, by the full amount of the shortfall (excess). The program assumes the following amounts of external budgetary assistance (including E.U. fishing compensation) (cumulative from January 1, 2008): by end-March CFAF 6.8 billions; by end-June CFAF 21.2 billions; by end-September CFAF 31.9 billions; and by end December CFAF 34.6 billion.
- **The ceiling on the accumulation of new domestic arrears will be adjusted in line with available domestic financing of the budget.** In particular, if the government is not able to increase (decrease) the domestic financing of the budget by the full amount of the shortfall (excess) in external budget support, the ceiling in the accumulation of new domestic arrears of nonpersonnel expenditures will be adjusted upward (downward) by that difference.

II. PROGRAM MONITORING

12. To allow monitoring of developments under the program, the Ministry of Finance will regularly report the following information to the staff of the IMF:

- The detailed reports on revenue and expenditure by budget line and a completed summary table on central government operations (TOFE) (monthly, two weeks after the end of the month);
- Data on any extra-budgetary expenditure (not included above), including: (i) incentives to tax collectors; (ii) restitutions to collecting agencies; (iii) and any other retentions operated by collecting agencies (DGA, DGCI, Fishing Ministry, etc.) (monthly, two weeks after the end of the month);
- Tables on nonregularized expenditures (DNT) (Monthly, two weeks after the end of the month);
- Table on accounts payable (rest-a-payer) broken down by budget category (wages, goods and services, transfers, other) (monthly, two weeks after the end of the month);
- Previous years domestic arrears (including 2007): stock and clearance, broken down by budget category (wages, goods and services, transfers, other) (monthly, two weeks after the end of the month);

- The monetary survey, the balance sheet of the central bank, and the balance sheet of the commercial banks, (monthly, within six weeks following the end of the month);
- A table with data on Treasury/Central Government outstanding loans (including short-term advances) from/and deposits in local and regional commercial banks (monthly, two weeks after the end of the month);
- The Treasury Committee monthly reports (monthly, within ten days after the end of the month);
- The amount and terms of new external debt (concessional or not) contracted or guaranteed by the government (within four weeks after the end of the month);
- A monthly table on the disbursements of budget support (grants and loans), by donors (two weeks after the end of the month);
- Indicators to assess overall economic trends, such as the household consumer price index and exports of cashew nuts (when such information becomes available);
- A table with a description of the status of implementation of the structural indicators in Table 3 of the MEFP (within two weeks after the end of the month); and
- Information on any type of financial assistance received and not programmed. This should be reported on a continuous basis.

13. **The Ministry of Finance will provide the staff of the IMF with any other information that the Ministry or the staff of the IMF deem necessary for program-monitoring purposes.**

14. **The above data will be provided to the Economist at the local office of the IMF in Bissau (Mr. Fonseca) for further transfer to the African Department of the IMF in Washington, D.C.**