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

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Bissau, May 22, 2008

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

Dear Mr. Strauss-Kahn:

1. The attached Memorandum of Economic and Financial Policies (MEFP) sets out the objectives and policies that the government of Guinea Bissau intends to pursue for the remainder of 2008. They are consistent with the objectives of the program of economic and financial policies supported by the IMF's Emergency Post-Conflict Assistance (EPCA) approved in January. Under the EPCA-supported program, the Government of Guinea Bissau has taken steps to stabilize an extremely difficult fiscal position, accelerate implementation of structural reforms, and improve financial relations with its international partners. The government's program is an important step toward meeting the country's medium-term objectives of reviving growth, reducing poverty, and achieving fiscal and external sustainability. Our economic reform efforts are being supported by the international community, including both traditional and nontraditional donors.
2. The fiscal situation has improved in the first part of 2008 after weaker than expected performance in 2007, and major progress is being made to advance structural reforms to strengthen fiscal management. Although real GDP growth was subdued in 2007, it is expected to improve in 2008. Annual inflation accelerated sharply at end-2007 and remained high in early 2008, driven mainly by the recent surge in international prices for food and oil.
3. Performance on the EPCA-supported program has been generally good. By the end of March 2008, four of six quantitative indicators were met. We expect that the two that were not met (payment of previous years' arrears and new domestic arrears) will be met for the year as a whole. The structural indicators for end-March were met; despite a delay on one measure, it was met on May 19, 2008.
4. Guinea Bissau's fiscal situation, however, remains very tight, and pressures are emerging, especially from the recent surge in world food and fuel prices. The government is nevertheless determined to take the measures necessary to maintain fiscal stability for the rest of the year and avoid accumulating new domestic arrears for the year as a whole. Our 2008 program envisages an acceleration of critical structural reforms, particularly in the areas of public expenditure management and revenue collection. These are key conditions for improving confidence in economic management and securing additional donor support.

5. In support of the government's objectives and policies, we are requesting a second purchase of the EPCA in an amount equivalent to SDR 1.775 (12.5 percent of quota). We believe that the policies and measures set forth in the MEFP are adequate for achieving the objectives of the EPCA program, but we will take any further measures that may become appropriate for that purpose. In such cases, and before implementing any policies that might adversely affect the program, we will consult the Fund.

6. To assist the Fund in assessing progress on the program, we will continue to regularly provide information as detailed in the attached Technical Memorandum of Understanding (TMU). Moreover, we invite the staff of the Fund to continue to review our performance in the program quarterly, on the basis of the revised quantitative and structural indicators (Tables 1 and 2 of the MEFP) as well as 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 OF ECONOMIC AND FINANCIAL POLICIES**

Bissau, May 22, 2008

I. INTRODUCTION

1. **This Memorandum of Economic and Financial Policies (MEFP) supplements that of January 2008 and our Letter of Intent dated January 9, 2008.** It describes (i) performance on the EPCA-supported program through March 2008; (ii) economic developments in 2007 and early 2008; and (iii) the government's economic program for the remainder of this year. The policies set forth in this MEFP should help the government stay the course and achieve the objectives of the EPCA-supported program.

II. RECENT DEVELOPMENTS AND PROGRAM PERFORMANCE

2. **Economic activity in 2007 was subdued, as expected, with real GDP growth at just 2.7 percent.** The 2007 performance reflected mainly much lower production of rice and other cereals due to late and inadequate rains. This was partially compensated for by an increase in production and exports of cashew nuts following normalization of marketing arrangements.

3. **Annual inflation accelerated sharply at end-2007 and remained high in early 2008 driven mainly by the surge in international prices for food and oil.** The 12-month inflation rate rose to 9.3 percent at end-2007, from 3.2 percent at end-2006, and has remained high in 2008.

4. **Monetary conditions remained stable in 2007.** Broad money growth reached 25 percent, faster than initially projected. The accumulation of foreign assets by the central bank accounted for about 75 percent of the total increase. There was also a significant increase in credit to the private sector in 2007, equivalent to 29 percent of the increase in broad money growth as the domestic banking sector became more involved in the financing of the cashew nuts campaign. As expected, the external current account deficit (excluding official current transfers) narrowed to 12.5 percent of GDP, from 27 percent in 2006, reflecting higher exports of cashews.

5. **Despite efforts to improve revenue collection, fiscal performance was weaker than expected in 2007.** Tax revenues did improve markedly in the second half of 2007, after the government implemented its emergency fiscal program.¹ However,

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

this was not enough to offset higher expenditures, including a large amount of nonregularized expenditures, owing to continued weaknesses in expenditure management and control. As a result, the domestic primary balance worsened to CFAF 19.1 billion (10.8 percent of GDP) in 2007, from CFAF 12 billion (7.5 percent of GDP) in 2006. Measures are being taken to better control expenditures (¶ 12).

6. **Fiscal performance improved in early 2008 and progress is being made to advance structural reforms, especially in fiscal management.** Performance on the EPCA-supported program was generally good. By the end of March, four of six quantitative indicators were met (domestic primary deficit, government revenues, domestic financing of the budget, and external nonconcessional borrowing) (Table 1). The quantitative indicators on payment of previous years' arrears and new domestic arrears were missed but the target for the year as a whole is achievable. The structural indicators for end-March were met with a delay on one measure (Table 2).

7. **Improved control of expenditure commitments on both wages and goods and services kept domestic primary expenditures below target by some CFAF [0.6] billion for the first quarter of 2008.** Total revenues were higher than programmed by some CFAF 0.5 billion, reflecting mainly unexpectedly high tax revenues. Nontax revenues were in line with the program, although fishing revenues were lower than expected. The domestic primary deficit for the first quarter of 2008 was CFAF 3.8 billion, below the program target of CFAF 5.1 billion.

8. **On the financing side, the government paid down more of 2007 domestic arrears than planned.** The EPCA program allowed for a portion of 2007 domestic arrears (about CFAF 3.6 billion) to be repaid in 2008. The authorities, however, repaid most of this amount in the first quarter (mainly related to wages and medical and education supplies), during the legal complementary period for fulfilling previous year expenditure commitments, and thus exceeded the amount programmed for that period by about CFAF 2 billion. As a consequence, some new domestic arrears accumulated, exceeding the adjusted quantitative indicator for end-March. The authorities have since taken measures to avoid any further payment of 2007 domestic arrears (¶ 12) so as to remain within the target for the year as a whole.

9. **At the same time, budget support expected in the first quarter of 2008 (about CFAF 7 billion), mainly from the World Bank, was not disbursed as scheduled for administrative reasons but are expected in the coming period.** In the circumstances, to make up for financing shortfalls, the government resorted to contracting new short-term domestic commercial debt backed by the expected donor disbursements. Compared to the adjusted quantitative indicator for end-March, the amount of domestic financing was below target, but the costs associated with

commercial borrowing in terms of commissions and interest have budgetary implications for 2008.²

10. **The government has announced import tax exemptions in response to the food and fuel price pressures.** Since March, all rice imports have been temporarily exempted from taxes. The government also established reference prices to calculate import duties for rice and diesel imports that are much lower than actual import prices. These measures are expected to alleviate some of the impact of higher import prices, particularly for rice, the main staple, on the most vulnerable groups, especially the urban poor, but will have a fiscal cost in terms of lost revenue for the year as a whole (see below).

11. **Structural reforms to improve fiscal revenue collection and expenditure management have continued, with some delays.** The Ministry of Finance created an Information Technology (IT) Department and began training staff (as expected for end-March). The Council of Ministers in May approved a new legal framework for the state budget classification system in line with WAEMU regulations (somewhat delayed compared to the program target of end-March). In May the authorities also launched an audit of domestic arrears for 2000–2007 (a structural indicator for end-April); the EU is paying the international firm that is conducting the audit.

12. **The government has taken a number of other significant actions to address weaknesses in the fiscal areas, including issuing decrees to:**

- Cease payment of outstanding 2007 domestic arrears as of March 12.
- Mandate that all expenditures should be paid only through the Treasury account at the BCEAO.
- Outlaw the payment of any extrabudgetary expenditures unless they are previously authorized by the Minister of Finance and the Prime Minister, and regularize them within 48 hours.
- Transfer to the BCEAO any remaining funds in Treasury accounts in commercial banks.

13. **The government has also made notable progress in other areas to further improve fiscal management.** The Ministry of Finance is currently installing new

² The government contracted short-term commercial loans in the first quarter of 2008 amounting to CFAF 4.7 billion at effective annual interest rates of about 15 percent, including fees and commissions. Part of the principal of the debt (CFAF 2.2 billion) has already been repaid plus a cost (interest and fees) of CFAF 100 million. The rest of the principal (CFAF 2.5 billion) is expected to be repaid in June when World Bank support is disbursed, plus an additional estimated cost of CFAF 156 million.

software to improve accounting and information flows of all Treasury operations (a structural indicator for end-June). The Ministry of Finance and the Ministry of Public Administration are on the final steps to merge the two payroll databases (a structural indicator for end-September). The government has also launched a financial audit, financed by the UNDP, of all government agencies that collect revenues, including state agencies (customs, fisheries, and mining); public enterprises (EAGB, APGB, and FISCAP); and parastatals (Guinetel, Guinea telecom, phosphate and petroleum companies, and ICGB). The audit will, among other things, confirm that levels transferred to the Treasury correspond to regulations, and identify areas where tax collection is currently below potential. The government is committed to adopt as soon as possible recommendations to capture potential revenues.

III. ECONOMIC POLICIES FOR THE REMAINDER OF 2008

14. **The outlook for 2008 remains positive despite the macroeconomic challenges posed by recent developments.** The government is committed to taking the measures necessary to maintain fiscal and economic stability for the remainder of 2008, contain inflationary pressures, and avoid accumulation of new domestic arrears for the year as a whole. We recognize that achieving these objectives will require vigorous and timely implementation of agreed policy measures and close cooperation between fiscal and monetary authorities. The government will continue to make every effort to speed up structural reforms, particularly in the areas of public expenditure management and revenue collection.

A. Macroeconomic Outlook

15. **Real GDP growth is still expected to increase to over 3 percent in 2008, from 2.7 percent in 2007, which is markedly above the average of 2.2 percent for the last four years.** A return of normal rains, a slight increase in cashew production, and increasing construction, mainly due to public works, is expected to underpin economic expansion in 2008.

16. **Inflation, on the other hand, is now expected to be higher in 2008 than previously projected assuming continued high food and fuel prices.** Given current international price projections for food and fuel products, inflation would average about 7 percent in 2008, compared to the initial projection of 3.3 percent. Unpredictably high import prices for food and fuel will also affect the country's external position; the external current account deficit (excluding official transfers) is now expected to widen to 17 percent of GDP in 2008, compared to the 12 percent initially projected.

B. Fiscal Policy

17. **The 2008 fiscal framework will remain very tight.** A number of factors are adding pressure, such as (i) revenue loss from import tax exemptions; (ii) additional spending on coming elections; (iii) higher costs of domestic financing associated with the new borrowing in 2008 and higher than expected debt owed to the BCEAO; and

(iv) losses in the CFA value of U.S. dollar-denominated external support, though these are partially offset by lower debt service on dollar-denominated debt.

18. **Despite the pressures the government remains committed to reducing the domestic primary deficit to CFAF 8.8 billion (4.7 percent of GDP) in 2008 (before additional gap-filling fiscal measures), slightly higher than the deficit of CFAF 7.5 billion (4.1 percent of GDP) initially expected but still a substantial decline from 2007.** For the remainder of the year, the government is determined to keep domestic expenditures within available resources, both domestic and external.

19. **The larger deficit reflects mainly higher domestic primary expenditures (by CFAF 1.3 billion, 0.7 percent of GDP), reflecting mainly the cost of additional election expenditures.** Specifically, the revised expenditure framework reflects the following:

- Election expenditures will be higher by CFAF 1.3 billion because of payment of arrears from previous elections.³
- The government will maintain its nominal freeze of the 2008 wage bill at CFAF 21.3 billion (before additional gap-filling fiscal measures). We also intend to consolidate the wage bill database to remove duplications in salary and pension payments for the same individual. The recent census of military personnel will also allow for more accurate payment of wages to military, which may result in budgetary savings.
- The government will strictly control nonwage discretionary outlays by adhering to the procedures requiring that expenditures be paid only through the Treasury account at the BCEAO. We government will also ensure that any nonaccounted or nonregularized expenditures will be regularized within 48 hours so that they are fully reflected in the expenditures tables of the National Direction of Budget at the end of each month.

20. **In other current expenditures, total interest costs should stay in line with program projections.** Higher domestic interest will be offset by lower interest on external borrowing denominated in U.S. dollars.

21. **The government intends to hold total revenues at CFAF 37.6 billion (20 percent of GDP) for 2008 as a whole.** A number of offsetting factors are expected to impact 2008 revenue performance:

³ These arrears from previous elections will be included in the EU audit of all domestic arrears now underway.

- **Import duties are expected to fall short of projections by some CFAF 0.6 billion (0.3 percent of GDP) because of the tax exemptions on rice imports.**⁴
- **The shortfall in revenue from rice imports will be offset by the strong collection of non-import-tax revenues;** tax revenues have already over performed by some CFAF 0.5 billion (0.3 percent of GDP) in the first quarter of the year and are expected to remain strong for the remainder of 2008.
- **Nontax revenues are expected to remain unchanged at CFAF 16.9 billion for 2008.** The government will work to improve collection of fishing penalties and fishing licenses.

22. **Budget support identified for 2008 is now estimated at CFAF 26.1 billion, some CFAF 1.3 billion higher than expected.** The government confirmed with Guinea-Bissau's external partners the amounts and timing of disbursements pledged for the remainder of 2008. The estimated budget support for 2008 includes new support from both traditional and nontraditional donors that more than compensates for shortfalls in some expected pledges and for losses in the CFA value of U.S. dollar-denominated support.

23. **Domestic financing costs will be higher than the program expected (by CFAF 3.8 billion), reflecting mainly higher debt owed to the BCEAO in 2008.**⁵ There are also some shortfalls in CFA terms compared to program expectations related to both external debt relief and the EPCA purchase.

24. **As a result of all these developments there remains a financing gap of some CFAF 5 billion for 2008.** Among measures to fill the gap are the following:

- (i) Reduce expenditures by CFAF 0.5 billion by ensuring that the expenditure savings already achieved in the first quarter are translated into permanent cuts for the year as a whole.
- (ii) To achieve expenditure savings of CFAF 0.3 billion, consolidate the government payroll database and remove duplications in salary and pension payments paid to the same civil servant.

⁴ Program projections of import tax revenues assumed reference prices used to calculate import duties on rice that are unchanged from 2007. The revised estimates, therefore, reflect only the shortfall related to tax exemptions. Revised projections assuming reference prices in line with actual import costs would yield substantially higher revenues for 2008.

⁵ Debt owed to the BCEAO has been revised upward to include payment of 2006 and 2007 arrears that were not previously assumed to be paid in 2008.

- (iii) Raise additional revenue (CFAF 0.5 billion) from customs, sales taxes, and non-tax revenues (licenses).
- (iv) Recover tax arrears of CFAF 1.2 billion, including CFAF 0.7 billion already budgeted and CFAF 0.5 billion in additional efforts.
- (v) Reschedule debt owed to the BCEAO in 2008 (CFAF 3.2 billion).

25. With these additional fiscal efforts (the above revenue and expenditure efforts total CFAF 2.5 billion), the domestic primary deficit should decline to CFAF 6.3 billion for 2008 (3.3 percent of GDP).⁶

26. **These measures, along with the second EPCA purchase (SDR 1.775 million), should fully cover the financing gap and allow Guinea-Bissau to avoid accumulating 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 domestic debt to the extent possible. The government also intends to hold later this year a meeting to follow up on the November 2006 Round Table Conference to 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 commercial debt, treasury bills, and audited domestic arrears, and to increase priority spending in social sectors above budgeted levels, in consultation with the Fund.

C. Structural Reforms in 2008

27. **The government intends to undertake additional structural policies in the fiscal area for the remainder of 2008.** These measures go beyond the commitments made already for the EPCA-supported program and focus on further strengthening revenue collection and improving public expenditure management. The additional measures planned:

- (i) Upgrade the automated customs systems to ASYCUDA++ (Automated System for Custom Administration).
- (ii) Sign a contract with a pre-shipment inspection agency (*Audit Contrôle Expertise*).
- (iii) Revitalize the PNG Committee of the BCEAO and Ministry of Finance with weekly meetings to reconcile Treasury operations with BCEAO and domestic banks.

28. **To the extent that inflationary pressures in Guinea Bissau reflect the increase in liquidity since 2007, the BCEAO will step up its efforts to sterilize**

⁶ Revised quantitative indicator for end-2008.

excess liquidity in the market. The government will also work to improve coordination between the Minister of Finance and the BCEAO to improve the latter's liquidity forecasting and ensure timely action to smooth the monetary impact of use of donor funds to finance government expenditures.

D. Capacity Building and Technical Assistance

29. **Capacity building remains a key complement to fiscal reform if we are to ensure that reform is effective and sustainable.** Technical assistance needs continue in all areas of public financial management and in macroeconomic statistics (Table 3). The highest priority continues to be 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 statistics. The European Union and the World Bank, through its support to low-income countries under stress (LICUS), are also assisting with these reforms.

E. Program Monitoring

30. **Monitoring of progress on the EPCA-supported program for the remainder of 2008 will be based on revised quantitative and structural indicators (see Tables 1 and 2).** 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; (v) a ceiling on payment of previous arrears; (vi) no short- or long-term nonconcessional external borrowing; and (vii) a ceiling on nonregularized expenditures (new indicator). The quantitative indicators are based on the revised 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 TMU.

31. **To demonstrate their commitment to the success of the program, the government intends to take the following measures before August:** (i) collect at least CFAF 300 million in tax arrears; (ii) regularize all nonaccounted expenditures for 2007 through April 2008 so that they are fully reflected in the expenditures tables of the National Direction of Budget; (iii) sign a contract with Audit Contrôle Expertise; and (iv) revitalize the PNG Committee of the BCEAO and Ministry of Finance with weekly meetings.

⁷ The monthly cash flow plan also serves as an informal indicative framework for regular assessment of EPCA performance.

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

	2008								
	End-Mar.			End-Jun.		End-Sep.		End-Dec.	
	Prog	Prog. Adj.	Actual	Prog	Prog. Rev.	Prog	Prog. Rev.	Prog	Prog. Rev.
1. Government Revenues 2/	4,226.6	4,226.6	4,609.9	10,413.9	11,388.7	17,824.3	19,162.1	23,130.4	24,580.3
Tax revenues (direct and indirect taxes (01.00.00 and 02.00.00))	3,635.0		4,116.8	9,230.7	9,993.5	16,049.5	16,483.3	20,764.0	20,753.9
Recovery of tax arrears and additional revenue effort					252.2		903.9		1,460.0
Fishing licenses (03.01.01)	591.6		493.1	1,183.2	1,143.0	1,774.8	1,774.8	2,366.4	2,366.4
2. Domestic primary deficit (commitment basis) 3/	-5,050.0	-5,050.0	-3,841.5	-4,861.7	-2,683.0	-3,522.1	-1,352.8	-7,463.7	-6,282
3. Domestic financing of the budget 4/	-238.7	5,865.8	2,094.3	-7,445.7	-5,053.0	-7,684.3	-7,398.7	-17,331.6	-15,036
4. New domestic arrears 5/	0.0	3,771.5	4,549.8	0.0		0.0		0.0	0.0
5. Payment of previous years arrears 6/	1,772.0	1,772.0	3,456.8	3,600.0		3,600.0		3,600.0	3,600.0
6. External nonconcessional public borrowing, maturity > 1 year	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
7. Non regularized expenditures (DNTs)			573.5		-596.4		200.0		200.0

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. 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. 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 2. Guinea Bissau: Structural Benchmarks Under the
Emergency Post-Conflict Assistance
January 1, 2008—December 31, 2008

	Target date	Status
Submit to Parliament 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
Approve and adopt by Council of Ministers legal framework for new state budget classification system in line with WAEMU regulations.	End-March 2008	Met with delay; approved in May.
Create an Information Technology (IT) Department in Ministry of Finance and start training staff.	End-March 2008	Done
Launch financial audit, by a reputable international firm, of domestic arrears for 2000-07. ⁸	End-April 2008	Met with delay; audit launched in May 2008.
Regularize all nonaccounted expenditures for end-2007 and end-April 2008 so that they are fully reflected in the expenditure tables of the National Direction of Budget.	End-May 2008	Met with delay; expenditures regularized as of July 10
Sign a contract with a pre-shipment inspection agency (Audit Contrôle Expertise).	End-June 2008	Done
Revitalize the PNG Committee of the BCEAO and Ministry of Finance with weekly meetings to reconcile Treasury operations with BCEAO and domestic banks.	End-June 2008	Done
Improve accounting and information flows of all Treasury transactions, including nonregularized expenditures (within 48 hours) and bank financing.	End-June 2008	In progress
Collect at least CFAF 300 million in tax arrears.	End-July 2008	

⁸ Audit financed by the European Union.

Table 2. Guinea Bissau: Structural Benchmarks Under the
Emergency Post-Conflict Assistance
January 1, 2008—December 31, 2008

	Target date	Status
Install new software for payroll and personnel management in order to merge the payroll databases of the Ministry of Finance and Ministry of Public Administration.	End-September 2008	
Implement an integrated management system for public accounts, linking data flows between customs (DGA), the tax department (DGCI), the budget office (DGO), and the Treasury	End-December 2008	
Upgrade the automated custom systems to ASYCUDA++ (Automated System for Customs Administrations).	End-December 2008	

Table 3. Technical Assistance Needs of the Ministry of Finance

Department	Area	Long-term	Short-term	(Possible) Provider
Minister's Cabinet	Macroeconomic advisor	X ¹		(WB LICUS/IMF) ²
Budget	Expert public finance	X		(EU)
	Expert computer systems	X		(EU)
	Computerization expenditure accounts	X ²		EU
	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 4. Guinea-Bissau: Treasury Cash-Flow Plan 2008
(CFAF millions)

	Jan.	Feb.	Mar.	Q1		Q2		Q3		Q4		Jan-Dec	Jan-Dec
	Act/Proj	Act/Proj	Act/Proj	EPCA	Act/Proj	EPCA	Proj.	EPCA	Proj.	EPCA	Proj.	EPCA	Proj.
A. Revenue and grants	2,202	3,489	1,556	9,810	7,248	14,766	16,757	17,676	15,380	9,249	12,658	51,501	52,043
Revenue	2,025	2,989	1,556	5,998	6,571	11,462	11,967	12,726	12,488	7,445	6,588	37,631	37,613
Taxes	1,713	1,239	1,165	3,635	4,117	5,596	5,877	6,819	6,490	4,714	4,271	20,764	20,754
Nontax revenue	312	1,750	391	2,363	2,454	5,866	6,090	5,907	5,998	2,730	2,318	16,867	16,859
Expected budget support	177	500	0	3,812	677	3,304	4,791	4,950	2,893	1,804	6,069	13,869	14,430
B. Expenditure	4,025	3,137	3,183	11,594	10,344	11,920	12,714	11,785	12,790	12,032	13,222	47,331	49,070
Current expenditure	3,882	2,980	3,171	11,297	10,033	11,398	12,235	11,150	12,140	11,397	12,573	45,242	46,981
Wages and salaries	1,735	1,732	1,782	5,330	5,250	5,330	5,467	5,330	5,302	5,330	5,302	21,322	21,322
Goods and services	446	254	317	1,784	1,017	1,784	1,924	1,784	2,097	1,784	2,097	7,134	7,134
Transfers	1,219	715	716	2,806	2,650	2,806	2,762	2,806	2,906	2,806	2,906	11,224	11,224
Other current expenditure	120	200	292	832	612	832	1,116	832	1,450	832	1,450	3,327	4,627
<i>Of which: Restitutions + Incentives + Others</i>	120	0	288	608	408	608	604	608	710	608	710	2,432	2,432
Interest on domestic and foreign debt	362	80	64	546	505	646	966	399	386	645	818	2,236	2,675
Interest on domestic and regional debt	80	10	56	172	146	172	607	172	185	172	402	690	1,340
Interest on foreign debt	282	70	8	373	360	474	360	226	200	473	416	1,546	1,335
Capital expenditure (domestically financed)	143	156	11	297	311	522	479	635	649	635	649	2,089	2,089
C. Extrabudgetary expenditures (DNT + tax compensations)			574	0	574	0	-574	0	0	0	0	0	0
D. Overall domestic balance: A - (B+C)	-1,822	353	-2,200	-1,784	-3,670	2,846	4,616	5,891	2,591	-2,783	-564	4,170	2,973
E. Payment of domestic arrears and complementary period	0	0	3,457	1,772	3,457	1,828	143	0	0	0	0	3,600	3,600
2007: complementary period + rest			3,457	1,772	3,457	1,828	143	0	0	0	0	3,600	3,600
F. Overall domestic balance (cash basis) D-E	-1,822	353	-5,657	-3,556	-7,127	1,018	4,473	5,891	2,591	-2,783	-564	570	-627
Financing	1,822	-353	5,657	3,556	7,127	-1,018	-4,473	-5,891	-2,591	2,783	564	-570	627
Domestic financing	0	0	2,094	-239	2,094	-5,483	-5,423	-239	-5,546	-2,907	-3,728	-8,868	-12,603
Bank financing	0	0	2,094	-239	2,094	-5,483	-5,423	-239	-5,546	-2,907	-3,728	-8,868	-12,603
BCEAO	0	0	0	-239	0	-239	-958	-239	-2,037	-990	-1,674	-1,706	-4,668
Commercial banks	0	0	2,094	0	2,094	-5,244	-4,465	0	-3,509	-1,917	-2,055	-7,161	-7,934
Nonbank financing (incl. privatization)	0	0	0	0	0	0	0	0	0	0	0	0	0
T-bills and regional commercial banks (net)	0	0	0	0	0	-1,724	-1,724	0	0	-6,740	-6,740	-8,464	-8,464
Amortization of external debt	-847	-133	-35	-1,020	-1,015	-1,630	-1,303	-388	-425	-1,882	-1,556	-4,920	-4,299
Financing requirements (+ = financing needs flow)	2,669	-220	3,597	4,815	6,047	7,819	3,977	-5,264	3,380	14,312	12,589	21,682	25,993
Additional identified budget support	0	0	0	2,970	0	6,233	2,442	849	5,441	849	3,785	10,900	11,668
EPCA	1,251			1,386	1,251	0	0	1,386	1,251	0	0	2,772	2,502
World Bank debt relief	81	128	34	284	243	1,810	1,547	284	243	1,810	1,547	4,188	3,579
Authorities' measures	0	0	4	175	4	175	177	175	260	3,329	3,090	3,854	3,531
Recovery of tax arrears	0	0	4	175	4	175	177	175	260	175	260	700	700
T-bills rescheduling	0	0	0	0	0	0	0	0	0	3,154	2,831	3,154	2,831
Additional Authorities' measures							186		4,187		627		5,000
Additional recovery of tax arrears							0		430		70		500
Additional revenue efforts (including exploration licenses)							71		214		214		500
Expenditure savings							43		129		129		300
Expenditure reduction							71		214		214		500
BCEAO debt rescheduling									3,200				3,200
Financing gap (flow) (+ = financing needs)	1,338	-348	3,560	0	4,550	-398	-374	-7,958	-8,001	8,356	3,540	0	-286
Financing gap (+ = financing needs accumulated stock)	1,338	990	4,550	0	4,550	-399	4,176	-8,356	-3,826	0	-286		

ATTACHMENT II
TECHNICAL MEMORANDUM OF UNDERSTANDING

Bissau, May 22, 2008

1. This memorandum describes the definitions of the quantitative indicators for the Program for 2008 to be supported by 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
 - g. cumulative ceiling on the amount of nonregularized expenditures

Quantitative indicators have been set for 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 EPCA purposes, the government is defined as the central government of Guinea-Bissau.** This definition excludes public entities with autonomous legal personality whose budget is not included in the central government budget.

4. For the targeted ceiling presented in Table 1, government revenues include direct taxes, indirect taxes, and fishing licenses, as well as negotiated recovery of tax arrears and additional revenue efforts. The cash flow estimates are based on tax revenue and fishing license income originally programmed for 2008.

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

	Mar. Actual	Jun. Prog. Rev.	Sept. Prog. Rev.	Dec. Prog. Rev.
1. Government Revenues	4,609.9	11,388.7	19,162.1	24,580.3
Tax revenues (direct, 01.00.00, and indirect, 02.00.00, taxes)	4,116.8	9,993.5	16,483.3	20,753.9
Recovery of tax arrears and additional revenue effort		252.2	903.9	1,460.0
Fishing licenses (03.01.01)	493.1	1,143.0	1,774.8	2,366.4

Source: Cash Flow 2008 revised

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. 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.

Table 2. Estimates of the Quarterly Domestic Primary Balance, New Domestic Arrears, and Payment of Previous Years' Arrears, 2008
(Cumulative, CFAF millions)

	Mar. Actual	Jun. Prog. Rev.	Sept. Prog. Rev.	Dec. Prog. Rev.
1. Total domestic primary deficit	-3,842	-3,049	-2,966	-8,782
Revenue	6,571	18,537	31,025	37,613
Domestic primary expenditure	10,412	21,587	33,991	46,395
Authorities' measures (higher revenues + lower expenditures)	0	366	1,613	2,500
2. New domestic arrears	4,550	0	0	0
Wages and other expenditures on personnel (including pensions)	--	0	0	0
Nonpersonnel expenditures	--	0	0	0
3. Nonregularized expenditures (DNTs)	574	200	200	200
4. Payment of previous years' domestic arrears	3,457	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, the stock of account payables (*rest-a-payer*).

(ii) At end-December, as accounts payables accumulated during 2008 and still outstanding one month after December 31 in the case of wages and salaries (including pensions), and three months after in the case of goods and services and transfers.

The targets for the program period are presented in Table 2.

7. **Nonregistered expenditures are defined as follows:** any Treasury outlay (including nontitularized expenditures, restitutions, etc.) not accounted for and therefore not reflected in the expenditures tables presented by the National Direction of Budget.

8. **Previous year's domestic arrears are defined as arrears in wages, transfers, and goods and services** outstanding as of January 1, 2008. The targets for the program period are presented in Table 2. The program allows for partial payment of expenditure commitments related to 2007 that are still outstanding as of January 1, 2008, up to a maximum of CFAF 3.6 billion (see MEFP ¶ 14).

9. **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 net changes in the balances of the treasury accounts at the BCEAO and at commercial banks (excluding balances in those accounts that are not available for budget financing, such as accounts that are held under double signature arrangements with donors) and the outstanding amounts of loans, including T-bills, from the BCEAO and commercial banks (local and regional). Domestic nonbank financing encompasses privatization receipts and any other domestic financial debt held outside the banking sector, other than new domestic arrears as defined above, that may arise. Table 3 provides the details.

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

	Mar. Actual	Jun. Prog. Rev.	Sept. Prog. Rev.	Dec. Prog. Rev.
Domestic financing	2,094	-5,053	-7,399	-15,036
Bank financing	2,094	-5,053	-7,399	-15,036
BCEAO	0	-958	-2,995	-4,668
BCEAO rescheduling	0	0	3,200	3,200
Commercial bank(s) (including regional banks)	2,094	-2,371	-5,880	-7,934
Regional Commercial banks and Treasury bills	0	-1,724	-1,724	-8,464
T-bills rescheduling	0	0	0	2,831
Non bank financing	0	0	0	0

Source: Table 2, MEFP

10. **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 EPCA purposes, 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, i.e., not contingent, liability, 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) in time; 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 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, i.e., 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, i.e., 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 purposes 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 that cover the operation, repair, or maintenance of the property. Under this definition of debt, arrears, penalties, and judicially awarded damages arising from the failure to make payment on 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 date the loan is contracted, 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 10-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.

11. The concept of government for the purposes of the indicators on 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

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

12. 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:⁹

- **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.

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-June CFAF 15.7 billions; by end-September CFAF 26.04 billions; and by end December CFAF 35.8 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 support, the ceiling on the accumulation of new domestic arrears of nonpersonnel expenditures will be adjusted upward (downward) by that difference.

⁹ For the purposes of the TMU, the CFAF/US\$ exchange rate was updated to 426,6 and the CFAF/Euro exchange rate is 656.

II. PROGRAM MONITORING

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

- 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 extrabudgetary expenditure (not included above), including: (i) incentives to tax collectors; (ii) restitutions to collecting agencies; and (iii) 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 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 after 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);
- Treasury Committee monthly reports (monthly, within 10 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 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.

14. **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.**

15. The above data will be provided to the economist at the local office of the IMF in Bissau (Mr. Fonseca) for transfer to the African Department of the IMF in Washington.