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

April 25, 2014

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, Rwanda
April 25, 2014

Ms. Christine Lagarde
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C., 20431

Dear Ms. Lagarde,

The attached memorandum of economic and financial policies (MEFP) is an update of the November 2013 MEFP and sets out the macroeconomic policies of the Rwandan government for the remainder of fiscal year 2013/14 and fiscal year 2014/15. Due to adverse weather conditions that affected agricultural production, spillovers associated with the aid shock and resulting delays in the implementation of some major government financed projects, growth in 2013 slowed down to 4.6 percent. Inflation remained well contained throughout the year.

As described in the MEFP, all but one end-December 2013 quantitative assessment criteria (QAC) were met; the continuous QAC on non-concessional borrowing was not observed when Rwandair financed the lease of an airplane. All indicative targets, but one, have been met. The slight breach of the domestic debt ceiling was the result of delays in disbursing donor financing deposited at the central bank. Reflecting our commitment to the PSI objectives, all five structural benchmarks were met.

In light of this satisfactory performance and its continued commitment to sound policies, the Government requests the completion of the first review under the PSI. The Government also requests a waiver for the non-observance of the QAC on non-concessional borrowing and reiterates its commitment to reinforcing procedures regarding non-concessional borrowing by public entities. These procedures require all public entities to consult early with and seek approval from the Ministry of Finance and Economic Planning for the contracting of any external loans.

The government believes that the policies and measures set forth in the MEFP will deliver the objectives of the PSI-supported program but we will take any further measures that may become appropriate for this purpose. The Government will consult with the IMF—at its own initiative or whenever the Managing Director of the IMF requests such a consultation—before the adoption of any such measures or changes to the policies described in the attached MEFP.

The government will provide the IMF with such information as the IMF may request in connection with the progress made in implementing the economic and financial policies and achieving the objectives of the program. It is expected that the second review will take place before end-December 2014.

The Government of Rwanda authorizes the publication and distribution of this letter, its attachments, and all reports prepared by the IMF staff.

Sincerely yours,

/s/	/s/
Claver Gatete	**John Rwangombwa**
Minister of Finance and Economic Planning	Governor, National Bank of Rwanda

Attachment I. Memorandum of Economic and Financial Policies—Update

April 25, 2014

1. This MEFP update reviews performance under the PSI-supported program through end-December 2013 and discusses the macroeconomic outlook and policies for 2014 and FY2014/15. It also describes quantitative and structural targets for end-June and end-December 2014. As in the November 2013 MEFP, policy formulation in all areas will take Rwanda's commitments to the East African Community into account.

Recent Economic and Policy Performance

2. **Introduction.** Policy implementation in FY 2012/13 was complicated due to the suspension of aid by some donors and delays in the approval of disbursements by others. While relations with donors have since normalized, delays in budget support disbursements and a shortfall in project grants resulted in cuts and postponements in public spending, particularly some major government infrastructure projects. These developments together with adverse weather conditions which affected agricultural output slowed down economic growth to 4.6 percent in 2013. Inflation remained subdued throughout 2013 and further decelerated during the last quarter to 3.7 percent at end December .This deceleration has continued in 2014 and at end March 2014 stood at 3.4 percent..

3. **Growth.** The slowdown in 2013 reflected a combination of the aid shock and adverse weather conditions. Due to adverse weather, growth in the agriculture sector–at 3 percent–was the same as in 2012. The spillover effects from the aid shock affected mostly the services sector, which represents 45 percent of GDP. The sector registered growth of 4 percent, the lowest of the last decade due to the combination of: (i) a slowdown in growth of credit to the private sector, itself constrained by limited availability of foreign exchange, and (ii) contracted government spending in the first half of 2013, which negatively affected domestic demand–total consumption fell (-1 percent) and investment stagnated (1 percent). The industry sector recorded a solid growth of 11 percent led by construction activities and the beverage industry, while mining activities grew 41 percent.

4. **Inflation**. Inflation, both headline and core, was firmly contained with the former standing at 3.7 percent year-on-year in December and the latter at 3.8 percent. This reflected a combination of lower imported inflation from the region, the reduction in fuel prices, and benign commodity prices.

5. **External balance.** On the external front, imports weakened partly due to the general slowdown as well as delays in implementing some large investment projects that affected capital and intermediate goods imports. The low growth in other current receipts, including tourism receipts, was more than compensated by the doubling in mining sector exports. The favorable

current account developments, facilitated by lower than expected imports, coupled with the unused Eurobond proceeds helped to stabilize reserves at 4.8 months of imports.

6. **Fiscal developments.** Fiscal policy implementation was complicated by the delays in donor disbursements. On the revenue side, lower tax revenue associated with the economic slowdown was compensated by non-tax revenue due to one-off disbursements associated with a larger than expected role for Rwanda in regional peace keeping operations. Global Fund disbursements were also higher than projected resulting in total revenue and grants exceeding projections by about 1.5 percent of GDP. Domestic tax revenue collections, at 13.7 percent of GDP, were 0.6 percent of GDP lower than the program target. This lower performance was more than offset by larger non tax revenue collections. Reflecting the authorities' commitment to fiscal discipline, both recurrent and capital expenditure were adjusted following the aid shock to preserve the domestic finance target. The wage bill was lower than expected due to delayed recruitment and capital expenditures were also lower due to delays in the construction of the Kigali Convention Centre (KCC) and other infrastructure projects, notably in energy and roads. Net lending was sharply curtailed as only a small amount of the Eurobond proceeds was used for the KCC and Nyabarongo hydro-power project. Furthermore the repayment of RWF 32.5 billion by Rwandair to the government curtailed net lending. The combined effects resulted in the fiscal accounts recording a surplus for the first half of the FY 2013/14 of 0.4 percent of GDP, compared to an initial deficit estimate of 4.8 percent of GDP.

7. **Monetary and exchange rate developments**. The NBR has continued to focus on limiting the risks from monetary inflation and anchoring inflationary expectations, while containing pressures on the exchange rate. Following the end of the tightening cycle in June 2013, when the key policy rate was reduced by 50 basis points, the policy rate has been left unchanged as credit to the private sector increased in the second half of 2013, pushing up the demand for foreign exchange. Credit growth to the private sector increased by 10.8 percent (year-on-year) compared to an initial projection of 14.3 percent. The slowdown in credit growth reflected the broader deceleration in the economy and commercial banks tightening lending criteria following increases in non-performing loans, mostly in the services sector. The economic slowdown also contributed to a weakening of imports. The exchange rate remained fundamentally market driven. A depreciation of 6.1 percent in the Rwandan Franc contributed to reducing the spread that had arisen due to lower aid flows and reduced NBR sales of foreign exchange. Regarding the monetary aggregates, broad money growth increased by 15.5 percent in 2013. Net foreign assets were higher than targeted on account of favorable current account developments and unspent proceeds of the Eurobond.

8. **Program performance**. Program performance under the new PSI has been strong. All but one of the quantitative assessment criteria (QAC) for end-December 2013 (Table 1) were met. The continuous QAC on non-concessional borrowing was not observed when Rwandair financed the lease of an airplane. All the structural benchmarks associated with the review were met (Table 2).

Macroeconomic Outlook and Policy for 2014 and FY2014/15

9. **Economic growth will pick up in 2014 and inflation will remain contained.** The government considers the slowdown in growth in 2013 to be temporary. With the normalization in aid flows and resumption of government infrastructure projects, a stronger outlook for the first agricultural season, and the rebound in services sector momentum, the government expects growth to recover to 6 percent in 2014. A growth of 5 percent in agriculture, led by food crops and an increase in the area under cultivation, is expected to support the recovery. Regarding the industry sector, growth is projected at 6 percent, compared to 11 percent in 2013. This is mainly due to many private construction activities nearing completion. Nevertheless, construction will still have a positive impact on the overall sector. Furthermore, the electricity and gas sub-sector will see much stronger growth due to the addition of new power plants to the grid. Growth in the services sector is expected to recover from 4 percent in 2013 to 7 percent in 2014. This is due to an upturn in government consumption and credit growth as well as higher growth of agriculture impacting on trade in services. The performance will be led primarily by wholesale and retail trade as well as by real estate and business services sub sectors with growths of 8 percent and 4 percent in 2014. Inflation will remain contained at 5 percent, in line with the NBR's target. This reflects both a combination of subdued inflationary pressures and the monetary policy stance.

10. **Regarding the external sector, the current account deficit is projected to deteriorate from 7.2 percent of GDP in 2013 to 12.1 percent in 2014.** This is due to the expected pickup in economic activity resulting in an increase in infrastructure related imports that were postponed in 2013. Capital and intermediate goods imports will contribute to the rebound in imports thereby contributing to a deterioration of the current account despite a robust export performance. The increase in imports will be financed primarily by the unused Eurobond proceeds allocated to the Kigali Convention Center and the Nyaborongo hydro project. Foreign reserves coverage will be around 4 months of imports.

11. **Notwithstanding the strong fiscal performance in the first half of FY 2013/14, the full year fiscal position remains similar to that expected at the initiation of the PSI.** This profile assumes that revenues bounce back in the second half of the fiscal year, while grants remain at the same level as projected. The original revenue ratio target of 15.1 percent of GDP is unlikely to be fully met. This is partly because of delays in implementing some of the revenue measures, including the excise on airtime, and weaker than expected royalty taxes. On the expenditure side, both current and capital spending will rebound in the second half of the fiscal year, including from new hiring and the implementation of delayed government investment projects. Overall expenditure, at 31.2 percent of GDP, is projected to be very similar to the initial program objectives.

12. **The fiscal framework for FY2014/15 is built on conservative assumptions regarding budget support and aims to sustain the domestic revenue mobilization efforts.** Budget support is expected to be around 9.5 percent of GDP. Given the continued uncertainty regarding long-term donor engagement and the government's commitment to reducing its reliance on donor financing, accelerating domestic revenue mobilization remains a key priority. By end-June 2014, we will assess the proposed FAD recommendations on agriculture, mining, and property taxes and consider those

that can be implemented within a defined time frame. Currently, these regimes are projected to be introduced into the fiscal framework by FY2015/16. Combined with the taxes on agriculture, mining, and property, the government will also consider additional revenue measures to generate an extra 0.4 percent of GDP in FY 2015/16. This will take the tax revenue collections to over 17 percent of GDP.

13. **Expenditures will increase in the FY 2014/15, but the overall deficit (including grants) will decline.** The expenditure composition is a reflection of the government's policies aimed at supporting growth and reprioritizing expenditure in a context of donor uncertainty. Total expenditure and net lending is estimated at RWF 1696.9 billion (29.5 percent of GDP) compared to RWF 1593.2 billion (31.2 percent of GDP) in FY 2013/14. The increase in nominal terms is driven by increases in both recurrent and capital spending. Recurrent expenditure is estimated at RWF 814 billion showing an increase of RWF 38.8 billion compared to FY 2013/14. Spending on new recruitments and transfers to the local government entities to compensate them for the revenue collections surrendered to the central government account for the increase. Capital expenditure is RWF 58.5 billion higher at RWF 782.2 billion. This is due to increased outlays for on-going energy projects. The overall deficit (including grants) is expected to decline to 3.1 percent of GDP compared to 5.3 percent of GDP in FY13/14. Net domestic cash finance of the 2014/15 budget is expected to be around RWF 69.6 billion (1.2 percent of GDP). If the growth momentum weakens and the rebound in revenue mobilization in the second half of FY 2013/14 does not materialize, the government will finance the shortfall with additional domestic finance. However, it will ensure that the additional finance does not "crowd out" the private sector.

14. **Structural measures aimed at supporting the domestic revenue mobilization strategy would be accelerated**. The following measures are to be implemented on the revenue side over the next two years :

- ***The draft investment code approved in March 2014 by Cabinet has streamlined incentives and exemptions.*** These will come into effect in FY2014/15 and are expected to yield additional tax revenues starting FY2015/16. The main measures include:

(i) The Cabinet may no longer grant a blanket discretionary incentive package.

(ii) VAT exemption for investment certificates holders no longer apply.

(iii) All the incentives related to customs duties have been aligned with EAC regulations and procedures. Investors granted such incentives prior to Rwanda's accession to the EAC would also be subject to the new code.

(iv) Investment thresholds (100,000USD for local investors and 250,000USD for foreign investors) no longer apply. Instead, fiscal incentives are provided to specific sectors.

(v) The provision which grants to investors a tax discount depending on the number of employees has been removed.

(vi) The flat tax of 5 percent on building and finishing materials, in lieu of import duties and excise for construction projects worth of at least 1.8 M USD, has been aligned with EAC regulations such that the Common External Tariff now applies.

(vii) The tax on capital gains was scrapped. However, it was decided that the income from the sale of properties shall be incorporated in the taxable income of the company.

- ***A tax expenditure assessment will be undertaken as part of forthcoming budget.*** The review of tax expenditures will cover customs and budget tax expenditures initially. It will be submitted with the FY2014/15 budget.
- ***Tax payer compliance is being enforced***. This is being done through implementation of the various continuous administrative measures highlighted in the November 2013 MEFP. Most of the measures are on track.
- ***The VAT law is being amended to reduce exemptions***. A draft is being submitted to the IMF for further comments before its submission to Cabinet for approval. The main VAT exemption measure has been the removal of exemption of VAT for investment certificates holders.
- ***The government will divest from the Rwanda Development Bank and foster greater private sector participation***. Negotiations are on-going with a strategic investor and an MOU was recently signed. The divestiture will also increase the asset base of the bank and allow the bank to diversify and increase lending products.

15. **Turning to public financial management, a number of measures are being introduced.** These include:

- ***The extension of IFMIS to 20 development projects.***
- ***Reviewing the grant formula for local governments.*** The block grant formula was to be reviewed following the findings of the local government revenue potential study, which would have allowed for districts with higher revenue potential to receive lower transfers. The formula would have also included a component that would have fostered greater local revenue generation. The completion of the study was delayed and finalised in November instead of March 2013. Another element was to work with all districts on the implementation strategy after which the formulae was to be reviewed. However, given the time required for such a process and the budget calendar, it was not possible to review the formula. Consultations on the LGRPS implementation strategy are now planned for May 2014, after which a new block grant formula will be prepared and submitted to cabinet to inform the budget processes for FY 2015/16.
- ***Financial reporting of sub-national entities***. A template has been developed and issued to all sectors (the administrative level below districts) to compile data and report to districts. To ensure accuracy and completeness in the use of the template, all sectors accountants and executive secretary have been trained on basic elements of PFM and a Subsidiary Entities Accounting System (SEAS) has

also been developed. To date, this system has been implemented in 8 districts and 88 sectors are using it to make payments. They are also using it for accounting and reporting to their respective districts on a monthly, quarterly, and on an annual basis. The SEAS will be implemented in all sectors by August 2014.

16. **Given the uncertainties concerning the level of donor grants and concessional funding, the government will seek non concessional finance for the implementation of some strategic investment projects.** These projects are critical towards meeting the economic and social objectives under the EDPRS 2. Consistent with these objectives, a number of projects have been identified for implementation during the current PSI period. To avoid the current ceiling on non-concessional borrowing (NCB) being breached during the PSI period, an increase of US$ 250 million on the existing level is being requested for FY 2014/15. This will allow the government to finance and implement some of the investment projects envisaged.

17. **The government's public investment program gives the highest priority to projects for water, energy, and affordable housing.** The government will keep the Fund informed on the financing structure and implementation of these projects. In addition, the government views the expansion of the national airline Rwandair as critical to its medium-term plan to build a new international airport at Bugesera as well to increase revenue from services, particularly tourism. The financing structure for the airport project, along with other large medium-term infrastructure projects like the railway and the oil pipeline, will be a hybrid of public and private financing. Although these larger projects will be completed beyond the current PSI period, the government wishes to indicate that the current NCB ceiling may need to be renegotiated again as and when financing for these projects is finalized. As the level of non-concessional debt increases, the government is highly mindful of the need to monitor the debt sustainability.

18. **The NBR will maintain its prudent monetary policy stance during 2014 in a bid to anchor inflationary expectations while supporting growth and containing pressures on the currency**. Private sector credit is expected to pick up in 2014 as the economy reverts to its potential. The exchange rate will remain market driven and NBR will continue to allow greater exchange rate flexibility to maintain the spread between the official and market rate below 2 percent and ensure reserve levels remain comfortable (at a minimum level of 4 months of prospective imports (CIF)).

19. **The NBR will also sustain its efforts aimed at strengthening the monetary policy framework**. In this regard, it will continue implementation of policies aimed at tackling the structural excess liquidity. The NBR has started issuing instruments with longer-term maturities. It has also published a quarterly bond issuance calendar for bonds with longer terms maturities. Following the recent successful issuance of an oversubscribed bond, activities picked up on the secondary market. Additionally, policies aimed at improving the interbank market and building capacity at the level of commercial banks would also be accelerated. The NBR is also committed to boost the interbank market by supporting the dealer's association to establish a code of conduct governing the interbank operations in local and foreign currency. The NBR would also sustain capacity building and modeling efforts to better understand the transmissions mechanism and inform the decision making of the monetary policy committee. The NBR will also continue policies to

strengthen its communication process, including through dialogue with players in the foreign exchange market. The NBR recently published its first quarterly inflation report.

20. **Financial sector policies will remain geared toward sustaining financial stability**. Policies rolled out to tackle the increase in non-performing loans have proved effective so far and commercial banks will continue to comply with the new guidelines, including the implementation of the recovery plans. The NBR will continue to conduct off-site surveillance and on-site examinations under risk-based supervision and capacity building efforts for bank supervisors will be sustained. Additionally, given the increasing importance of cross-border banks, the NBR will increase its participation in supervisory colleges to conduct joint on-site inspection of cross-border banks. Ongoing efforts to increase financial inclusion and deepening would also be sustained, particularly through the implementation of the Financial Sector Development Plan (FSDP2).

21. **The legal and regulatory framework will continue to be bolstered**. The NBR law and the banking law are nearing the final stages and will be implemented in FY2014/15. The draft was approved by the NBR's Board in December 2013. The approved document is under translation for transmission to MINECOFIN for cabinet approval and before submission to Parliament for ratification. Subsequently, this will lead to the development of new regulations or updates of existing ones for implementation of the New Banking Law. The updated related regulations and guidance as well as new regulations and other supervisory tools to implement the new laws are also being finalized. Similarly, the NBR's Board approved the Deposit Insurance Law. The Deposit Insurance Law will continue to be tracked for finalization and as will the development of its implementing regulations. The project of legal and regulatory reform is also intended to cater for the Basel II/III project implementation. Other changes to the legal and regulatory frameworks include: (i) Banking Law amendments and its implementing regulations (especially regulation on general provisioning); (ii) completion of the draft new Deposit Insurance Law; (iii) amendment of the Insurance Law and its regulations; and (iv) completion of the legal and regulatory framework for pensions.

22. **Program issues**. Table 1 contains new end-June 2014 and end-December 2014 QACs for the second and third reviews under the PSI and new indicative targets for end-June and end-December 2014. These QACs have been amended to reflect changes to the adjusters and are consistent with the understandings reached with IMF staff on the macroeconomic framework. To avoid the recurrence of the non-observance of the NCB ceiling, the government will further strengthen communication of borrowing plans between parastatals and the Ministry of Finance, and between the government and the IMF to improve program design. The assessment of the end-December 2014 targets is expected to be completed by end-June 2015, at the time of the third review. Table 2 includes the structural benchmarks under the PSI. A new benchmark on publication of quarterly reports of budget execution against annual fiscal objectives is being proposed.

Table 1. Quantitative Assessment Criteria and Indicative Targets[1]

	Dec. 2013 Prog	Dec. 2013 Adj. Prog	Dec. 2013 Actual	Difference	Status	June 2014 IMF country report 13/372	June 2014 Modified Program	Dec 2014 Prog
Assessment criteria [2]								
Net foreign assets of the NBR at program exchange rate (floor on stock) [3, 4]	511.7	541.0	597.7	56.7	Met	459.0	519.7	516.3
Reserve money (ceiling on stock) (upper bound) [5]	218.0	218.0	210.8	7.2	Met	231.1	229.3	242.7
Reserve money (ceiling on stock) [5]	213.7		206.7			226.5	224.8	238.0
Reserve money (ceiling on stock) (lower bound) [5]	209.5		202.6			222.0	220.3	233.2
Net domestic financing (ceiling on flow) [4, 6]	22.2	-7.1	-84.5	106.7	Met	86.7	162.8	152.9
New nonconcessional external debt contracted or guaranteed by the public sector (US$ millions) (ceiling on stock) [9]	0.0	0.0	18.2	18.2	Not Met	0.0	250.0	250.0
External payment arrears (US$ millions) (ceiling on stock)	0.0	0.0	0.0	0.0	Met	0.0	0.0	0.0
Indicative targets								
Domestic revenue collection (floor on flow) [6]	787.1	787.1	799.0	11.9	Met	466.4	415.4	882
Net accumulation of domestic arrears (ceiling on flow) [6]	-50.8	-50.8	-50.8	0.0	Met	-1.9	-1.3	-6.3
Consolidated domestic debt of public sector (ceiling on stock, eop) [4, 7]	337.3	308.0	312.2	4.2	Not Met	337.6	371.8	363.5
Total priority spending (floor on flow) [6]	587.1	587.1	595.3	8.2	Met	357.1	349.1	683.5
Memorandum items:								
Total budget support (US$ millions) [6, 8]	487.8		483.0	-4.8		100.2	164.6	486.2
Budget support grants (US$ millions)	473.6		468.8	-4.8		100.2	164.6	486.2
Budget support (loans, US$ millions)	*14.2*		14.2	0.0		0.0	0.0	0.0
Euro bond (US$ millions)	400.0		400.0	0.0		400.0	400.0	400.0
Unused euro bond proceeds (US$ millions)	121.2		172.4	51.2		0.0	107.3	0.0

Sources: Rwandan authorities and IMF staff estimates and projections.

[1] All items including adjusters are defined in the Technical Memorandum of Understanding (TMU).
[2] Assessment criteria for NFA, RM, NDF are for end-June 2014 and end-Dec 2014 but are continuous for NCB and EA.
[3] Dec 2013 numbers are at the program exchange rate of RWF 631.41 per U.S. dollar. June 2014 and Dec 2014 numbers are at the new program exchange rate of RWF670.1 per U.S. dollar.
[4] Subject to adjustors. See TMU for details.
[5] Targets are calculated as an arithmetic average of the stock of reserve money for the three months in the quarter. Assessment criterion applies to upper bound only. See TMU for details.
[6] Numbers for 2013 are cumulative from 12/31/2012, and those for 2014 are cumulative from 12/31/2013. The figure excludes revenues associated with peace keeping operations
[7] Excluding NBR's debt issued for monetary policy purposes. See TMU for details.
[8] Excluding demobilization and African Union peace keeping operations, HIPC grant, and COMESA compensation grant.
[9] For end-June 2014, cumulative since end-Dec 2013.

Table 2. Status of Structural Benchmarks for PSI (First Review)

Policy Measure	Target Date	Macroeconomic rationale	Status
Revenue Mobilization			
Prepare tax expenditure budget covering main tax expenditures.	Annually, starting end-June 2014	To enhance revenue mobilization.	
Revise exemption and zero-rating schedules under the VAT-law.	End-June 2014	To enhance revenue mobilization.	
Implement plan for better enforcement of tax payer compliance.	End-June 2014	To enhance revenue mobilization.	
Revise legislation on the taxation of property.	End-Dec 2014	To enhance revenue mobilization.	
Prepare legislative proposal for new tax regime for agriculture.	End-Dec 2014	To enhance revenue mobilization.	
Prepare legislative proposal for new tax regime for mining.	End-Dec 2014	To enhance revenue mobilization.	
Public Financial Management			
Pilot the extension of IFMIS to 20 development projects.	End-June 2014	To strengthen budget execution and controls.	
Review the block grant formula on the basis of the Local Government Revenue Potential Study	End-Sep 2014	To enhance collection of districts own revenues.	
Sub-national entities (416) to produce monthly, quarterly, and annual financial reports using a uniform template.	End-Dec. 2015	To improve comprehensiveness and transparency of intergovernmental fiscal transfers.	
MINECOFIN to publish (and put on its website) quarterly reports of budget execution against annual fiscal policy objectives, within 45 days of end of each quarter.	Continuous, starting mid-May 2014	To improve fiscal transparency.	New - Proposed
Monetary and Exchange Rate Policy			
Issue Treasury bills with maturities of six months and longer as a monetary policy instrument to absorb longer-term liquidity.	End- Dec 2013	To develop money market instruments.	Met
Start publishing money market rates (interbank, repo, and T-bill)for different maturities bi-weekly.	End- Dec 2013	To develop money market instruments.	Met
Prepare plan, based on MCM TA recommendations and NBR assessment, for strengthening monetary and exchange rate operations.	End- March 2014	To strengthen monetary and exchange rate operations and foster greater exchange rate flexibility.	Met
Start publishing quarterly inflation reports.	End- March 2014	To improve transparency of monetary policy.	Met
Use Treasury bills (or other tradable securities) as the underlying collateral in liquidity absorbing repos.	End- June 2014	To develop money market instruments.	
Financial Sector Development			
Design a deposit guarantee scheme.	End-June 2014	To increase confidence in banking system.	
Statistics			
NBR to gather high frequency data and undertake economic sentiment surveys.	End-2013	To improve quality and timeliness of economic data.	Met

Attachment II. Technical Memorandum of Understanding

April 25, 2014

1. This memorandum defines the quantitative targets described in the memorandum of economic and financial policies (MEFP) for the period December 2, 2013–November 30, 2016 supported by the IMF Policy Support Instrument (PSI), and sets out the data reporting requirements. This technical memorandum of understanding (TMU) supersedes the TMU issued in Country Report No. 13/372.

QUANTITATIVE PROGRAM TARGETS

2. The quantitative program will be assessed through assessment criteria (AC) and indicative targets (IT) for the duration of the program.

3. AC will apply to the following indicators for June 30, 2014 and December 31, 2014 (the test dates) throughout the program period:

- Floor on stock of net foreign assets (NFA) of the National Bank of Rwanda (NBR);
- Ceiling on stock of reserve money;
- Ceiling on flow of net domestic financing (NDF) of the central government;
- Ceiling on contracting or guaranteeing of new non-concessional external debt by the public sector; and
- Ceiling on stock of external payment arrears of the public sector.

4. IT targets apply to the following indicators throughout the program period:

- Floor on flow of domestic revenue collection of the central government;
- Ceiling on flow of net accumulation of domestic arrears of the central government;
- Ceiling on stock of consolidated domestic debt of the public sector; and
- Floor on flow of priority spending.

5. Assessment criteria on contracting or guaranteeing of new non-concessional external debt by the public sector and stock of external payment arrears of the public sector are applicable on a continuous basis for the duration of the program.

6. **Program exchange rates**. For accounting purposes, the following program exchange rates, which are end-December 2013 rates, apply for 2014:

Program Exchange Rates (US$ per currency unit, unless indicated otherwise)	
	2014
Rwanda Franc (per US$)	670.1
Euro	1.3791
British Pound	1.6375
Japanese Yen (per US$)	103.4116
SDR	1.5383

A. Institutional Coverage of the Fiscal Sector

7. The **central government** fiscal operation table comprises the treasury and line ministries, hereafter referred to as the government unless specified otherwise.

B. Targets Related to the Execution of the Fiscal Program

Ceiling on net domestic financing of the government (AC)

8. **A ceiling applies to NDF**. The ceilings for June 30, 2014 and December 31, 2014 are cumulatively measured from December 31, 2013.

9. **Definition**. NDF of the government is defined as the change in the sum of (i) net banking sector credit to the government and (ii) non-bank holdings of government domestic debt.

10. Net banking sector credit to the government is defined as

- Consolidated credit to the government from the banking system (NBR and commercial banks, as recorded in the monetary survey), including credit to the government, provinces and districts. The outstanding consolidated government debt held by the banking system,[1] includes government debt to the NBR amounting to RWF 38.6 billion incurred as a result the overdraft to the pre-war government and the 1995 devaluation [2], as well as the current overdraft with the NBR. Credit to the government will exclude treasury bills issued by the NBR for monetary policy purposes, the proceeds of which are sterilized in deposits held as other NBR liabilities.

- less total government deposits with the banking system (as recorded in the monetary survey), including in the main treasury account, the accounts of line ministries, the fund for assistance to genocide survivors, the Rwanda Revenue Authority, the electoral commission, the demobilization commission, fonds routier, the privatization account, and the accounts of any other autonomous public enterprises and public agencies over which the government has direct control over their deposits. Thus, this definition excludes any government deposits, over which the central government does not have any direct control (i.e., for project accounts, Global Fund money meant for the private sector, counterpart funds, and *fonds publics affectés*).

11. Non-bank holdings of government domestic debt consist of non-bank holdings of treasury bills, bonds (domestic and non-resident), old development bonds (pre-1994 debt), new development bonds (including those used for recapitalization of banks), and other accounts receivable.

Adjusters to NDF:

- The ceiling on NDF will be adjusted *upward* by the amount of any shortfall between actual and programmed budgetary loans and grants[3] (defined in Table 1. Quantitative Assessment Criteria and Indicative Targets of the MEFP), up to a maximum of US$80 million, evaluated in Rwandan francs at the program exchange rate.

- The ceiling on NDF will be adjusted *upward/downward* by the extent to which in Rwandan francs at the program exchange rate the unused proceeds of the US$400 million euro bond

[1] Consisting of bank holdings of treasury bills, bonds (domestic), old development bonds (pre-1994 debt), new development bonds (including those used for recapitalization of banks), and other accounts receivable.

[2] The authorities will inform Fund staff of any substantive changes in government accounts with the banking system, which may affect the calculation of net bank claims.

[3] Budgetary grants exclude COMESA and HIPC grants, but include Global Fund.

issued in April 2013 is lower than/exceed US$107.3 million by end-June 2014 and not zero by end December 2014.

- The ceiling on NDF will be adjusted *upward* by the amount of expenditure for food imports in the case of a food emergency.

12. **Reporting requirement**. Data on NDF (showing separately treasury bills and government bonds outstanding, other government debt, and central government deposits), each type of debt to be shown by debt holder, will be transmitted on a monthly basis within five weeks from the end of each month. Deposits of the government with the NBR and with the commercial banks will be separated from the deposits of the public enterprises and autonomous public agencies and agencies that the government does not have any direct control over.

Floor on flow of domestic revenues (IT)

13. A floor applies to domestic revenue. The floors for June 30, 2014 and December 31, 2014 are cumulatively measured from December 31, 2013.

14. **Definition**. The floor on domestic government revenue is defined as total government revenue (tax and non-tax revenues), per the central government fiscal operation table, but excluding external grants, peace keeping operation, and privatization receipts.

15. **Reporting requirement.** Detailed data on domestic revenues will be transmitted on a monthly basis within five weeks of the end of each month.

Floor on priority expenditure (IT)

16. The floor applies to priority spending of the government. The floors for June 30, 2014 and December 31, 2014 are cumulatively measured from December 31, 2013.

17. **Definition.** Priority expenditure is defined as the sum of those recurrent expenditures, domestically-financed capital expenditures, and net lending that the government has identified as priority in line with the EDPRS2. Priority expenditure is monitored through the computerized SIBET expenditure management system which tracks priority spending of the annual budget at the program level.

18. **Reporting requirement.** Data on priority expenditure will be transmitted on a monthly basis within five weeks of the end of each month.

Net accumulation of domestic arrears of the government (IT)

19. A ceiling applies to net accumulation of domestic arrears of the government.[4] The ceilings for June 30, 2014 and December 31, 2014 are cumulatively measured from December 31, 2013.

20. **Definition.** The net accumulation of arrears is defined as the difference between the gross accumulation of new domestic arrears (measured as the difference between payment orders and actual payments related to payment orders issued) and gross repayment of any arrears outstanding since the beginning of the year under review (including repayment of float during the review year and the repayment of older arrears).

21. **Reporting requirement.** Data on repayment of domestic arrears and the remaining previous year's stock of arrears will be transmitted on a monthly basis within five weeks of the end of each month.

C. Limits on External Debt

Limit on new non-concessional external debt of the public sector (AC)

22. A ceiling applies to the contracting and guaranteeing by the public sector of new non-concessional borrowing with non-residents (see below for the definition of the public sector, concessionality and debt). The ceiling is given in Table 1. Quantitative Assessment Criteria and Indicative Targets of the MEFP which applies continuously from December 2, 2013 to October 31, 2016. The ceiling also excludes non-concessional borrowing by one state-owned bank, the Bank of Kigali, which is assumed not to seek or be granted a government guarantee. The ceiling also applies to private debt for which official guarantees have been extended, including future swaps involving foreign currency loans guaranteed by the public sector (see below for swaps), and which, therefore, constitute a contingent liability of the public sector.

23. **Definition of the public sector**. The public sector comprises the general government (the central government, the NBR, local governments which include provinces and districts) and entities in which the government holds a controlling stake (owning more than 50 percent of the shares or

[4] A negative target thus represents a floor on net repayment.

the ability to determine general corporate policy).[5] This definition of public sector excludes the Bank of Kigali.

24. For program purposes, the guarantee of a debt arises from any *explicit* legal obligation of the public sector to service a debt in the event of nonpayment by the debtor (involving payments in cash or in kind), or from any *implicit* legal or contractual obligation of the public sector to finance partially or in full any shortfall incurred by the debtor.

25. **Definition of concessionality**. For program purposes, a debt is concessional if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt.[6] The discount rate used for this purpose is 5 percent.

26. **Definition of debt** for the purposes of the limit in the QAC table is set out in point 9 of the Guidelines on Performance Criteria with Respect to External Debt, effective December 1, 2009. It not only applies to the debt as defined in Point 9 of the Executive Board decision, but also to commitments contracted or guaranteed for which value has not been received. The definition of debt set forth in No. 9 of the Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements reads as follows:

> (a) The term "debt" will be 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, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

[5] Government control of an entity can be established based on the following criteria: (i) ownership of the majority of the voting interest; (ii) control of the board or other governing body; (iii) control of the appointment and removal of key personnel; (iv) control of key committees of the entity; (v) golden shares and options; (vi) regulation and control; (vii) control by a dominant public sector customer or group of public sector customers; and (viii) control attached to borrowing from the government.

[6] The calculation of concessionality will take into account all aspects of the loan agreement, including maturity, grace period, payment schedule, upfront commissions, and management fees.

(i) loans, i.e., 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 sometime after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which 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. The debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(b) Under the definition of debt set out in point 9(a) above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes 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.

Limit on the stock of external payment arrears (AC)

27. A continuous assessment criterion applies to the non-accumulation of payment arrears on external debt contracted or guaranteed by the public sector. External payment arrears consist of external debt service obligations (principal and interest) that have not been paid at the time they are due, as specified in the contractual agreements, but shall exclude arrears on obligations that are subject to rescheduling.

Consolidated Domestic Debt of the Public Sector (IT)

28. For program purposes, domestic debt (DD) excludes treasury bills issued by the NBR for monetary policy purposes. The ceiling on DD applies to domestic commitments contracted or guaranteed by the public sector. This also applies to private debt for which official guarantees have

been extended either implicitly or explicitly. The authorities would inform Fund staff of any changes in debt position of public sector entities.

Adjusters:

- In the case of a shortfall in programmed budgetary loans and grants (per paragraph 11), the ceiling on consolidated domestic debt of public sector will be adjusted *upward* by the same amount as the increase in the ceiling in the NDF, but capped per paragraph 11.
- The ceiling on the DD will be adjus*ted upward* by the amount of expenditure for food imports in the case of a food emergency.

29. **Reporting requirement.** Data on domestic debt of the public sector, including treasury bills issued by the NBR for monetary policy purposes, will be tr*ansmitt*ed on a monthly basis within five weeks of the end of each month.

D. Targets for Monetary Aggregates

Net foreign assets of the National Bank of Rwanda (AC)

30. A floor applies to the net foreign assets (NFA) of the NBR for June 30, 2014 and for December 31, 2014.

31. **Definition.** NFA of the NBR in Rwandan francs is defined, consistent with the definition of the Special Data Dissemination Standard (SDDS) template, as external assets readily available to, or controlled by, the NBR net of its external liabilities. Pledged or otherwise encumbered reserve assets (including swaps) are excluded; such assets include, but are not limited to, reserve assets used as collateral or guarantee for third party external liabilities. Foreign assets and foreign liabilities in U.S. dollars are converted to Rwandan francs by using the U.S. dollar/Rwanda franc program exchange rate. Foreign assets and liabilities in other currencies are converted to U.S. dollars by using the actual end-of-period U.S. dollar/currency exchange rate. Foreign liabilities include, inter alia, use of IMF resources (CCFF and post-conflict emergency assistance purchases and SAF/ESAF/ECF disbursements).

Adjusters:

- The floor on NFA will be adjusted *downward* by the amount of any shortfall between actual and programmed budgetary loans and grants per Table 1. Quantitative Assessment Criteria and Indicative Targets of the MEFP. This adjustment will be capped at the equivalent of US$80 million, evaluated in Rwanda francs at the program exchange rate.

- The floor on NFA will be adjusted *downward* (*upward*) by the extent to which actual encumbered reserve assets are lower (higher) than programmed encumbered reserve assets, evaluated in Rwandan francs at the program exchange rate.[7]

- The floor on NFA will be adjusted *upward/downward* by the extent to which in Rwandan francs at the program exchange rate unused proceeds of the US$400 million euro bond issued in April 2013 exceed/is lower than US$107.3 million by end-June 2014 and not zero by end December 2014..

- The floor on NFA will be adjusted *downward* by the amount of expenditure for food imports in the case of a food emergency, evaluated in Rwanda francs at the program exchange rate.

32. **Reporting requirement.** Data on foreign assets and foreign liabilities of the NBR will be transmitted on a weekly basis within seven days of the end of each week, including breakdown of assets that are pledged or encumbered. This transmission will include daily and weekly data on the NBR's foreign exchange liabilities to commercial banks (including required reserves with the NBR) and the exchange rate used for their conversion into Rwanda francs will be shown separately.

Reserve money (AC)

34. A ceiling applies to the stock of reserve money for June 30, 2014 and December 31, 2014 as indicated in Table 1. Quantitative Assessment Criteria and Indicative Targets of the MEFP. The ceiling is the upper bound of a reserve money band (set at+/- 2 percent) around a central reserve money target).

35. The stock of reserve money for a given quarter will be calculated as the arithmetic average of the stock of reserve money at the end of each calendar month in the quarter. Daily average of all the three months in the quarter will constitute the actual reserve money to be compared with the target.

[7] The programmed amount of encumbered reserve assets stands at zero at June 30, 2014 and December 31, 2014.

36. **Reserve money** is defined as the sum of currency in circulation, commercial banks' reserves, and other nonbank deposits at the NBR.

Adjuster:

- The ceiling on the stock of reserve money will be adjusted symmetrically for a change in the required reserve ratio of commercial banks. The adjustor will be calculated as (new reserve ratio minus program baseline reserve ratio) multiplied by actual amount of liabilities (Rwanda Franc plus foreign-currency denominated) in commercial banks.

37. **Reporting requirement.** Data on reserve money will be transmitted on a weekly basis within seven days of the end of each week. This transmission will include a daily and a weekly balance sheet of the NBR which will show all items listed above in the definitions of reserve money.

OTHER DATA REPORTING REQUIREMENTS

38. For the purposes of program monitoring, the Government of Rwanda will provide the data listed in TMU Table 1 below, weekly data within seven days of the end of each week; monthly data within five weeks of the end of each month; annual data as available.

39. The authorities will inform the IMF staff in writing at least ten business days (excluding legal holidays in Rwanda or in the United States) prior to making any changes in economic and financial policies that could affect the outcome of the financial program. Such policies include but are not limited to customs and tax laws (including tax rates, exemptions, allowances, and thresholds), wage policy, and financial support to public and private enterprises. The authorities will similarly inform the IMF staff of any non-concessional external debt contracted or guaranteed by the government, the NBR, or any statutory bodies, and any accumulation of new external payments arrears on the debt contracted or guaranteed by these entities. The authorities will furnish an official communication to the IMF describing program performance of quantitative and structural assessment criteria and benchmarks within 8 weeks of a test date. The authorities will on a regular basis submit information to IMF staff with the frequency and submission time lag as indicated in TMU Table 1. The information should be mailed electronically to the Fund. (email: afrrwa@imf.org).

TMU Table 1. Summary of Reporting Requirements

	Frequency of Data[10]	Frequency of Reporting[10]	Frequency of Publication[10]
Exchange Rates[1]	D	W	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	W	W	M
Reserve/Base Money	W	W	M
Broad Money	M	M	M
Central Bank Balance Sheet	W	W	M
Consolidated Balance Sheet of the Banking System	M	M	M
Interest Rates[3]	M	M	M
Volume of transactions in the interbank money market and foreign exchange markets and sales of foreign currencies by NBR to commercial banks	D	W	W
Liquidity Forecast Report[4]	W	W	W
Consumer Price Index[5]	M	M	M
Composite Index of Economic Activity (CIEA) and sub-components compiled by the NBR	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[6] – General Government[7]	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[6]– Central Government	M	M	M
Comprehensive list of tax and non tax revenues[8]	M	M	M
Comprehensive list of domestic arrears of the government	M	M	M
The ten (10) largest components of transfers in the fiscal table	M	M	M
Social security contributions (RAMA and CSR)	M	M	M
Stocks of public sector and public-Guaranteed Debt as compiled by MINECOFIN and NBR[9]	A	A	A
Privatization receipts	M	M	M

TMU Table 1. Summary of Reporting Requirements (concluded)

	Frequency of Data[10]	Frequency of Reporting[10]	Frequency of Publication[10]
External Current Account Balance	A	SA	A
Exports and Imports of Goods and subcomponents.	M	M	Q
Exports and Imports of Goods and Services and subcomponents	A	A	A
GDP/GNP	A, Q	Q, SA	Q

[1] Includes the official rate; Forex Bureau Associations rate; weighted average of the interbank money market rates; and weighted average of the intervention rate by the NBR.
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Both market-based and officially-determined, including discount rates, money market rates, interbank money market rate, rates on treasury bills, notes and bonds.
[4] One-week ahead forecasts of liquidity submitted on weekly basis. For example, in reporting data as of the last week of April, liquidity forecasts for the first week of May should be reported. The forecasted liquidity should be classified by net foreign assets, net credit to government, nongovernment credit, reserve money, currency in circulation, net credit to commercial banks broken down into discount window and money market (absorption or injection), and other item net.
[5] Includes General Index; Local Goods Index; Imported Goods Index; Fresh Products Index; Energy Index; General Index excluding Fresh Products and Energy; and their breakdowns as published by the NISR.
[6] Foreign, domestic bank, and domestic nonbank financing.
[7] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[8] Includes proceeds from privatization, accompanied by information on entities privatized, date of privatization, numbers and prices of equities sold to the private sector.
[9] Includes debts of the Bank of Kigali. Also includes currency and maturity composition.
[10] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Semi-annually (SA); Irregular (I).