International Monetary Fund

Rwanda and the IMF

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July 31, 2009

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Rwanda: Letter of Intent and Memorandum of Economic and Financial Policies

July 23, 2009

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

Letter of Intent

Kigali, July 23, 2009

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

Dear Mr. Strauss-Kahn:

1. The fifth review of our financial and economic program support under the Fund's Poverty Reduction and Growth Facility (PRGF) was completed on January 12, 2009. In the attached Memorandum of Economic and Financial Policies (MEFP) we review recent economic developments and progress in the implementation of our program through the first half of 2009, and set out policies for the medium term.

2. Program implementation under the PRGF arrangement has been broadly on track. All performance criteria for end December 2008 were met. The indicative target on the net present value of external debt was not met, reflecting higher absorptive capacity of projects, which accelerated disbursement of existing loans. Due to severe external shocks affecting Rwanda, several indicative targets for end March 2009 were missed.

3. Rwanda is affected by the global crisis, and its growth rate will slow from 11.2 percent in 2008 to an expected 5.3 percent in 2009. Falling demand in international markets and related decline in world prices will adversely affect our balance of payment. Our macroeconomic framework has been adjusted to reflect this impact.

4. To proceed with the rehabilitation and financing of Kigali's urban road network, the Government of Rwanda has contracted a nonconcessional external loan and requests a waiver for the continuous performance criterion on contracting of nonconcessional debt. This project is important to address our infrastructure and urban development needs.

5. The Government of Rwanda also requests a waiver for the continuous performance criterion on nonintroduction of multiple currency practice (MCP). In March, the National Bank of Rwanda introduced a foreign exchange risk hedging facility for the commercial banks in order to encourage foreign borrowing and longer-term domestic lending. As the facility has created an MCP, it was removed in June, before it was used.

6. The Government of Rwanda has the intention to seek a new program with the IMF under the Policy Support Instrument (PSI) as a follow-up program to the PRGF arrangement. We would like to hold discussions on the new program in early 2010 at the time of the consideration of the budget for the new fiscal year July 2010/June 2011.

7. In the meantime, we have developed a medium-term macroeconomic framework with indicative quantitative targets and policy plans. A detailed macroeconomic program was also developed for June 2009 to July 2010. This will help bridge the gap between the end of economic program supported by the PRGF arrangement and the beginning of the successor program.

8. In support of our policies described in the MEFP, the Government of Rwanda requests completion of the sixth review under the PRGF arrangement and disbursement of the seventh loan of SDR 1.17 million.

9. The Government of Rwanda believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of its program but will take any further measures that may become appropriate for this purpose. The Government of Rwanda will consult with the Fund on the adoption of these measures and in advance of revisions to the policies contained in the MEFP, in accordance with the Fund's policies on such consultations.

10. The Government of Rwanda authorizes the publication and distribution of this letter and MEFP together with the related staff report.

Sincerely yours,

/s/	/s/
François Kanimba	James Musoni
Governor National Bank of Rwanda	Minister of Finance and Economic Planning

Attachment: Memorandum of Economic and Financial Policies

Attachment 1:

Memorandum of Economic and Financial Polices (MEFP) of the Government of Rwanda

July 23, 2009

1. The Government of Rwanda remains committed to achieving sustained economic growth and poverty reduction through the pursuit of prudent economic and social policies as well as structural reforms. The strategies to achieve these goals are set out in the Economic Development and Poverty Reduction Strategy (EDPRS) as well as in the Vision 2020 development plan. This memorandum of economic and financial policies (MEFP) reviews performance under the program supported by the IMF's Poverty Reduction and Growth Facility (PRGF) and describes the policies and targets for the medium-term as well as for the fiscal year July 2009/June 2010. The Government of Rwanda has the intention to seek a program with the IMF under the Policy Support Instrument (PSI) as a follow-up program to the PRGF. We would like to hold discussions on the new program in early 2010 at the time of the consideration of the budget for the new fiscal year July 2010/June 2011.

I. Recent Economic Development

2. Growth was strong in 2008 and reached 11.2 percent. This is the first double-digit real GDP growth in the last five years, which was achieved despite the volatile international financial crisis. Agriculture led the way with a real growth of 15 percent. This sector benefited from the favorable weather conditions as well as Government's crops intensification program supported with fertilizer application, improved seeds and storage facilities.

3. Despite monetary tightening, inflation accelerated in 2008. Rising prices of food, transport and housing and utilities pushed inflation to 22.3 percent by end December. The average annual inflation was 15.4 percent. These developments partly reflect the pass-through of the high international food and fuel prices that also affected domestic food prices.

4. Fiscal performance was also strong. Total revenue collections at 15.6 percent of GDP were higher than programmed in 2008 because of higher growth, inflation, increased monetization of the economy and "one off" payments. Tax revenue collections were 19.5 percent higher than programmed and reached 13.5 percent of GDP benefiting from the collection of tax arrears of RWANDATEL. Non-tax collections that contributed about 2.1 percent of GDP to revenues were RWF 30 billion higher than programmed on account of "one off" accrual of RWF33.4 billion (US$60 million, 1.4 percent of GDP) in mobile license fees from TIGO company.

5. Government spending on priority programs accelerated during the second half of the year because of the purchases of seeds and fertilizer and spending on storage facilities (largely financed by grants from IDA and AfDB) and maintenance of the road network. The accrual of the additional revenue during the year allowed the Government to increase outlays for various energy, water and sanitation projects in line with the EDPRS.

6. All end-2008 fiscal program targets were met. In the case of the targets for net credit to Government (NCG), domestic fiscal balance (DFB) and priority spending, these were met with comfortable margins largely on account of the "one-off "receipts. The net liquidity impact of fiscal operations, given the high import content of the budget, amounted to 2.7 percent of GDP in 2008, lower than envisaged in the program.

7. The external current account deteriorated sharply compared to 2007. Despite a strong increase in export receipts from coffee, tea, minerals and tourism, the trade deficit widened because of rising import volumes and a surge in food and fuel prices. As a result the terms of trade also deteriorated sharply in 2008. The accrual of donor disbursements together with the inflow of the fees for the mobile license by TIGO led to an increase in gross official reserves from 4.8 months at end 2007 to 5.3 months by end 2008.

8. Regarding the exchange rate policy, over 2008 the Rwandan Franc depreciated by almost 2 percent against the U.S. dollar; however due to the high inflation in 2008, the Rwandan appreciated significantly in real terms against the dollar during the year. It is worth noting that more foreign exchange was sold in 2008 than in 2007, partly reflecting the high demand for imports. However, the stock of foreign exchange has increased over the year as a result of donor disbursements made during 2008 and the large sale of the telecommunication license.

9. The end December 2008 targets for reserve money and Net Foreign Assets (NFA) were met. However, there was a persistence of high levels of currency in circulation and vault cash, which increased in the face of rapid pace of economic growth, inflationary developments and the opening of new bank branch networks. NBR relied more on the sale of foreign exchange for sterilization purposes rather than on the issuance of domestic instruments. As a result, domestic debt declined sharply in 2008. This policy was also in response to the demand of both the private sector and Government for foreign exchange to finance the high cost of imports in 2008.

10. Broad money growth declined to 5.5 percent at end 2008, which was well below the program projections. The broad money even began to decrease in nominal terms from November 2008 due to falling deposits. The decline in deposits was mainly the result of some large depositors withdrawing their deposits for long term investment both locally and externally. By end-2008 there was a tightening of the liquidity in the banking system. The Central Bank responded to this situation by (i) reducing the reserve requirement ratio by

3 percentage points from 8 percent to 5 percent in early 2009, as well as significantly reducing the stock of outstanding domestic assets (including treasury bills and repos).

II. Structural Reforms

11. Significant progress has been made in developing Rwanda's financial sector. The number of people accessing formal financial services increased. In line with the objective of the government to increase access to financial services to the population, in 2008 the Central Bank licensed two more commercial banks. These are Banque Populaire du Rwanda which was upgraded from a microfinance institution and the Kenya Commercial Bank Rwanda. In addition, NBR permitted the establishment of 23 new microfinance institutions. Furthermore, six new commercial bank branches were opened in 2008. The total number of beneficiaries of formal financial services has increased by 29.5 percent from 2007 to 2008.[1] Structural reforms continued to be developed across the sector, with notable achievements including:

- *Amendments made to the Central Bank Act*. These amendments, made in February 2008, gave NBR the authority to regulate the non-banking financial sector, comprising insurance companies, brokers and pension funds. The Central Bank will be able to draw from its experience in regulating the banking sector to ensure the safety and soundness of the non bank financial sector.

- *A number of systems have been implemented by NBR under the new National Payments Strategy***.** As planned, the switch for card-based payments is operational. A number of key supporting policies are close to being ready for full implementation, including the operation of the Automated Clearing House and the Real Time Gross Settlement system (integrated with the Central Securities Depository). In addition, a National Payments Council has been established to oversee and advise this process, which involves representation from the commercial banks, MFIs, Government, teams involved in the national switch-over, telecoms representatives and the Rwandan Development Board.

- *The Insurance Sector Law came into force in March 2009.* The core set of implementing regulations have been released for comments by the industry and will be issued as soon as these comments are discussed and evaluated.

- *In line with the license issued in 2008, a private credit reference bureau will be operational before the end of 2009*. The private credit bureau will replace the public credit bureau housed at the Central Bank and will now also cover microfinance

[1] Beneficiaries of all formal financial services (including microfinance institutions) increased from 1.4 million in 2007 to 1.8 million in 2008.

institutions. The purpose of the new bureau will be to compile information concerning the repayment behaviour of individuals and businesses and will organize this information for resale to banks, credit providers, insurance companies and other eligible entities. The information provided by credit bureaus is used by credit providers to better assess the risks posed by a particular credit application, based on the credit customer's ability to manage credit in the past. Credit Bureaus are an essential component in the development of a sound financial sector and a robust credit industry.

12. Progress has been made in reforming Public Financial Management (PFM) in 2008 and early 2009.

- *The PFM Reform Strategy (2008-2012) was approved by Cabinet in December 2008*. Since the strategy was approved, a PFM steering committee has been established and the first meetings were held in early 2009. To further embed the principles of PFM, a Manual of Budget Processes and Procedures has recently been approved and training on the content has been scheduled for July 2009. In addition, the piloting of an Integrated Personnel and Payroll Information System has been successfully managed by MIFOTRA, with civil servant salaries paid through this route since February 2009. Further pilots are due across a number of other Ministries over 2009, streamlining payment processes.

- *Embedding the principles of MTEF at every level of government*. The government's MTEF manual formalized practices already in use across the budget process. Indeed, the practices outlined in this document were central to formulating the mini-budget for 2009 as well as the budget for the new financial year 2009/10 that was recently approved by the Parliament. To ensure complete implementation of the manual across all budget agencies, MINECOFIN is currently recruiting a consultant to undertake comprehensive training of all planning and budgeting officers to reinforce the MTEF principles. An appointment will be made by the end of June 2009, with training to commence shortly after.

- *The Government and development partners signed a memorandum for budget support harmonization*. Sector-Wide Approaches (SWAPs), designed to harmonize and align donor interventions, were adopted in the energy, transport and agriculture sectors.

III. Program Performance in the First Half of 2009

13. Multiple external and domestic shocks affected economic performance during the first half of 2009. These shocks are expected to reduce demand for exports, especially minerals, reduce income and revenues from tourism and remittances, as well as foreign direct investments. Despite these shocks, performance at end March 2009 was satisfactory as inflation decelerated on account of good season A harvest.

14. Two indicative fiscal targets for end March were missed. The targets for Net Credit to Government (NCG) and the Domestic Fiscal Balance (DFB) were missed by some margins. These targets were missed mostly because of the delayed disbursement of budget support grants from the World Bank and the need to finance the DRC military operations, as well as the frontloading of some priority expenditures. The Government financed these expenditures by drawing down deposits in NBR. The target spending for priority expenditures was met with a significant margin.

15. The indicative target for net repayment of domestic arrears was also missed at end March. This reflected delays in implementing new payment procedures to reduce frauds and increase transparency in payments. Where payments orders did not meet all legal requirements, these were cancelled and re-issued subsequently. Moreover currently, there is lack of synchronization between the payment information system of MINECOFIN and NBR as this is done manually, resulting in a perceived accumulation of arrears though payments by NBR have been effected. Efforts are ongoing to provide an electronic interface between the two softwares (using SmartGov). This will allow automatic synchronized recording of all payments. In the second quarter, there was a sharp reduction of arrears as payments accelerated; as a result end-June target is likely to be met with a margin.

16. Revenue collection during the first quarter matched projections despite the impact of the world economic crisis. Tax and customs revenue collections exceeded projections reflecting a still robust economic growth at the end of 2008 and delayed high imports in early 2009. These imports contained a large portion of capital goods that were partly funded by a drawdown of Government deposits.

17. Government spending exceeded program projections by about RWF 12 billion during the first quarter on account of the internationally approved military operations in the DRC at the beginning of the year, as well as the frontloading of spending on telecommunications, water and energy projects.

18. The impact of the external shocks were felt in the early months of 2009 as exports declined by about 10 percent in U.S. dollar value terms in the first quarter compared to the same period last year. On the other hand, imports in value terms were about 58 percent higher than in the corresponding period of 2008. This reflected delays in arrival of imports

contracted last year at high prices as well as a still robust economic growth at end 2008. As a result the trade deficit widened significantly compared to the same period last year.

19. The Net Foreign Assets (NFA) of NBR declined sharply by about 22percent during the first quarter of 2009. This reflected the delayed disbursements of budget support grants from the World Bank and the need to sell foreign exchange to support import activities. The end-March NFA indicative target was thus missed. Broad money also declined by about 8 percent during the same period, reflecting a decline in currency in circulation and deposits. These developments also reflected the tight liquidity situation in the first quarter of 2009.

20. Regarding fiscal performance in the first half of 2009, the continuing economic growth, high imports and improvements in Rwanda Revenue Authority's (RRA) efficiency will likely keep revenue collections at the level projected for this period. Strict adherence to expenditure allocation levels as well as enforcement of spending procedures are expected to reduce the incidence of over-spending as well as avoid arrears build up by ministries and agencies. According to our preliminary information, Net Credit to Government and Domestic Fiscal Balance indicative targets for end June 2009 are likely to be missed on account of (i) delays of disbursement of sector budget support grants, and (ii) expenditures related to the military operations in DRC, which were not foreseen when program targets were set. The Priority Expenditure target was likely met with a comfortable margin.

IV. Macroeconomic Outlook and Medium Term Strategy

21. Multiple external and domestic shocks are expected to continue to impact on economic performance for the rest of the year as well as for the medium term, in particular:

- Real GDP growth will be led by the agriculture sector, which will continue to benefit from investment in inputs and extension services. This is evident in the strong harvest observed in season A. However, growth in the medium term is expected to be lower than the exceptional performance in 2008/09.

- The global economic and financial crisis will impact negatively on economic performance by reducing financial inflows through two main channels; (i) declining external demand for Rwandan goods and services with tourism and minerals strongly hit and (ii) reducing other financial inflows including remittances and FDIs.

- The current liquidity shortage could exacerbate the impact of the global financial crisis by reducing the availability of domestic credit for growth. The stock of credit to the private sector had already declined by 0.5 percent during the first four months of 2009.

22. In light of these factors, real GDP growth is projected to slow down in 2009–10. Real GDP growth is expected to decline from the estimated 11.2 percent in 2008 to about 5.5 percent in 2009/2010 reflecting the slowdown of non agricultural growth. Construction and real estate, mining hotel and restaurants and trade will be particularly affected by the global crisis and the liquidity shortage. From 2010, however, a gradual recovery of the nonagricultural sector in line with developments in the world economy is expected. This together with a normal agricultural growth will be expected to raise real GDP growth to about 6.3 percent in 2010/11 and about 7 percent in subsequent years.

23. Inflation is projected to decline to single digits in the second half of 2009. This decline will result largely from a reduction in import prices, lower domestic food prices on account of the good harvest and an easing of domestic demand pressures. The headline inflation has already fallen from 22 percent at end December 2008 to about 12.7 percent at end May, largely reflecting slowing growth of food and housing prices. Continued prudent monetary management will be required to keep inflationary expectations down so as to achieve the target inflation rate of 5 percent in 2010.

24. The balance of payments is likely to deteriorate in 2009–2010. This reflects the sharp deterioration in the external environment as exports of goods and services are expected to decrease by about 23 percent in U.S. dollar terms in 2009 compared to 2008. This decline will be partially offset by a reduction of approximately 7 percent in imports. Despite frontloading of official foreign assistance, the current account deficit (including official transfers) is expected to deteriorate slightly from 5.5 percent of GDP in 2008 to about 6.6 percent of GDP in 2009. Foreign Direct Investment and other capital inflows are also expected to fall, resulting in the deterioration of the overall balance of payments by about US$ 80 million compared to 2008.

25. Although exports of goods and services and other private capital flows are expected to recover from 2010 as the global environment improves, the concomitant increase in imports to support the EDPRS investment needs and the projected decline in official transfers would be expected to lead to a further worsening of the balance of payments. An overall deficit of about US$ 30 million is projected for 2010. To support the projected import values in line with EDPRS investment needs, some draw down of international reserves can be accommodated in the next few years. The balance of payments is expected to improve from 2011 as the world economy recovers and demand for Rwandan goods and services increases. However, the current external shock could have a lasting impact on the reserve coverage of the country, which could stabilize at about 4 months of imports over the medium term, down from about 5.3 months at end December 2008.

26. The medium-term balance of payments projections assume greater exchange rate flexibility to stem the loss of foreign exchange reserves. This will help gradually offset the competitiveness losses that Rwanda suffered as a result of the large real appreciation in 2008.

27. Fiscal policy will have to balance the competing objectives of cushioning the impact of the economic crisis on growth and poverty reduction as envisaged in the EDPRS whilst preserving the medium-term fiscal and external sustainability. Declining revenues, and from 2010/11 lower committed external budget support, are expected to reduce the available budget resources. For fiscal year 2009/10, fiscal revenues are expected to decline by about 2.4 percent of GDP compared to 2008/09. This largely reflects absence of "one off" payments, slowing economic activity, losses from adopting the East African Community (EAC) common external tariff (CET), and elimination of value added tax on large trucks and surcharge on sugar.

28. In the medium-term, revenues are projected to increase by at least 0.2 percent of GDP per year, reflecting both economic recovery and continued increases in efficiency of tax collection. Grant financing is projected to remain high in 2009/10, but the projection for 2010/12 takes into account only the grants already committed by donors. This shows a decline of about 2–3 percent of GDP compared to the level of 2009/10. To maintain expenditures at a level of the 2009/10 as a share of GDP, projections envisage an increase in concessional borrowing.

29. The expenditure plan shows a gradual adjustment partly offsetting the reduction in resources. The total expenditure in the budget for fiscal year 2009/10 approved by Parliament amounted to 26.9 percent of GDP. A gradual reduction to about 25.2 percent of GDP by 2011/12 is envisaged. The main source of the reduction is externally financed capital expenditure, which reflects expected reduction in donor grants for capital projects. Recurrent expenditure and domestically financed capital expenditure for 2009/10 are projected at about 20.2 percent of GDP, confirming that the expenditure profile will be sufficient to achieve the objectives outlined in Rwanda's poverty reduction strategy (EDPRS). Priority expenditures will remain at about 13 percent of GDP during this period.

30. The budget deficit (excluding grants) is expected to rise sharply to 13.6 percent of GDP in the 2009/10 budget but thereafter decline to about 11.5 percent of GDP by 2011/12. The increase in 2009/10 and the subsequent decline are broadly consistent with the macroeconomic policy objectives and available financing. The projected net liquidity impact of the budget spending (about 2 percent of GDP per year in 2009/10–2011/12) will provide a stimulus to the economy without compromising the Government's objective of restraining inflation to single digits. The expanding budget deficit in 2009/10 would imply a draw down of government deposits in the NBR of up to 1 percent of GDP. This would be covered by funds from the mobile telephone license fees of about 1.4 percent of GDP received at the end of 2008. Consistent with the medium-term projections, the budget does not envisage any further domestic bank financing except for monetary policy purposes. An update of the debt sustainability analysis (DSA) indicates that the medium-term fiscal profile is broadly consistent with the maintenance of public debt at a sustainable level.

31. The Government is in the process of studying the macroeconomic implications of its plans for the pension system reform and the introduction of the Provident Fund. This will involve a possible redirection of a part of central Government revenue (and expenditure) to the Provident Fund. Given that more time is needed for the Government to assess the implications of the possible reforms for the central budget, including the revenue losses and offsetting measures for them, the budget for 2009/10 does not include these reforms, and the current medium term projections do not yet include the estimates of the impact. These will be included in the fiscal framework once the technical work has been completed.

32. Monetary policy in the medium term will be more proactive in averting balance of payment pressures as well as moderating inflation. It will also pay more attention to managing the bank liquidity situation. The NBR will continue to use reserve money as the operational target to control inflation. To achieve this objective, NBR will aim to meet the reserve money target on average and not only at end-month, through a coordinated sale of domestic and foreign sterilization instruments. NBR will work with the Fund team to develop a reserve money operational framework that would reduce volatility and improve its effectiveness as an operational target.

V. The Macroeconomic Program for Fiscal Year 2009/10

33. The fiscal year 2009/10 marks the beginning of Rwanda's aligning itself to the EAC budget calendar as well as implementing the EAC Common External Tariff (CET) from 1st July 2009 under the Customs Management Act. This implies that the customs tariff bands will change from tariff bands of 30 percent for finished products, 15 percent for semi-finished goods, 5 percent and 0 percent for raw materials to a three tariff band of 25 percent for finished goods, 10 percent for semi finished goods and 0 percent for raw materials. Under the CET, taxes on international trade will be levied at point of entry basis instead of CIF Kigali.

34. Managing the impact of the external and internal shocks on economic performance will be at the heart of our macroeconomic policies. On the real GDP growth front, we will intensify our investment and extension service activities in agriculture as the lead sector to achieve our projected growth of 5.3 percent in 2009. The expected good harvest together with our fiscal and monetary policies that are outlined below should enable us to achieve single digit inflation in mid-2009.

35. Regarding fiscal policy, the domestic fiscal deficit (excluding spending on demobilization and peacekeeping operations) is projected to rise from about 5.3 percent in calendar year 2008 to about 6.2 percent in fiscal year 2009/10. This will result from increasing allocation of budgetary resources to investment and other priority projects outlined in the EDPRS, which will provide a solid base for growth in Rwanda.

36. We expect fiscal revenues to decline by about 2.4 percent of GDP compared to 2008/09. This is due to reasons previously highlighted in paragraph 27. These losses will be partially offset by additional revenue measures introduced by the Government, which include increasing fuel levy earmarked for road maintenance, gradually eliminating implicit subsidies on petroleum products and raising excise taxes on mobile airtime.

37. In the case of expenditures, the focus lies in increasing resources to public infrastructure, especially energy and roads. The development of physical infrastructure aims at reducing the cost of doing business in Rwanda to promote private sector led growth. In addition, more resources have been allocated to agriculture, education, health and water. Priority spending will remain high at about 13 percent of GDP, about the same level as in 2008. The priority areas are as follows:

- Agriculture—we will pursue a multi-pronged approach to growth in this sector. Activities will focus on the provision of fertilizer and improved seeds and other inputs. Funds for reduction of soil erosion, irrigation and water management as well as marshland development have been increased.

- Energy—to address the issue of limited and insufficient energy, we have allocated sufficient funds to continue various energy projects including the Nyabarongo hydro dam as well as other microdam projects. In addition, funds have been allocated for investment in the Lake Kivu gas project, provision of heavy fuel generating plant for Electrogaz as well as for rehabilitation of distribution infrastructure. It is expected that the implementation of all these projects will make it possible to reduce electricity tariff by half after 2010 as well as cut the subsidy to Electrogaz by 0.5 percent of GDP in 2010–12.

- Roads—we will undertake various projects aimed at upgrading and rehabilitating key road networks in the country including Kigali and the surroundings. With regards to the Kigali and surroundings road network, we have contracted a loan of US$33 million from the ExImBank of China at end-June 2009. This project is of utmost importance to urban and economic development. The World Bank has confirmed its technical and economic viability. Other more concessional financing for this project was not available. Development partners indicated that this would not jeopardize Rwanda's access to future concessional financing. This loan has a grant element of 34 percent and our analysis shows that the loan will not significantly worsen the external debt sustainability. We are therefore requesting a waiver for the continuous performance criterion on contracting nonconcessional debt.

- Information and communication technologies (ICT)—we will continue to invest the proceeds from the sale of Rwandatel in the ICT sector. The objective of this project is to provide a robust nationwide broadband backbone using fiber optics. Over time it is expected that the availability of this ICT backbone will provide a platform to induce new economic activity countrywide.

- Education and health—In line with our EDPRS policies, we will retain the momentum generated last year in these sectors. Regarding education, after achieving a significant increase in enrolment, the focus is now turned to improving quality of the "9 year basic education" by raising the completion rate and strengthening post-basic education. We will therefore intensify the rehabilitation of existing classrooms as well as construction of new ones. We will also speed up the distribution of textbooks to improve learning, intensify the training of teachers to improve standards as well as distribute 100,000 laptops to various schools to encourage distance learning and promote computer literacy. In the case of health, the budget will support activities aimed at improving human health and slowing down population growth. The focus will therefore be on the purchase of drugs, vaccines and other medical supplies as well as catering for the "*mutuelle*" insurance schemes and expanding the contractual approach to community health programs.

PRIORITY EXPENDITURE AS PERCENT OF GDP, 2008/09 AND 2009/10

	2008/09	2009/10
EMPLOYEE COST	1.9	1.8
GOODS AND SERVICES	2.0	2.0
TRANSFER AND SUBSIDIES	4.0	4.5
EXCEPTIONAL EXPENDITURES	0.5	0.2
NET LENDING	0.1	0.1
DOMESTIC CAPITAL	4.5	4.5
Total	**12.8**	**13.1**
Memorandum item:		
Total expenditure and net lending (excluding privatization receipts) as percent of GDP	27.8	26.7

- Water and sanitation—we will continue with the rehabilitation of existing water and sanitation infrastructure as well as construction of new ones to improve delivery of services. In the area of water facilities we will finalize the construction of water pipes to various districts and towns including the supply of Kigali with water from the Nyabarongo underground sources. To improve sanitation, we will also complete the construction of various schools and town latrines.

38. On the external front, the impact of the global crisis will result in a slight widening of the current account deficit in the next fiscal year. We will therefore draw down a small amount of our international reserves to enable us sustain our projected level of imports to achieve our growth objective. Should the balance of payments situation unexpectedly deteriorate, to stem the loss of reserves beyond what we have projected we will allow greater flexibility in the exchange rate by replacing the current system of on-demand sales of foreign currency to commercial banks with an auction system based on predetermined foreign exchange sales.

39. Reserve money will remain the anchor of the monetary program for the fiscal year 2009/10 to return and maintain inflation at single digits. We will therefore limit reserve money growth in the July- December 2009 and the January–June 2010 periods to about 6.5 percent and 7.5 percent respectively. To create enough room for an expansion of private sector credit, NBR may have to inject medium to long term liquidity in the banking system.

40. We will implement the facility for collateralized three to twelve month lending by NBR consistent with the reserve money target. The interest rate on the scheme, currently at 11.5 percent, will be changed in line with future changes in policy interest rates.

41. We will further improve our liquidity forecasting and coordination of fiscal and monetary policies. In this regard, we will strengthen the Treasury Management Committee (TMC) to enable it improve the coordination of fiscal and monetary policies. To this end it will pay more attention to the monitoring of the import component and the domestic demand impact of fiscal spending.

42. To prevent the risk of sharp credit slowdown, the Government will temporarily move part of its deposits currently at the NBR to commercial banks. The scheme is currently assessed and limited to 12 billion Rwf for the second half of 2009. Banks that increase the stock of their investment lending with maturity of over 3 years will be eligible for the government deposits. Banks will select the projects, will bear the credit risk, and set the lending rate. At the same time, the participation in the scheme will be voluntary. Only commercial banks that meet the Capital Adequacy Ratio will be eligible to participate in the scheme.

43. The NBR will also aim to restore positive real interest rates to prevent further deterioration of private sector deposits in commercial banks.

44. The NBR will strengthen its efforts to improve the functioning of the banking system and bank supervision. The focus will be on the following areas:

- We will finalize and implement a new liquidity regulation which will require banks to comprehensively report on maturity of assets and liabilities. On the basis of these reports, we will develop a new and more comprehensive liquidity ratio. When necessary, we will require that banks prepare action plan, including contingency funding plans if needed, to maintain an adequate liquidity position.

- We will implement the recently approved regulation on classification of nonperforming loans and provisioning. In addition, the capital adequacy requirement was raised in May from 10 to 15 percent to further strengthen the banking sector.

- We will enforce better risk management practices and corporate governance in the commercial banks, in line with existing regulations. In particular, we will advise each commercial bank to present its risk management program to be discussed with NBR before end-2009.

- We will strengthen risk-based bank supervision. We will rebuild the Banking Supervision Department capacity to conduct on-site inspections once a year as soon as possible. We will hire, on a temporary basis, external auditors to assist banking supervision department at the NBR in undertaking on-site inspections of two large banks by end-2009.

- We will augment the supervisory capacity at the NBR. Therefore, we will address the staffing shortage at the bank supervision department. Recruiting and training of new staff is now underway. In addition, by end-2009, we will improve the salary structure of the NBR to enhance motivation of the staff.

45. On the upcoming SDR allocation, this will increase the Net International Reserve position of Rwanda. While this will provide an additional buffer to gross reserves, it will not impact Rwanda's Net Foreign Assets position because both foreign assets and liabilities will increase. Because Rwanda's reserve cover in our baseline scenario is projected to be reduced from 5.3 months of imports to about 4 months of imports in the medium term, and the proposed fiscal stance is appropriate, we will save the SDR reserves as a safeguard against potential balance of payments pressure in the medium term. Should the balance of payments deteriorate more than expected, the use of the SDR allocation will be revisited at that time.

VI. Structural Policies for Fiscal Year 2009/10

46. The focus on the structural side will remain on enhancing the productivity of the agricultural and export sectors, improving conditions for the private sector and effectiveness of public financial management.

47. **Export Promotion**

- Our export promotion strategy will continue to focus on enhancing the productivity in traditional sectors and diversifying our export base. New developments include the formation of a National Export Board which is to be established in July 2009 and will incorporate promotion of all agricultural exports under one institution. In the tea sector, 2009/10 will see the privatization of three factories which is hoped to improve productivity. For coffee, a Marketing Alliance will be established in 2009/10 to improve marketing. On tourism, a new regional approach aims to market EAC as one destination with a diversification of activities within. Rwanda will continue to focus on high-end cultural and eco-tourism.

48. **Financial Sector**

- The Financial Sector Development Plan (FSDP) is expected to be fully implemented by June 2010**.** The multifaceted FSDP has the task of strengthening and deepening the financial sector in Rwanda from microfinance to long term capital markets. Areas still to be completed include:

- *Improving access to credit*. Regulations for the newly developed Savings and Credit Cooperatives (SACCOs) and Micro Finance Institutions are ready for gazetting, thereafter they will be implemented. A private credit reference bureau which has been be set up will commence work to improve the quality of information and the assessment of risk posed by banks credit customers.

- *Savings.* Implementation of the National Savings Mobilization Strategy and the Umurenge SACCO's strategy (adopted by Cabinet in early 2009) will commence soon. These strategies will aid the Government in reaching the gross national savings target of 10 percent of GDP by 2012 (8.5 percent in 2008/09).

- *Improving the Pensions Sector.* Liberalization of the pension sector will be achieved by setting up a legal framework for the private pension scheme and personal retirement saving accounts. The law is expected to be officially published in early 2010.

- *Regulation and Legal Framework for the Insurance Industry*. NBR will work on legal and structural issues in the coming year to ensure a well regulated insurance sector.

- *Modernization of the National Payment System*. The NPS framework and strategy among others encapsulates the vision and projects will be undertaken to continue to modernize the Rwandan Payment Systems. The aim of this strategy is to have a clear vision and plans that we will enable us to set up an efficient, safe, fast and reliable payment system and expedite high value funds transfer. Many stakeholders are involved as indicated in the membership of the National Payments Council (NPC) where there is a wide range of representation.

49. **Cost of Doing Business**

- Efforts to improve the business climate will continue. A key development will be the modernization of Rwanda's business registration. A registry for secured transactions and intellectual property rights will be established. Moreover, businesses will benefit from the developments in online taxation, as well as other online applications and issuance of certificates; for example, it is planned to make it possible to register a business on-line (by the end of 2009).

50. **Public Investment and Public Private Partnerships**

- The Government will utilize its new National Public Investment Policy to improve resource allocation, quality, and efficiency of the investment portfolio and increased level of project execution rates. In 2009/10 it will strengthen the newly established instruments for public investment. These include the Public Investment Committee and the Technical Team. In addition, we will finalize the institutional framework as well as the operational guidelines. Care will be taken to ensure alignment of public investment with the new Public Private Partnership program and Rwanda's development goals.

- To foster private sector participation in infrastructure development, while enhancing the government's capacity to manage related fiscal risks, the Government will develop a Public Private Partnership (PPP) framework**.** During the year, the Government shall develop and adopt an agreed PPP framework that will set the scope of PPP program, detailed institutional and legal framework, regulations and procedures, procurement and negotiation, and the appropriate distribution of risks between the public and private sectors.

51. **Fiscal Structural Reforms**

- Tax administration reforms will continue to achieve our targets for widening the tax base. To achieve the goal we will focus on three areas in 2009/10:

- *Enhancing taxpayer compliance*. To widen the tax base we will effectively implement the Block Management System for which a pilot program has begun and a national roll out is expected by January 2010. Since employers will be forced to declare the same figures for PAYE tax and social security compliance levels are expected to rise.

- *Increasing efficiency of operation and minimizing transaction costs*. We are planning to increase the amount of transactions customers can carry out online. This will increase the use of banks for payments, and tax services will be decentralized away from headquarters and closer to businesses.

- *Facilitating trade*. Cargo scanners will be introduced by January 2010 to assist in expediting the clearance of cargo, and so reducing the need for timely physical verification of imported goods. We will continue to provide incentives to compliant taxpayers and enforce appropriate sanctions to the non compliant.

52. Specific tax reforms will be imposed to enhance the effectiveness of the decentralization process. The RRA will strengthen its presence in the provinces and computerize all provincial offices by the end of 2010. At the district level the Government will undertake a study to identify new revenue sources available at the local level. It will recommend possible policy actions to widen revenue base.

53. **Public Financial Management**

- The Government will undertake a range of measures in continuation of Public Financial Management (PFM) reforms. Some of the activities for 2009/10 include:

- *The MTEF process will be revitalized and integrated fully into budget preparation focusing on strengthening performance based budgeting.* The costing of all major sectors for MTEF purposes will continue in 2009/10. Gender budgeting and performance-based budgeting will be mainstreamed into the budget process. Furthermore, Government will ensure that all externally financed projects and programs which managed by Government are fully reflected in the budget in order to minimize extra-budgetary funding.

- *Strengthen the newly established Rwanda Public Procurement Authority (RPPA).* A new organizational structure and human resources strategy will be adopted by the RPPA, which is linked with anti-corruption institutions.

- *IT improvements—'Smartgov'.* The budget IT system will be developed to increase coverage of expenditures which are carried out outside the treasury system. This includes self-generated revenues of agencies and districts and donor-funded expenditures. Improvements also include the management of government bank accounts. This will assist the monitoring of project execution rates. The pilot for this new system should begin in July 2009.

- *District level reforms.* Pilot projects have begun in the installation of new software for Tax Management Systems for districts, it is expected that this can begin to be rolled out to districts by end 2009. Training of local government staff in financial management procedures and reporting, focusing on local revenue mobilization will be carried out.

Att. 1. Table 1. Rwanda: Quantitative Performance Criteria and Benchmarks for 2008
(Billions of Rwandan francs, unless otherwise indicated)
(Quantitative benchmarks* and performance criteria on test dates**)

	2008			
	March*	June**	September*	December**
Benchmarks and performance criteria				
Net foreign assets of the NBR (floor on stock)[1]				
Actual (program exchange rate)	297.0	331.9	315.8	317.5
Adjusted program	257.5	321.8	301.8	272.9
Program	257.5	321.8	314.8	275.7
Reserve money (ceiling on stock)[2]				
Actual	101.1	106.6	112.2	114.1
Adjusted program	100.3	107.7	113.8	114.8
Program	98.0	102.4	107.1	107.6
Net credit to the government (ceiling on flow)[3]				
Actual	-29.0	-62.1	-33.7	-59.4
Adjusted program	47.5	-46.9	-22.4	-10.7
Program	47.5	-46.8	-35.4	-13.4
Domestic fiscal balance (floor on flow)[3, 4]				
Actual	-30.2	-48.9	-100.1	-128.1
Adjusted program	-42.4	-67.8	-108.3	-148.6
Program	-42.4	-67.8	-113.7	-148.6
Total priority spending (floor on flow)[3, 4]				
Actual	63.3	129.5	220.7	313.1
Adjusted program	57.3	128.4	199.0	275.1
Program	57.3	128.4	201.7	275.1
New nonconcessional external debt[5]				
Actual	0.0	0.0	0.0	0.0
Program	0.0	0.0	0.0	0.0
New external payment arrears (ceiling on stock)[5, 6]				
Actual	0.0	0.0	0.0	0.0
Program	0.0	0.0	0.0	0.0
Short-term external debt (ceiling on stock)[7]				
Actual	0.0	0.0	0.0	0.0
Program	0.0	0.0	0.0	0.0
Net accumulation of domestic arrears (ceiling on flow)[3]				
Actual	6.4	-4.0	4.6	-8.0
Program	-3.0	-4.0	-5.5	-7.0
Indicative targets				
Broad money (ceiling on stock)[1]				
Actual	363.6	371.3	399.1	393.9
Program	365.9	389.5	394.3	422.3
Extended broad money (ceiling on stock)[1]				
Actual	431.2	444.1	477.1	473.7
Program	425.5	453.7	459.3	491.1
Net Present Value of the Stock of Outstanding Debt (Millions of US$)[8]				
End-December 2007--Actual		240.9		240.9
End-December 2008--Actual		331.5		331.5
End-December 2009--Actual				
End-December 2007--Program		200.4		200.4
End-December 2008--Program		286.4		286.4
End-December 2009--Program		405.6		405.6
Ceiling on stock of domestic debt[9]				
Actual	162.1	159.1	146.1	124.8
Program	208.6	189.7	187.6	198.6
Memorandum items:				
General budget support (Millions of US$)[4,10]				
Received	104.2	219.8	255.3	312.5
Expected	104.1	219.3	289.1	317.5
Of which: budget support grants (received)	97.2	212.8	248.3	305.5
Of which: budget support grants (expected)	97.1	212.3	282.1	310.5
Baseline privatization receipts (RF billion)				
Received	…	3.6	3.6	3.6
Expected	…	3.5	3.5	17.1

Sources: Rwandese authorities and IMF staff estimates and projections.

[1] At the program exchange rate of RF545/US$ for 2008.
[2] Targets are calculated as an arithmetic average of the stock of reserve money on the last day of each calendar month in the quarter. Program projections are done quarterly.
[3] Numbers are cumulative from December 31, 2007.
[4] The domestic fiscal balance targets will be adjusted by the amount of grants exceeding or below programmed grants with the adjusters as specified in the TMU of February 12, 2008. Also the priority spending targets will be adjusted by the amount of grants exceeding or below programmed grants.
[5] This is a continuous performance criterion. Excluded from the criterion are changes in indebtedness resulting from refinancing credits and rescheduling operations of existing debt, credits extended by the Fund, and US$97.7 million in credit from the Exim Bank of India with concessionality of 40 percent for the construction of the hydro power plant at Nyabarongo.
[6] Excludes arrears on obligations that are subject to rescheduling.
[7] Ceiling on the stock of external debt (excluding normal imported-related credits) owed or guaranteed by the central governments, local government, or the NBR with original maturity of up to, and including one year.
[8] Figures indicate the NPV projections based on debt contracted at the test date.
[9] Numbers show end of period stocks. The stock of debt at end-2007 was revised from RF200.3 billion to RF236 billion, which prompted revision of the program numbers for September and December 2008.
[10] Excluding external donor financing for demobilization and peacekeeping.

Att. 1. Table 2. Rwanda: Quantitative Indicative Targets and Benchmarks for 2009-10
(Billions of Rwandan francs, unless otherwise indicated)

	2009				2010	
	March	June	September	December	March	June
Net foreign assets of the NBR (floor on stock)[1]						
Actual (program exchange rate)	267.0					
Adjusted program	298.3					
Program	311.6	298.0	341.6	326.1	325.0	301.8
Reserve money (ceiling on stock)[2]						
Actual	112.3					
Adjusted program	114.8					
Program	123.2	128.3	113.3	114.0	114.7	121.0
Net credit to the government (ceiling on flow)						
Actual	41.0					
Adjusted program	-2.3					
Program	-15.6	-24.2	-38.1	-25.2	-10.9	16.0
Domestic fiscal balance (floor on flow)						
Actual	-47.3					
Adjusted program	-6.5					
Program	-35.8	-72.2	-145.8	-209.3	-25.7	-61.4
Total priority spending (floor on flow)						
Actual	88.7					
Adjusted program	63.6					
Program	78.2	159.8	266.9	375.0	91.2	184.5
New nonconcessional external debt[3]						
Actual	0.0					
Program	0.0	0.0	0.0	0.0	0.0	0.0
New external payment arrears (ceiling on stock)[3, 4]						
Actual	0.0					
Program	0.0	0.0	0.0	0.0	0.0	0.0
Short-term external debt (ceiling on stock)[5]						
Actual	0.0					
Program	0.0	0.0	0.0	0.0	0.0	0.0
Net accumulation of domestic arrears (ceiling on flow)						
Actual	4.0					
Program	-1.6	-3.3	-5.4	-8.4	-1.6	-3.3
Broad money (ceiling on stock)[1]						
Actual	431.7					
Program	543.1	555.4	480.1	474.9	509.9	512.7
Actual						
Net Present Value of the Stock of Outstanding Debt (Millions of US$)[6]						
End-December 2007--Actual		240.9		240.9		240.9
End-December 2008--Actual		331.5		331.5		331.5
End-December 2009--Actual						
End-December 2007--Program		200.4		200.4		200.4
End-December 2008--Program		286.4		286.4		286.4
End-December 2009--Program		413.7		413.7		413.7
Ceiling on stock of domestic debt[7]						
Actual	98.8					
Program	183.3	168.4	102.0	100.1	86.1	85.7
Memorandum items:						
Expected general budget support (Millions of US$)[8]	96.2	173.7	330.1	424.7	57.8	72.0
Received	19.5	159.6				
Of *which:* budget support grants (received)	19.5	159.6				
Of *which:* budget support grants	96.2	173.7	330.1	424.7	57.8	72.0
Baseline privatization receipts (RF billion)	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Rwandese authorities and IMF staff estimates and projections.

[1] At the program exchange rate of RF555/US$ through June 2009 and RF576.8 from September 2009 to June 2010.

[2] Targets are calculated as an arithmetic average of the stock of reserve money on the last day of each calendar month in the quarter.

[3] This is a continuous indicative target.

[4] Excludes arrears on obligations that are subject to rescheduling.

[5] Ceiling on the stock of external debt (excluding normal imported-related credits) owed or guaranteed by the central governments, local government, or the NBR with original maturity of up to, and including one year.

[6] Figures indicate the NPV projections based on debt contracted at the test date.

[7] Numbers show end of period stocks.

[8] Excluding external donor financing for demobilization and peacekeeping.