INTERNATIONAL MONETARY FUND

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DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

December 2017

THIRD AND FOURTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, EXTENSION OF THE ARRANGEMENT, AND MODIFICATION OF PERFORMANCE CRITERIA—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

In the context of the third and fourth reviews under the Extended Credit Facility Arrangement, Extension of the Arrangement, and Modification of Performance Criteria, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on December 11, 2017, following discussions that ended on October 5, 2017, with the officials of the Democratic Republic of São Tomé and Príncipe on economic developments and policies underpinning the IMF arrangement under the Extended Credit Facility. Based on information available at the time of these discussions, the staff report was completed on November 27, 2017.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the International Development Association (IDA).
- A **Statement by the Executive Director** for the Democratic Republic of São Tomé and Príncipe.

The documents listed below have been or will be separately released:

Letter of Intent sent to the IMF by the authorities of the Democratic Republic of São Tomé and Príncipe*
Memorandum of Economic and Financial Policies by the authorities of the Democratic Republic of São Tomé and Príncipe*
Technical Memorandum of Understanding*

*Also included in Staff Report

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Press Release No. 17/482
FOR IMMEDIATE RELEASE
December 11, 2017

International Monetary Fund
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Washington, D. C. 20431 USA

IMF Executive Board Concludes Third and Fourth Reviews of the Program Supported by the Extended Credit Facility (ECF) Arrangement with São Tomé and Príncipe

The Executive Board of the International Monetary Fund (IMF) today completed the third and fourth reviews of the arrangement under the Extended Credit Facility (ECF)[1] for São Tomé and Príncipe. The Board's decision enables the immediate disbursement of SDR 1,268,570 (about US$1.8 million), bringing total disbursements under the arrangement to roughly SDR 3.17 million (about US$4.5 million).

In completing the review, the Executive Board granted the authorities' request for waivers for nonobservance of the end-December 2016 performance criteria on the domestic primary balance and changes in net bank financing of the central government, based on the corrective measures introduced by the authorities. In addition, the Executive Board established targets and structural benchmarks for 2018. The ECF arrangement for São Tomé and Príncipe in the amount of SDR 4.44 million (about US$6.2 million or 60 percent of the country's quota at the time of approval) was approved on July 13, 2015 (see Press Release No. 15/336) to support the government's economic reform program for stronger and more inclusive growth.

Following the Executive Board's discussion, Mr. Tao Zhang, Deputy Managing Director and Acting Chair, said:

"São Tomé and Príncipe's economy continues to grow steadily and the outlook is favorable. However, implementing sound policies to bring the fiscal deficit and public debt to sustainable levels will be key to achieving sustained, robust growth and reducing poverty. In this context, the 2017-21 National Development Plan is expected to help diversify the economy and improve the business environment.

"The authorities have taken decisive action to bring the program back on track. Program targets have been met and good progress was made on structural reforms, including the planned

[1] The ECF is a lending arrangement that provides sustained program engagement over the medium to long term in case of protracted balance of payments problems.

adoption of a VAT. Measures have been taken to meet the end-2017 fiscal targets. In addition, the 2018 budget appropriately targets further consolidation to lower the domestic primary deficit.

“The authorities aim to strengthen public financial management. Efforts will be made to prevent new domestic arrears, reduce the current stock of arrears, and tackle fiscal risks posed by the large operational losses at the state-owned electricity and water enterprise. To ensure debt sustainability while meeting the large investment needs, external borrowing should be at concessional terms.

“In the financial sector, banking supervision has been strengthened and financial soundness indicators have improved. The liquidation of Banco Equador has resumed. Steps will be taken to reduce the stock of non-performing loans and further enhance financial stability.”

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

THIRD AND FOURTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, EXTENSION OF THE ARRANGEMENT, AND MODIFICATION OF PERFORMANCE CRITERIA

November 27, 2017

KEY ISSUES

The economy is expected to grow at a steady pace of 4 percent in 2017, albeit slower than projected at the second review. Over the medium term, growth is projected to accelerate to 5½ percent, spurred by tourism, agriculture, and externally-funded investment. Meanwhile, excessive rainfall damaged some crops and raised the price of locally-produced food. Consequently, inflation is expected to increase to 6 percent at end-2017, from 5.1 percent at end-2016.

Program implementation is broadly back on track. After missing the end-2016 fiscal targets by large margins, the government adopted corrective measures and met all five end-June 2017 performance criteria (PCs). The implementation of structural reforms under the program is progressing, albeit at a much slower pace than anticipated due mainly to capacity constraints and delays in the delivery of technical assistance (TA).

Discussions focused on safeguarding end-2017 targets and setting the policy framework for 2018. The government identified expenditure cuts to offset potential revenue shortfalls in the second half of 2017. The 2018 budget will target a domestic primary budget deficit of 1 percent of GDP against the target of 1.8 percent of GDP in 2017, reflecting a decline in external financing. The government also plans to take near-term measures to address the large losses from the state-owned utility company, EMAE. Meanwhile, the central bank continues to strengthen banking supervision, implement a strategy for resolving the high rate of non-performing loans in the banking system, and liquidate the failed Banco Equador.

Significant risks to the program remain, notably from delays in structural reforms and the associated shortfalls in external financing. In addition, the authorities' commitment to implement the program will also be tested in the run-up to the July 2018 legislative elections.

In light of the recently-improved program performance, reflecting the authorities' strong corrective actions, staff recommends the completion of the joint third and fourth reviews, approval of the extension to end-2018 and rephasing of the program.

Approved By
David Owen (AFR) and Kevin Fletcher (SPR)

Discussions were held in both São Tomé and Príncipe islands during September 20 to October 5, 2017. The staff team included Xiangming Li (head), Charles Amo-Yartey, Jehann Jack, Gabriel Srour (all AFR) and Luiza Antoun de Almeida (SPR). The mission was assisted in headquarters by Marlon Francisco and María Inés Canales Munoz. The mission met with Prime Minister Patrice Trovoada, Minister of Finance Américo Ramos, Minister of Justice Ilza Vaz, Minister of Foreign Affairs Urbino Botelho, the Governor of the Central Bank Hélio Almeida, the president of the autonomous region of Príncipe José Cassandra, other senior government officials, and representatives of the private sector and development partners.

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RECENT ECONOMIC DEVELOPMENTS

1. **The economy continues to grow steadily in 2017, but growth has been more subdued than projected at the second review, and prices have risen more than expected.** Real GDP is forecast to grow by 4 percent in 2017, similar to 2016 but 1 percentage point below the previous projection. While externally-funded investment has picked up, with imports of equipment and construction materials rising by 30 percent, tourist arrivals and cocoa exports declined slightly. Twelve-month inflation picked up mid-year and was at 6.5 percent at end-August 2017, driven mainly by prices of locally-produced food. As this effect dissipates, inflation is projected to moderate to 6 percent at end-2017. Net international reserves remained adequate at US$54.4 million (or 3.5 months of imports) at end-June 2017.

2. **Fiscal targets for end-June 2017 were met through prudent expenditure execution and corrective tax measures, following slippages in the previous year (Text Table 1).** The domestic primary deficit (DPD) reached 4 percent of GDP in 2016 against the program target of 2 percent of GDP, driven by overspending in the run-up to the two-stage presidential elections, a sharp drop of oil import duties due to lower oil prices, and delayed implementation of corrective measures identified during the second review (¶13). The authorities took corrective measures in 2017, reducing primary domestic expenditure by almost 1½ percent of GDP (annualized) during the first eight months relative to the same period in 2016. At the same time, they implemented tax measures in late 2016 and in the May revised budget to raise revenue. However, tax revenue through end-August was lower than anticipated (¶3). Consequently, the DPD reached 2.7 percent of GDP (annualized rate) in August, significantly above the 1.8 percent of GDP target for the whole year.

Text Table 1. Fiscal Performance 2017: Jan-Aug
(in percent of GDP)

	2016			2017			
	Jan-Aug			H1	Jan-Aug		
	Actual [1]	Actual	2nd rev.	Actual [1]	Actual [1]	2nd rev.	Prog.
Total domestic revenue	14.6	14.5	15.7	14.2	13.7	16.4	14.5
Total domestic revenue (ex oil)	13.2	13.6	14.9	13.7	13.2	16.4	14.2
Tax revenue	12.0	12.2	13.5	12.2	11.9	15.0	13.0
Import taxes	4.7	4.8	6.3	4.4	4.2	6.9	4.9
Consumption taxes	1.2	1.2	1.3	1.6	1.7	1.5	1.6
Profit taxes	1.1	1.3	1.3	1.8	1.8	1.6	1.6
Personal income taxes	3.4	3.4	3.3	2.9	2.9	3.6	3.4
Other taxes	1.6	1.6	1.2	1.5	1.4	1.5	1.6
Nontax revenue	2.6	2.3	2.3	2.0	1.8	1.4	1.5
Of which: oil revenue	1.4	1.0	0.9	0.5	0.5	0.0	0.4
Total domestic expenditure	17.9	18.1	17.6	17.0	16.3	18.9	16.7
Primary domestic expenditure	17.5	17.6	16.9	16.5	15.9	18.1	16.0
Current expenditure	16.9	17.2	16.1	16.4	15.8	17.2	16.2
Personnel costs	8.3	8.8	8.7	8.8	8.1	8.5	8.5
Goods and services	3.3	3.2	3.0	3.0	3.1	3.1	2.7
Interest payments	0.4	0.4	0.7	0.5	0.4	0.8	0.7
Transfers	3.9	3.6	2.9	3.3	3.2	3.7	3.4
Other expenditures	1.0	1.1	0.8	0.7	0.8	1.0	0.9
Treasury-funded capital expend.	0.8	0.6	0.7	0.4	0.3	1.1	0.3
HIPC-related capital expenditure	0.2	0.2	0.9	0.2	0.2	0.6	0.2
Domestic Primary Balance	-4.3	-4.0	-2.0	-2.8	-2.7	-1.8	-1.8
Program target	…	-2.0	-2.0	-3.0	…	-1.8	-1.8

Sources: Ministry of Finance and IMF staff estimates.
[1] Annualized rates

Text Table 2. Domestic Arrears

(Stocks, in billions of dobra unless specified otherwise)

	2016 Actual	Jun-17 Actual
Treasury arrears to suppliers	442.7	452.4
EMAE	55.1	51.6
CST	98.6	111.9
Other suppliers	288.9	288.9
In millions of dollars		
Treasury arrears to ENCO (price differential)	43.9	41.9
EMAE to ENCO	60.4	66.6

Sources: Ministry of Finance and IMF staff estimates.

3. **The government faced a tight financing constraint (Text Table 2).** A number of unanticipated developments contributed to the poor revenue outturns (MEFP ¶5). These included a decline in imports of key commodities, lower than projected oil prices, a negative impact of a correction of the formula for calculating personal income tax (PIT), delayed tax payments by the main oil importer, ENCO, and little revenue yields from a higher duty on alcoholic beverages implemented in July. This duty was on top of a new consumption tax implemented in January (¶13) and triggered a sharp fall in imports. Furthermore, the World Bank has postponed disbursement of its budget support grant of $5 million (1.3 percent of GDP) for 2017 due to a delay in preparing the least-cost production and financial management plans of the state-owned utility company, EMAE. Against this challenging financing situation, the government's arrears to suppliers increased slightly (about 0.1 percent of GDP). Favorable oil price differentials, however, have reduced the debt to ENCO by about $2 million during the first half of 2017, and $4.5 million (1.3 percent of GDP) in 2016.

4. **Credit growth remains tepid and financial soundness improved somewhat, albeit from a weak position** (MEFP ¶7&8, Table 6). Year-on-year, credit to the economy grew by 3.6 percent at end-June 2017. Meanwhile, excess liquidity in the banking system remained high, and the Banco Central de São Tomé e Príncipe (BCSTP) lowered the reference rate by 100 basis points to 9 percent in June. Tighter supervision and loan reclassification led to higher non-performing loans (NPL) and provisioning in some banks, although the sector-wide NPL ratio declined marginally and the risk-weighted capital adequacy ratio rose from 28 percent to 30 percent.

5. **The liquidation of Banco Equador is proceeding.** The strike in the judicial system ended in July, which allowed the court-appointed liquidator to assume duties in September. The liquidator is working with the Management Commission, which had taken over the bank since the central bank withdrew the bank's license.

6. **The current account deficit is expected to widen, financed by FDI and external project loans.** The deficit is projected to increase from 6 percent of GDP in 2016 to 12 percent of GDP in 2017. Imports of capital goods and oil products rose by 30 and 25 percent respectively in the first six months of 2017, while tourist arrivals and cocoa exports remained broadly constant over the same period. In contrast, imports were contained in 2016, while exports of goods and services increased by 8 percent, boosted by tourist arrivals from more frequent flights and the ease of tourist visa restrictions for certain categories of visitors since the beginning of 2016. Meanwhile, FDI related to deep-water oil exploration picked up in 2017, and concessional project-loan disbursements increased relative to the previous year.

PROGRAM PERFORMANCE

7. After missing two fiscal performance criteria (PCs) at end-2016, the program is broadly back on track (MEFP Table 1). The PCs on DPD and changes in net bank financing of the central government for end-2016 were missed. In response, the government introduced corrective measures in early 2017 (¶13), which, along with measures implemented since late 2016, have enabled the authorities to meet all the PCs, including DPD and NIR, for end-June 2017. However, three fiscal indicative targets (ITs) were missed by small margins: (a) the tax revenue shortfall was attributable to ENCO's delayed payment of import duties; (b) the floor on pro-poor spending was missed narrowly (by about 0.1 percent of GDP) as the authorities were unable to fully protect this spending after making significant expenditure cuts to bring the fiscal program back on track; and (c) Treasury accumulated arrears to utility and communication companies. It is worth noting that the poor and vulnerable were largely protected from bearing an undue burden of adjustment, as pro-poor spending increased by about 1.5 percentage points as a share of domestic primary spending compared with the original budget, and the floor on pro-poor spending targeted for the whole year remains as in the second review. The IT on base money was also missed.

8. Progress was made on structural reforms (MEFP Table 2). The end-2016 benchmark on completing an assessment of regulation and supervision was met and that on enhancing the responsibilities of BCSTP's Audit Board in line with a conventional audit committee was implemented with a delay (in March 2017). A reform plan for EMAE, consistent with full cost recovery, was also adopted. Two other end-2016 and one end-June 2017 structural benchmarks (SBs)—submitting a VAT law to the National Assembly, completing a Public Investment Management Assessment (PIMA), and submitting a draft public private partnership (PPP) law to the National Assembly—were not implemented due largely to delays in technical assistance (TA) delivery.

ECONOMIC OUTLOOK AND RISKS

9. The near- and medium-term outlook is favorable but challenges remain. GDP growth is expected to be 4 percent in 2017 and to accelerate to 5.5 percent in the medium term, driven by robust activity in construction, agriculture, and tourism, which, in turn, are spurred by externally-financed infrastructure projects, including the airport expansion and road construction. The outlook is subject to both upside and downside risks. On the upside, externally-financed projects could be implemented faster than envisaged; some indications suggest that new projects financed by the World Bank and EU may materialize soon. In particular, two hydroelectric projects financed by the World Bank may proceed faster than expected and a project for the expansion of the airport could start as early as mid-2018. In addition, following the resumption of diplomatic relations with China in December 2016, investment and economic support from China is likely to accelerate, including by the private sector as indicated by the increased visits of Chinese entrepreneurs and the recent establishment of an association of Chinese businesses. On the downside, risks include less buoyant tourist arrivals due to infrastructure constraints, the continued large arrears accumulation by EMAE to ENCO, which represents a major fiscal risk, and weak capacity given that São Tomé and Príncipe is a fragile state, which could delay structural reforms and the associated official financing. In addition, the legislative elections of July 2018 could disrupt policy implementation.

10. The updated Debt Sustainability Analysis (DSA) shows that São Tomé and Príncipe remains at a high risk of debt distress. The baseline scenario shows that debt is sustainable over the medium term if the government continues fiscal consolidation, eschews non-concessional loans, and works to diversify the economy and expand the export base. The ratios of the present value of debt to GDP, exports, and revenue exceed their thresholds for high risk of debt distress early in the projection, but decline below the thresholds in the long run. The unsustainable historical scenario illustrates that continued fiscal consolidation is essential. A customized scenario shows that it is vital to seek grants, highly concessional financing, and equity financing without government guarantee for extremely large infrastructure projects, such as the airport and seaport, because a large amount of loans, even at concessional terms, would threaten debt sustainability. To this end, the government has committed to limit external borrowing to only concessional loans, with an indicative annual ceiling of 4 percent of GDP.

11. The external debt to GDP ratio is expected to continue to decline in 2017, while the total debt to GDP ratio has been revised up as domestic arrears are included for the first time. External debt is projected at 46 percent of GDP at end-2017 from 62 percent in 2015-16, benefiting from a strengthening euro and steady real growth. The ratio is expected to continue to decline moderately in the coming years even as concessional loans contracted during the past three years ($80 million) are disbursed overtime. Meanwhile, the government was able to secure relief from China of $18.4 million (4.9 percent of GDP) in pre-HIPC legacy arrears and is making best efforts to reach an agreement consistent with the representative Paris Club agreement on other pre-HIPC legacy arrears, which are excluded in the DSA. It is also actively seeking a debt rescheduling agreement with Angola, Brazil, and Equatorial Guinea.[1] Meanwhile, the total public and publicly guaranteed (PPG) debt is estimated at 59 percent of GDP ($225 million) in June 2017 after including domestic arrears of 13 percent of GDP ($48.9 million), mainly from the central government to ENCO. It would rise further to 76 percent of GDP if the arrears of state-owned EMAE to ENCO were included.

12. A new debt management performance assessment (DeMPA) has been completed with the support of the World Bank in November 2016. The DeMPA underscores some progress since the last assessment in 2011, notably the approval of a public debt law in 2013 and the development of a medium-term debt management strategy and a T-bill market. The main recommendations include improving the debt service projections, conducting risk analyses, reporting more detailed information of the debt stock, and migrating the database from Excel to CS-DRMS.

[1] External arrears have accumulated under these loans. A $30 million loan extended to Sao Tome and Principe by Nigeria is under dispute. The loan was extended as an advance of oil revenues of a now stalled joint development project. The first payment was due in 2010.

POLICY DISCUSSIONS

A. Address Fiscal Slippage and Minimize Contingent Liabilities

13. The government has taken significant steps to bring the program back on track, but further effort is needed to meet the end-2017 DPD target. As noted previously, corrective measures were implemented in late 2016 and new ones were introduced in the May revised 2017 budget. The revenue measures, including a new consumption tax on imported alcoholic beverages and higher duties on selected imported commodities, are expected to generate gains of about 1 percent of GDP in 2017 (Text Table 3). Spending measures, including cuts in goods and services, transfers, and capital projects, yield savings of about 0.6 percent of GDP. The government also reached agreements in July with two large private businesses and SOEs to gradually pay tax arrears, including withheld income taxes on employees' salaries and consumption tax. Close to 22 billion dobras (about ¼ percent of GDP) have already been paid by the private businesses during July and August, and an additional 8.5 billion dobras (about 0.1 percent of GDP) will be paid over the remainder of the year, while 5 billion dobras is expected from the SOEs in 2017. Nevertheless, in light of the lower-than-expected outturns at end-August due to unanticipated developments, staff estimates that, on current trend, revenue will fall short by 2.4 percent of GDP in 2017 relative to the revised budget.

14. The authorities have identified additional measures to address the shortfall in revenues (Text Table 3). An agreement was reached with ENCO for it to pay the balance of import duties in 2017 (close to 0.8 percent of GDP). Similar agreements are being pursued with others with significant arrears (0.2 percent of GDP). Furthermore, the authorities identified cuts in primary current expenditure and domestically-funded capital expenditures of 1.4 percent of GDP. The cuts are made possible by the cautious execution of the budget to-date to match available resources and by the substantial external project grants and loans that finance essential capital spending.

15. The authorities reiterated their commitment to achieve the end-2017 program target of 1.8 percent of GDP. They will continue to closely monitor budget execution in 2017 and stand ready to further limit non-mandatory spending as needed to ensure expenditure commitments remain within available resources. They recognize that this is important in light of the uncertainty in the timing of the EU disbursement of €3.5 million (1 percent of GDP) in 2017 and the amount of the associated variable tranche of €1 million. To smooth out the impact of the postponed disbursement of a World Bank budget support grant of $5 million (1.3 percent of GDP) in 2017, the floor for domestic financing was raised by the equivalent of $3 million (0.8 percent of GDP); the rest of the shortfall will be addressed by rephasing previously budgeted arrears clearance in 2017 to 2018-20, and by consolidation in 2018. The accumulation of new arrears will be avoided.

Text Table 3. Estimated Impact of Fiscal Measures in 2017

(in percent of GDP)

	Impacts of measures in 2017			Projected improvement of 2017 relative to 2016
	taken at end-2016 and in revised budget	taken in Q3 to offset revenue shortfall	Total	
Total revenue gains	1.0	1.0	2.0	1.1
Higher duty on imported goods	0.1	…	0.1	0.1
Higher consumption taxes	0.4	…	0.4	0.4
Broader profit tax base	0.2	…	0.2	0.2
Broader personal income tax base and collection	0.1	…	0.1	0.1
Nontax revenue	0.1	…	0.1	0.1
Payment of duty by ENCO	…	0.8	0.8	…
Collection of tax arrears based on agreements	…	0.2	0.2	0.2
Total domestic expenditure cuts	0.6	1.4	2.0	1.5
Cuts in primary current expenditure	0.6	0.6	1.2	1.2
Cuts in domestically-financed capex	0.0	0.8	0.8	0.3
Total savings	**1.6**	**2.4**	**4.0**	**2.6**

Sources: Ministry of Finance and IMF staff estimates.

16. **Further fiscal consolidation will continue in 2018**. The DPD targets 1 percent of GDP, ½ percent below the target established in the second review, to address a further shortfall in budget support in 2018 (MEFP ¶17) and to make up for delayed arrears clearance payment. The additional consolidation will be achieved mainly by suspending the current tax credit in the PIT, with an estimated gain of 0.2 percent of GDP and limiting current expenditure increases. Particularly, the authorities have agreed to limit wage growth, restricting new hiring to priority needs such as education and health, and seeking savings in these sectors and other current spending to offset the costs of new hiring. They indicated that new teachers are urgently needed to lower the teacher-to-student ratio and to improve teaching. Staff advised that spending in these sectors be scaled up gradually to allow time for adjustment.

17. **The government is also committed to bringing the arrears clearance plan back on track over the medium term** (MEFP ¶16-17). Due to a shortfall in external financing in 2017-18, some arrears clearance repayments have been rephased to later years. However, the government agreed that arrears clearance is a priority and will prioritize arrears clearance if additional resources, including privatization proceeds or budget support, materialize. Adopting a 2018 budget in line with these parameters is a prior action for the combined third and fourth reviews.

18. **Structural fiscal reforms are proceeding slowly due to capacity constraints and delays in technical assistance as the IMF is faced with high demand for its TA.** The automatic price adjustment mechanism has been implemented since July 2016, and allowed the favorable fuel price differentials between import and pump prices to reduce the government's debt to ENCO from the past fuel price subsidy. In addition, the authorities are working towards introducing a VAT regime in early 2019 with the assistance of an IMF advisor funded by the Revenue Mobilization Trust Fund. The VAT law is being drafted for submission to the National Assembly by end-2017 (*delayed end-2016 SB*)

and an AfDB-financed IT system is being installed to support VAT implementation. Progress is being made in strengthening public financial management (PFM) to rein in arrears (MEFP ¶22). In addition, a PPP law is being finalized for submission to the National Assembly by end-2017 *(delayed end-June 2017 SB)*. Completion of a PIMA (*end-December 2016 SB*), which will help to build capacity for managing public investment, has been delayed; the World Bank now plans to provide a streamlined PIMA more suitable to the country's need. With the support of IMF TA, the authorities are implementing the recommendations of recent IMF TA on tax administration and PFM (MEFP ¶21).

19. The authorities are continuing to pursue strategies to address the unreliable supply and high cost of electricity. With the support of the World Bank and the European Investment Bank, a major project is underway to revamp EMAE with concrete actions to implement least-cost production options, strengthen financial discipline, and move to full cost recovery. To contain the fiscal risks while the medium-term measures are being implemented, near-term measures have been adopted to increase bill payments, collect arrears, and conduct an audit to help design measures to cut labor costs (MEFP ¶19).

B. Advance Monetary Reforms

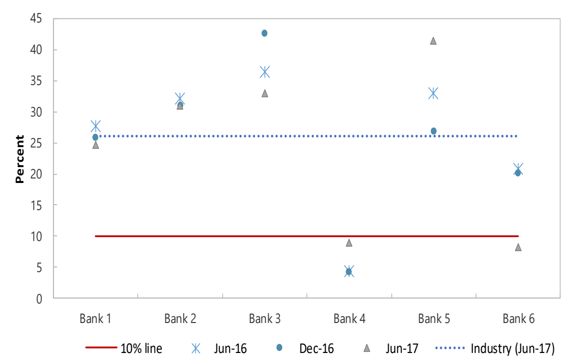
20. The authorities have taken steps to further develop the securities' market. The BCSTP is working on amending regulations to allow for a secondary market and longer-term instruments, including a 3-year note. While the interbank market continues to be dormant, BCSTP required all banks to publish their 2016 financial statements to increase transparency and promote interbank activity.

21. The central bank announced the redenomination of the currency. Among the set of monetary reforms, the BCSTP has announced its plans to redenominate the currency from January 1, 2018, exchanging 1 new dobra for 1,000 old ones. The new bills will include innovative features to make them secure against counterfeiting and the redenominated exchange rate will be 24.50 dobras for 1 euro. New coins will also be issued. The BCSTP is implementing an extensive awareness campaign to smooth the transition and support this monetary reform plan.

C. Reduce Risks in the Banking Sector

22. The authorities have made progress in implementing an NPL reduction strategy, but the banking sector remains vulnerable. As noted previously, the BCSTP has stepped-up supervision and conducted internal asset quality assessments, strengthening financial soundness. As a result, NPLs in some banks have increased. In particular, the NPL ratio of one bank rose from 27 percent to 41 percent during the first half of the year, but have since reverted as a large loan started to perform again by August. Meanwhile, to tackle the still high NPL ratios, an out-of-court settlement mechanism is being developed and judges with requisite skills to deal with NPL cases are being hired. The implementation of international accounting standards as discussed below would also help speed up NPL write-off.

Text Chart 1. NPL Ratios by Bank, Jun-16 to Jun-17



Sources: São Tomé and Príncipe authorities and IMF staff estimates.

23. The Asset Quality Review (AQR, *end-December 2017 structural benchmark*) has begun with the support of the World Bank. The authorities launched the call for expressions of interest in September to find an international audit firm to carry out the AQR. The AQR report will be used to assess NPLs and provisioning. Because of earlier difficulties in identifying funding, the process is not expected to be completed before mid-2018. Staff proposes to reset the completion date of this benchmark to end-June 2018.

24. The authorities plan to move forward with implementation of the International Financial Reporting Standards (including IFRS 9) as soon as the AQR results on the value of bank assets are available. BCSTP signed a cooperation arrangement with the Central Bank of Brazil in October to facilitate IFRS implementation. The authorities are working to ensure that all the preparatory work—including the legal instruments as well as the full adoption of the accrual basis of recording assets, reclassification of financial statement items, and reconfiguration of the IT system to align with the new presentation and disclosure rules—is at an advanced stage by mid-2018 so that the central bank and commercial banks can become fully IFRS compliant by end-2018.

25. The liquidation of Banco Equador is proceeding to realize the value of the remaining assets. The court-appointed liquidator is working with the BCSTP Management Commission, complemented by IMF TA in mid-November 2017 to guide the resolution.

D. Other Structural Reforms

26. The authorities have prepared a National Development Plan (NDP 2017-2021) to operationalize their long-term development agenda over the medium term (MEFP ¶33). The comprehensive plan, which replaces the second National Poverty Reduction Strategy Paper (PRSP-II 2012-16), identifies priorities for developing the economy and reducing poverty across social and economic areas. The paper acknowledges little improvement in the poverty rate, which has remained over 65 percent since 2000, and weak implementation of sectoral programs in the past due to capacity constraints and limited resources. It sets ambitious objectives, including achieving a sustainable growth rate of 5.5 percent and reducing poverty to 40 percent.

27. Key sectorial strategies are also being planned. A private sector strategy (2015–24), prepared with the help of AfDB, is being implemented and a national export diversification strategy (*end-December 2017 structural benchmark*), centered on sustainable tourism growth, is also being developed with World Bank support. The latter project has been further delayed due to setbacks in securing an external expert, and is now expected to be completed at end-June 2018 (MEFP ¶32).

PROGRAM ISSUES, SAFEGUARDS, AND RISKS

28. Completing the third and fourth reviews is conditional on the authorities implementing a prior action on submitting to parliament a 2018 budget in line with the program.

29. The authorities are requesting waivers for the nonobservance of two periodic performance criteria on the basis of strong remedial measures implemented (¶7). The PCs on DPD and net domestic borrowing were missed at end-December 2016; all end-June 2017 PCs were met. Given that São Tomé and Príncipe has a pegged exchange rate, which limits control of monetary conditions, staff proposes to change the indicative target on base money into a memorandum item for future test dates. The authorities are also requesting a modification of the external arrears PC to clarify that the PC captures the accumulation of new external arrears.

30. The authorities also request an extension of the ECF program to end-2018, from July 12, 2018, and a rephasing of the final disbursement. The extension would provide more time for the implementation of structural reforms to meet program objectives—including strengthening revenue mobilization, improving PFM, and taking initial steps to contain the fiscal risk of EMAE—and for conducting the last review. Accordingly, the March 2018 test date is proposed to be rephased to June 2018. As discussed in the policy section, the authorities agreed to introduce new SBs for adopting measures to contain EMAE's losses in the near term (end-December 2017) and for adopting a financial management plan and a least-cost production plan for EMAE to achieve financial sustainability over the medium term (end-June 2018). In addition, new target dates are proposed for the SBs on adopting a VAT law, completing the AQR, and finalizing the export diversification strategy. Clarifications to the TMU are also proposed.

31. Staff notes a mistaken assessment that the end-June 2016 PC on changes in net bank financing of the central government was met at the time of the second review. Since this was a technical computation error by the staff, no waiver is required. Furthermore, the corrective actions that were taken to address the missed end-June 2016 PC on the domestic primary balance addressed the same underlying problem.

32. The program is fully financed and staff's assessment of São Tomé and Príncipe's capacity to repay the Fund remains broadly unchanged from the ECF arrangement request (Table 11). São Tomé and Príncipe's capacity to repay the Fund remains strong, as obligations remain small relative to exports and reserves.

33. Significant risks to the program remain. Revenues could surprise on the downside and weak capacity could constrain program implementation, which, in turn, could delay external financing. Contingent liabilities from EMAE and policy slippages ahead of legislative elections in July 2018 also represent risks.

34. Safeguards. The 2015 safeguards assessment found that severe capacity constraints have contributed to a weak safeguards framework at the BCSTP. However, external audits conducted by a reputable audit firm continue to serve as a critical safeguard. The BCSTP strengthened the Audit Board with revised roles and responsibilities that are in line with a conventional audit committee in March 2017 (delayed end-December 2016 structural benchmark). The BCSTP also plans on submitting draft legal reforms to the Ministry of Finance, in line with staff's recommendations, by end-2017. In addition, to obtain technical assistance for IFRS implementation, the BCSTP has established a cooperation agreement with the Central Bank of Brazil; it also plans to be fully IFRS compliant for FY18.

35. Statistics. Efforts to address data shortcomings will continue, including improving the balance of payments statistics and extending the coverage of the international investment position. With the national accounts rebased to 2008 and a new CPI, the next steps include splicing the pre- and post-2008 GDP and pre- and post-2014 CPI series and developing demand side GDP data with support of the IMF Statistics Department (STA), programmed for FY18 within a broader TA strategy. Ongoing TA from STA and the Central Africa Regional Technical Assistance Center, which São Tomé and Príncipe has recently joined, will support these initiatives.

36. Continued TA is essential to mitigate the risks from weak capacity in São Tomé and Príncipe, a fragile state. Continued hands-on support to help the authorities learn by doing is essential to build gradually much needed capacity. In particular, the authorities need guidance on how to implement the recommendations that have been provided by IMF TA, including in (i) strengthening tax administration, (ii) implementing VAT, (iii) improving PFM (macroeconomic forecasting, reporting, budget preparation, control, and monitoring), (iv) strengthening banking supervision, and (v) improving macroeconomic statistics.

STAFF APPRAISAL

37. The authorities have demonstrated strong commitment to the program by bringing the program broadly back on track following slippages in 2016, despite significant challenges. Expenditure cuts and revenue measures implemented since late 2016 have enabled the authorities to meet all end-June 2017 PC targets. In addition, budget execution in 2017 has been kept in line with realized revenue, making it possible to implement additional spending cuts in the last quarter of 2017 to offset the lower-than-expected revenue outturn. Steady progress has been made in implementing structural reforms, despite delays caused by capacity and financing constraints. Notably, a VAT regime is now expected to be introduced in early 2019 with support from the IMF and the AfDB.

38. Overall, São Tomé and Príncipe's macroeconomic conditions and outlook are favorable. GDP growth is projected to stay at 4 percent in 2017 and pick up to 5.5 percent over the medium term, while inflation should gradually wind down to around 5 percent. Fiscal consolidation is expected to narrow the DPD to 1.8 percent of GDP at end-2017 and 1 percent of GDP in the medium term, which will provide support to the pegged exchange rate. The baseline scenario shows that debt is sustainable over the medium term if the government continues fiscal consolidation, eschews non-concessional loans, and works to expand the export base.

39. This outlook is subject to both downside and upside risks. In particular, a weakening of resolve for reform in the run-up to legislative elections in mid-2018 could derail continued fiscal consolidation. Significantly delayed progress in reducing the large losses of EMAE would increase the fiscal risk. Contracting a large amount of new debt, even on concessional terms, for very large projects could threaten debt sustainability. In addition, failure to implement structural reforms could hinder investment and growth. At the same time, the economy and revenue could surprise on the upside if externally financed projects pick up more than expected.

40. In this context, staff welcomes the authorities' assurances to closely monitor budget execution and ensure expenditure matches available resources. This is essential for ensuring that 2017 targets are achievable considering the significant expenditure cuts and the uncertain revenue.

41. The authorities appropriately anchored the 2018 budget at a DPD of 1 percent of GDP. The continued fiscal consolidation is needed because of the lower than previously anticipated budget support and the persistent high risk of debt distress. The consolidation is expected mainly through suspending tax allowances and containing current expenditure increases, including wages.

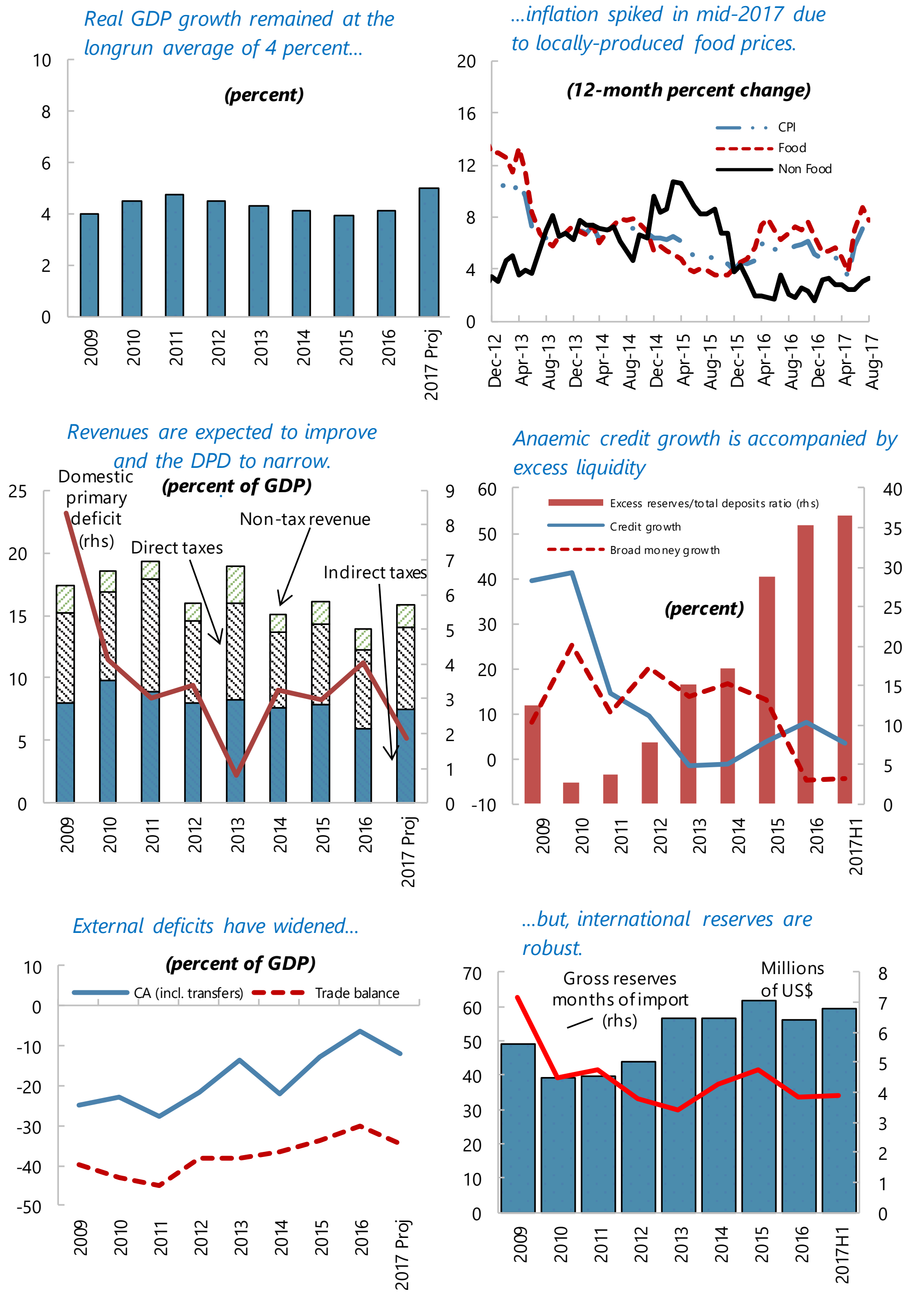
42. Staff welcomes the authorities' commitment to limit borrowing to a moderate amount of concessional loans, address domestic arrears, and tackle fiscal risks posed by EMAE's operational losses. PFM reforms are being implemented to avoid further accumulation of arrears in 2017. The government will also prioritize arrears reduction if additional resources become available. The proposed borrowing plan is consistent with reducing the risk of high debt distress overtime. In addition, concrete steps are being taken to limit losses at EMAE in the near term, while longer-term reforms supported by the World Bank and EU take hold.

43. The gradual improvement of financial sector soundness indicators is promising, but the sector remains vulnerable. The BCSTP is pressing ahead with financial sector reforms, stepping-up supervision and making good progress in implementing the NPL reduction strategy, including the launch of the AQR with the support of the World Bank. However, continued efforts are needed to reduce the still-high level of NPLs, and vigilant supervision of vulnerable banks should be maintained.

44. Efforts by the authorities to promote the business environment and economic growth are welcome. A national export diversification strategy, developed with the support of the World Bank, is expected to be completed by mid-2018; and a private sector strategy, prepared with the help of AfDB, is being implemented. The authorities' 2017-2021 National Development Plan fulfills requirements for an economic development document under the ECF arrangement.

45. Staff recommends completion of the third and fourth reviews and the disbursement of an amount equivalent to SDR 1,268,570 under the ECF arrangement. Based on corrective measures taken, staff supports the authorities' request for waivers for nonobservance of the end-December 2016 PCs on the domestic primary balance and changes in net bank financing of the central government. Staff also supports the proposed extension of the ECF arrangement, and establishment and modification of PCs, indicative targets, and structural benchmarks for end-March, end-June and end-December 2018.

Figure 1. São Tomé and Príncipe: Recent Macroeconomic Developments



Sources: São Tomé and Príncipe authorities' data and IMF staff estimates.

Figure 2. São Tomé and Príncipe: Financial Sector Developments

The three largest banks account for 81% of total assets.

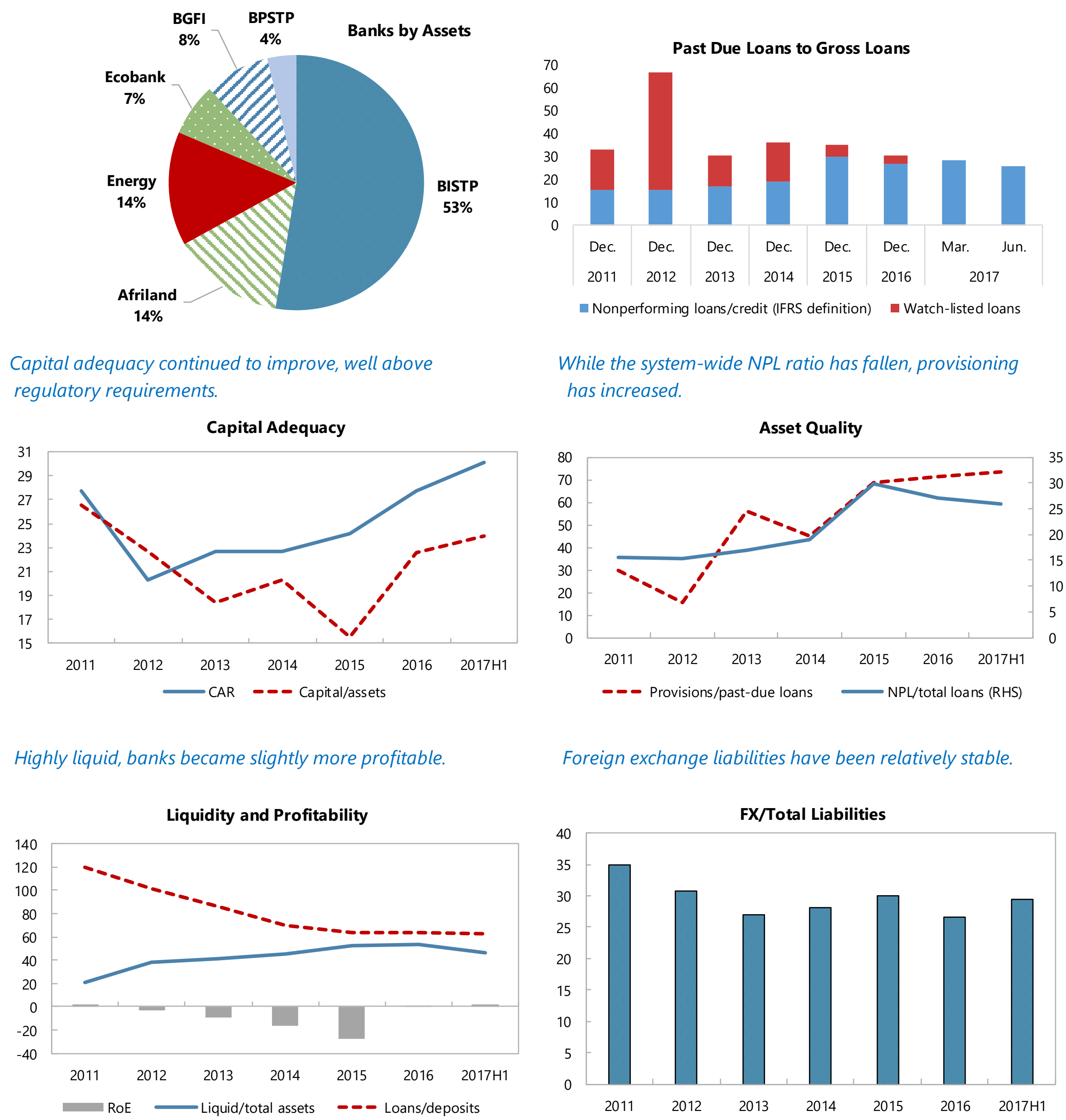
Past due loans have been slowly declining.

Capital adequacy continued to improve, well above regulatory requirements.

While the system-wide NPL ratio has fallen, provisioning has increased.

Highly liquid, banks became slightly more profitable.

Foreign exchange liabilities have been relatively stable.



Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

Table 1. São Tomé and Príncipe: Selected Economic Indicators, 2015–20

(Annual change in percent, unless otherwise indicated)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Prel.	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
National income and prices									
GDP at constant prices	4.0	4.0	4.1	5.0	4.0	5.5	5.0	5.5	5.5
GDP deflator	4.9	…	6.3	…	2.7	…	3.5	4.0	3.7
Consumer prices									
End of period	4.0	5.5	5.1	3.0	6.0	3.0	5.0	4.5	4.0
Period average	5.3	5.4	4.6	4.2	5.6	3.0	5.5	4.7	4.2
External trade									
Exports of goods and nonfactor services	1.7	7.2	7.4	10.6	2.7	6.6	7.6	7.3	6.3
Imports of goods and nonfactor services	-18.6	2.7	-0.4	11.9	8.4	8.1	5.6	6.5	5.6
Exchange rate (dobras per US$; end of period) [1]	22,424	…	23,438	…	…	…	…	…	…
Real effective exchange rate (depreciation = -)	0.7	…	6.6	…	…	…	…	…	…
Money and credit									
Base money	37.5	10.3	5.0	6.8	1.5	7.2	5.1	3.5	3.5
Broad money (M3)	13.1	11.4	-4.8	6.8	-0.2	7.2	8.7	9.7	9.4
Credit to the economy	3.8	7.1	8.3	4.8	3.4	5.2	5.8	9.2	8.9
Velocity (GDP to broad money; end of period)	2.6	2.5	3.0	2.5	3.1	2.5	3.1	3.1	3.1
Central bank reference interest rate (percent)	10.0	…	10.0	…	…	…	…	…	…
Average bank lending rate (percent)	23.3	…	19.6	…	…	…	…	…	…
Average bank deposit rate (percent)	6.9	…	4.1	…	…	…	…	…	…
Government finance (in percent of GDP)									
Total revenue, grants, and oil signature bonuses	28.0	31.1	29.4	30.1	24.6	30.3	28.3	28.2	28.4
Of which: tax revenue	14.3	13.5	12.2	15.0	13.0	15.5	13.4	13.7	13.9
Nontax revenue	1.5	2.3	2.3	1.4	1.5	1.4	1.6	1.6	1.6
Grants	11.5	14.7	14.8	13.7	10.1	13.5	13.3	12.9	12.8
Total expenditure and net lending	34.3	29.5	32.1	31.8	29.5	32.7	30.8	31.1	30.6
Personnel costs	8.9	8.7	8.8	8.5	8.5	8.4	8.3	8.2	8.1
Interest due	0.8	0.7	0.4	0.8	0.7	0.7	0.5	0.7	0.7
Nonwage noninterest current expenditure	8.5	6.6	7.9	7.9	7.0	7.6	6.8	6.8	6.8
Treasury funded capital expenditures	0.7	0.7	0.6	1.1	0.3	1.8	0.3	0.6	1.2
Donor funded capital expenditures	14.8	11.9	14.0	12.8	12.8	13.7	14.6	14.3	13.3
HIPC Initiative-related capital expenditure	0.6	0.9	0.2	0.6	0.2	0.5	0.2	0.7	0.5
Domestic primary balance [2]	-3.0	-2.0	-4.0	-1.8	-1.8	-1.5	-1.0	-1.0	-1.0
Overall balance (commitment basis)	-6.3	1.6	-2.7	-1.7	-4.9	-2.4	-2.4	-2.7	-1.8
External sector									
Current account balance (percent of GDP)									
Including official transfers	-12.6	-8.9	-6.0	-11.3	-12.2	-12.1	-7.2	-7.0	-6.2
Excluding official transfers	-25.2	-23.6	-20.8	-25.2	-22.3	-25.8	-20.5	-19.9	-19.0
PV of external debt (percent of GDP)	39.7	36.2	31.5	38.3	30.5	39.4	31.2	30.7	29.8
External debt service (percent of exports) [3]	3.8	6.8	3.4	6.0	4.7	5.6	4.7	5.5	5.2
Export of goods and non-factor services (US$ millions)	89.9	96.4	96.5	106.6	99.2	113.6	106.7	114.5	121.7
Gross international reserves [4]									
Millions of U.S. dollars	61.9	58.7	55.9	63.9	58.7	68.9	64.4	67.1	68.5
Months of imports of goods and nonfactor services [5]	4.8	4.2	4.0	4.3	4.0	4.3	4.2	4.1	3.9
National Oil Account (US$ millions)	10.3	11.5	11.5	9.3	11.7	7.6	10.6	9.0	7.6
Memorandum Item									
GDP									
Billions of dobra	7,018	7774.0	7,769	8,248	8,300	8,839	9,019	9,891	10,816
Millions of U.S. dollars	317.7	352	350.8	374.7	375.0	402.5	417.7	459.8	503.5

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] Central Bank (BCSTP) mid-point rate.

[2] Excludes oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlay.

[3] Percent of exports of goods and nonfactor services.

[4] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements, for new licensing, and for meeting capital requirements.

[5] Imports of goods and nonfactor services, excluding imports of investment goods and technical assistance.

Table 2a. São Tomé and Príncipe: Financial Operations of the Central Government, 2015–20

(Billions of Dobras)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Actual	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Total revenue and grants	1965	2422	2280	2480	2042	2680	2556	2788	3071
Total revenue	1108	1224	1130	1349	1206	1490	1359	1514	1683
Tax revenue	1006	1047	949	1237	1077	1370	1213	1354	1508
of which: import taxes	455	493	371	602	409	662	466	520	579
Other taxes	550	554	578	635	668	708	747	834	929
Nontax revenue	102	177	181	112	128	120	146	160	175
of which: oil revenue	0	66	74	0	29	0	35	38	39
Grants	804	1141	1151	1131	836	1190	1197	1274	1388
Project grants	610	781	891	801	641	859	933	1023	1118
Nonproject grants	61	212	194	181	113	183	181	156	171
HIPC Initiative-related grants	133	149	65	149	82	149	83	95	98
Total expenditure	2405	2294	2494	2621	2451	2893	2774	3081	3307
Of which: domestic primary expenditure	1315	1312	1370	1498	1329	1624	1416	1605	1790
Current expenditure	1274	1248	1334	1418	1343	1475	1411	1550	1685
Personnel costs	623	676	684	702	702	741	749	807	874
Interest due	54	56	34	66	59	59	44	66	80
Goods and services	239	234	249	253	226	271	246	269	290
Transfers	248	223	282	311	280	312	295	324	349
Other current expenditure	110	59	84	86	76	92	77	84	92
Capital expenditure	1087	978	1141	1152	1090	1369	1341	1465	1563
Financed by the Treasury	51	53	50	94	27	159	28	56	126
Financed by privatization proceeds	…	0	0	0	0	0	0	0	0
Financed by external sources	1036	926	1090	1057	1063	1210	1314	1410	1436
HIPC Initiative-related capital expenditure	44	68	19	52	19	49	21	66	59
Domestic primary balance [1]	-207	-154	-314	-148	-152	-133	-92	-100	-105
Overall fiscal balance (commitment basis)	-440	127	-214	-141	-410	-212	-218	-263	-196
Net change in arrears, float, and stat. discrepancies (reduction = -)	-65	-85	224	-86	-12	-86	-36	-86	-86
Overall fiscal balance (cash basis)	-505	43	10	-227	-422	-298	-254	-349	-282
Financing	505	-42	-10	227	422	298	254	294	170
Net external	576	34	62	229	298	283	200	299	223
Disbursements [2]	742	215	143	256	422	352	381	387	318
Scheduled amortization	-187	-181	-112	-51	-124	-69	-181	-88	-95
Net domestic	-71	-76	-72	-2	123	15	54	-4	-53
Net bank credit to the government	-71	-76	-72	-2	123	15	54	-4	-53
Banking system credit (net, excluding National Oil Account) [3]	-61	0	-45	-53	93	-26	58	-49	-90
National Oil Account	-10	-76	-27	51	30	42	-4	44	37
Nonbank financing	0	0	0	0	0	0	0	0	0
Of which: Privatization	0	0	0	0	0	0	0	0	0
Financing gap	0	0	0	0	0	0	0	-54	-112
Memorandum items:									
National Oil Account balance (US$ million, excl. transfers to budget)	10.3	11.5	11.5	9.3	11.7	7.6	10.6	9.0	7.6

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] Excludes oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlays.

[2] Includes loan from Angola in 2016 and 2017.

[3] Includes use of IMF program support.

Table 2b. São Tomé and Príncipe: Financial Operations of the Central Government, 2015–20

(Percent of GDP)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Actual	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Total revenue and grants	**28.0**	**31.1**	**29.4**	**30.1**	**24.6**	**30.3**	**28.3**	**28.2**	**28.4**
Total revenue	15.8	15.7	14.5	16.4	14.5	16.9	15.1	15.3	15.6
Tax revenue	14.3	13.5	12.2	15.0	13.0	15.5	13.4	13.7	13.9
of which: import taxes	6.5	6.3	4.8	7.3	4.9	7.5	5.2	5.3	5.4
Other taxes	7.8	7.1	7.4	7.7	8.1	8.0	8.3	8.4	8.6
Nontax revenue	1.5	2.3	2.3	1.4	1.5	1.4	1.6	1.6	1.6
of which: oil revenue	0.0	0.9	1.0	0.0	0.4	0.0	0.4	0.4	0.4
Grants	11.5	14.7	14.8	13.7	10.1	13.5	13.3	12.9	12.8
Project grants	8.7	10.0	11.5	9.7	7.7	9.7	10.3	10.3	10.3
Nonproject grants	0.9	2.7	2.5	2.2	1.4	2.1	2.0	1.6	1.6
HIPC Initiative-related grants	1.9	1.9	0.8	1.8	1.0	1.7	0.9	1.0	0.9
Total expenditure	**34.3**	**29.5**	**32.1**	**31.8**	**29.5**	**32.7**	**30.8**	**31.1**	**30.6**
Of which: Domestic primary expenditure	18.7	16.9	17.6	18.2	16.0	18.4	15.7	16.2	16.5
Current expenditure	18.1	16.1	17.2	17.2	16.2	16.7	15.6	15.7	15.6
Personnel costs	8.9	8.7	8.8	8.5	8.5	8.4	8.3	8.2	8.1
Interest due	0.8	0.7	0.4	0.8	0.7	0.7	0.5	0.7	0.7
Goods and services	3.4	3.0	3.2	3.1	2.7	3.1	2.7	2.7	2.7
Transfers	3.5	2.9	3.6	3.8	3.4	3.5	3.3	3.3	3.2
Other current expenditure	1.6	0.8	1.1	1.0	0.9	1.0	0.9	0.9	0.9
Capital expenditure	15.5	12.6	14.7	14.0	13.1	15.5	14.9	14.8	14.4
Financed by the Treasury	0.7	0.7	0.6	1.1	0.3	1.8	0.3	0.6	1.2
Financed by privatization proceeds	...	0.0	0.0	0.0	0.0	0	0.0	0.0	0.0
Financed by external sources	14.8	11.9	14.0	12.8	12.8	13.7	14.6	14.3	13.3
HIPC Initiative-related capital expenditure	0.6	0.9	0.2	0.6	0.2	0.5	0.2	0.7	0.5
Domestic primary balance [1]	-3.0	-2.0	-4.0	-1.8	-1.8	-1.5	-1.0	-1.0	-1.0
Overall fiscal balance (commitment basis)	-6.3	1.6	-2.7	-1.7	-4.9	-2.4	-2.4	-2.7	-1.8
Net change in arrears, float, and stat. discrepancies (reduction = -)	-0.9	-1.1	2.9	-1.0	-0.1	-1.0	-0.4	-0.9	-0.8
Overall fiscal balance (cash basis)	**-7.2**	**0.5**	**0.1**	**-2.8**	**-5.1**	**-3.4**	**-2.8**	**-3.5**	**-2.6**
Financing	**7.2**	**-0.5**	**-0.1**	**2.8**	**5.1**	**3.4**	**2.8**	**3.0**	**1.6**
Net external	8.2	0.4	0.8	2.8	3.6	3.2	2.2	3.0	2.1
Disbursements[2]	10.6	2.8	1.8	3.1	5.1	4.0	4.2	3.9	2.9
Program financing (loans)	0.3	0.0	0.4	0.3	0.0	0.0	0.0	0.0	0.0
Scheduled amortization	-2.7	-2.3	-1.4	-0.6	-1.5	-0.8	-2.0	-0.9	-0.9
Change in arrears (principal)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net domestic	-1.0	-1.0	-0.9	0.0	1.5	0.2	0.6	0.0	-0.5
Net bank credit to the government	-1.0	-1.0	-0.9	0.0	1.5	0.2	0.6	0.0	-0.5
Banking system credit (net, excluding National Oil Account) [3]	-0.9	0.0	-0.6	-0.6	1.1	-0.3	0.6	-0.5	-0.8
National Oil Account	-0.1	-1.0	-0.3	0.6	0.4	0.5	0.0	0.4	0.3
Nonbank financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: Privatization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.6	-1.0
Memorandum items:									
National Oil Account balance (US$ million, excl. transfers to budget)	10.3	11.5	11.5	9.3	11.7	7.6	10.6	9.0	7.6
Nominal GDP (Billions of dobra)	7,018	7,774	7,769	8,248	8,300	8,839	9,019	9,891	10,816

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] Excludes oil related revenues, grants, interest earned, scheduled interest payments, and foreign-financed capital outlays.

[2] Includes loan from Angola in 2016 and 2017.

[3] Includes use of IMF program support.

Table 3. São Tomé and Príncipe: Summary Accounts of the Central Bank, 2015–20

(Billions of Dobras)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Prel.	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Net foreign assets	**1,903**	**1,868**	**1,776**	**1,937**	**1,717**	**2,022**	**1,709**	**1,740**	**1,759**
Claims on nonresidents	2,243	2,243	2,144	2,331	2,072	2,446	2,092	2,115	2,123
Official foreign reserves	1,864	1,870	1,752	1,954	1,724	2,069	1,744	1,766	1,777
Other foreign assets	379	373	392	378	348	377	348	349	346
Liabilities to nonresidents	-341	-375	-368	-395	-355	-424	-383	-375	-365
Short-term liabilities to nonresidents	-120	-158	-144	-175	-156	-205	-185	-176	-167
Other foreign liabilities	-221	-217	-224	-220	-199	-219	-199	-199	-198
Net domestic assets	**-341**	**-146**	**-135**	**-97**	**-52**	**-46**	**41**	**70**	**115**
Net domestic credit	110	88	199	86	251	102	251	252	204
Claims on other depository corporations	128	128	198	128	198	128	198	198	198
Net claims on central government	-133	-159	-129	-165	-83	-152	-89	-93	-145
Claims on central government	247	243	386	246	323	245	481	374	271
Of which: use of SDRs/PRGF	*196*	*193*	*180*	*195*	*114*	*195*	*48*	*48*	*48*
Liabilities to central government	-380	-403	-515	-411	-406	-398	-569	-466	-417
Ordinary deposits of central government	-11	-11	-33	-64	-8	-90	-194	-125	-106
Counterpart funds	-120	-120	-82	-120	-82	-120	-82	-82	-82
Foreign currency deposits	-249	-272	-400	-227	-316	-188	-294	-260	-229
Of which: National oil account	*-230*	*-253*	*-271*	*-205*	*-252*	*-166*	*-229*	*-192*	*-163*
Claims on other sectors	115	119	131	123	136	126	142	147	152
Other items (net)	-451	-234	-335	-183	-303	-148	-210	-182	-89
Base money	**1,562**	**1,722**	**1,640**	**1,839**	**1,665**	**1,971**	**1,750**	**1,811**	**1,874**
Currency issued	315	348	309	371	302	398	300	310	321
Bank reserves	1,247	1,375	1,332	1,468	1,364	1,573	1,450	1,501	1,553
Of which : domestic currency	980	1,081	1,183	1,156	1,203	1,237	1,281	1,326	1,372
Of which: foreign currency	266	294	149	312	161	336	169	175	181
Memorandum items:									
Gross international reserves (US$ millions) [1]	61.9	58.7	55.9	63.9	58.7	68.9	64.4	67.1	68.5
Months of imports of goods and nonfactor services [2]	4.8	4.2	4.0	4.3	4.0	4.3	4.2	4.1	3.9
Net international reserves (US$ millions) [3]	56.5	51.5	49.7	55.9	51.5	59.5	55.8	58.9	60.8
Months of imports of goods and nonfactor services [2]	4.4	3.7	3.6	3.8	3.5	3.8	3.6	3.6	3.5
National Oil Account (US$ millions)	10.3	11.5	11.5	9.3	11.7	7.6	10.6	9.0	7.6
Commercial banks reserves in foreign currency (US$ millions)	11.9	13.3	6.3	14.2	7.5	15.3	7.9	8.1	8.4
Guaranteed deposits (US$ millions)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Base money (annual percent change)	37.5	10.3	5.0	6.8	1.5	7.2	5.1	3.5	3.5

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements, for new licensing, and for meeting capital requirements.

[2] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

[3] Net international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements, for new licensing, and for meeting capital requirements.

Table 4. São Tomé and Príncipe: Monetary Survey, 2015–20

(Billions of Dobras)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Prel.	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Net foreign assets	**2,527**	**2,526**	**2,106**	**2,632**	**2,001**	**2,737**	**2,012**	**2,062**	**2,083**
Net foreign assets of the BCSTP	1,903	1,868	1,776	1,937	1,717	2,022	1,709	1,740	1,759
Net foreign assets of other depository corporations	624	658	330	696	283	715	303	322	324
Net domestic assets	**301**	**624**	**586**	**732**	**686**	**868**	**908**	**1,139**	**1,418**
Net domestic credit	1,630	1,742	1,719	1,837	1,915	1,965	2,096	2,305	2,477
Net claims on central government	-323	-349	-396	-355	-272	-342	-218	-222	-275
Claims on central government	255	252	424	254	430	254	648	541	439
Liabilities to central government	-578	-601	-819	-610	-703	-596	-866	-763	-714
Budgetary deposits	-11	-11	-33	-64	-8	-90	-194	-125	-106
Counterpart funds	-120	-120	-82	-120	-82	-120	-82	-82	-82
Foreign currency deposits	-448	-471	-704	-426	-613	-386	-591	-557	-526
Of which: National Oil Account	-230	-253	-271	-205	-252	-166	-229	-192	-163
Claims on other sectors	1,953	2,092	2,115	2,193	2,187	2,308	2,314	2,527	2,751
Of which: claims in foreign currency	608	690	515	931	533	982	564	618	675
(Millions of $US)	27	31	22	42	25	45	26	29	31
Other items (net)	-1,329	-1,118	-1,134	-1,106	-1,229	-1,097	-1,189	-1,166	-1,059
Broad money (M3)	**2,828**	**3,150**	**2,691**	**3,364**	**2,687**	**3,605**	**2,919**	**3,202**	**3,501**
Local currency liabilities included in broad money (M2)	1,894	2,090	1,898	2,239	1,900	2,399	2,065	2,264	2,476
Money (M1)	1,431	1,579	1,522	1,691	1,435	1,812	1,560	1,711	1,870
Currency outside depository corporations	247	272	259	275	227	286	239	219	240
Transferable deposits in dobra	1,184	1,306	1,264	1,416	1,208	1,527	1,321	1,491	1,631
Other deposits in dobra	463	511	375	548	465	587	505	554	606
Foreign currency deposits	934	1,060	794	1,125	787	1,206	855	937	1,025
Memorandum items:									
Velocity (ratio of GDP to M3; end of period)	2.6	2.5	3.0	2.5	3.1	2.5	3.1	3.1	3.1
Money multiplier (M3/M0)	1.8	1.8	1.6	1.8	1.6	1.8	1.7	1.8	1.9
Base money (12-month growth rate)	37.5	10.3	5.0	6.8	1.5	7.2	5.1	3.5	3.5
Claims on other resident sectors (12-month growth rate)	3.8	7.1	8.3	4.8	3.4	5.2	5.8	9.2	8.9
M3 (12-month growth rate)	13.1	11.4	-4.8	6.8	-0.2	7.2	8.7	9.7	9.4
Eurorization ratio	35.9	36.8	32.3	36.4	29.8	36.3	30.2	30.3	30.7

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

Table 5. São Tomé and Príncipe: Financial Soundness Indicators, 2011–June 2017

	2011	2012	2013	2014	2015	2016	2017	
	Dec.	Dec.	Dec.	Dec.	Dec.	Dec.[1]	Mar.	Jun.
Capital Adequacy								
Regulatory capital to risk-weighted assets	27.7	20.3	22.7	22.6	24.1	27.8	34.4	30.1
Percentage of banks (out of total number) with regulatory capital to risk-weighted assets								
... greater or equal to 10 percent	100.0	87.5	75.0	75.0	85.7	100.0	100.0	100.0
... between 6 and 10 percent	0.0	0.0	12.5	0.0	0.0	0.0	0.0	0.0
... below 6 percent minimum	0.0	12.5	12.5	25.0	14.3	0.0	0.0	0.0
Capital (net worth) to assets	26.5	22.7	18.4	20.3	15.5	22.5	24.5	23.9
Deposits with banks below 6 percent capital to assets								
... (in billions of dobras)	0.0	83.2	59.0	325.1	455.3	0.0	0.0	0.0
... (percent of deposits)	0.0	4.6	2.9	13.7	17.5	0.0	0.0	0.0
... (percent of GDP)	0.0	1.7	1.1	5.1	6.5	0.0	0.0	0.0
Asset quality								
Foreign exchange loans to total loans	68.5	57.9	53.9	46.5	42.1	27.5	28.1	25.5
Past-due loans to gross loans	33.2	66.7	30.4	36.2	35.0	30.7	32.5	30.6
Nonperforming loans/credit (IFRS definition)	15.6	15.4	16.9	19.1	29.8	27.0	28.3	26.0
Watch-listed loans	17.5	51.3	13.6	17.2	5.2	3.7	4.2	4.6
Provision as percent of past-due loans	30.0	15.4	56.3	45.1	68.7	71.2	73.8	73.3
Earnings and profitability								
Return on assets	0.5	-0.8	-2.1	-3.2	-5.2	0.0	0.3	0.4
Return on equity	1.5	-3.3	-9.3	-15.9	-27.1	0.2	1.3	1.9
Expense (w/ amortization & provisions)/income	119.3	117.8	471.1	164.5	215.9	108.6	92.2	97.3
Liquidity								
Liquid assets/total assets	20.4	37.8	40.8	45.8	52.0	54.0	49.5	46.2
Liquid assets/short term liabilities	36.7	61.5	39.6	72.7	72.5	84.6	70.4	67.6
Loan/total liabilities	83.0	64.7	56.3	47.3	47.1	47.0	50.8	53.8
Foreign exchange liabilities/total liabilities	35.0	30.8	27.0	28.1	30.0	26.6	29.4	29.4
Loan/deposits	119.5	101.7	85.8	69.6	63.5	63.5	60.6	62.9
Sensitivity to market risk								
Foreign exchange liabilities to shareholders funds	97.0	105.0	119.3	110.3	162.8	91.5	90.7	93.5

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates.

Note: Beginning June 2013, data are based on improved methodology and not strictly comparable with earlier data.

[1] Excluding Banco Equador (whose banking licence was withdrawn in August 2016).

Table 6a. São Tomé and Príncipe: Balance of Payments, 2015–20

(Millions of U.S. Dollars)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Est.	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Trade balance	**-107.6**	**-98.1**	**-105.5**	**-113.1**	**-115.1**	**-123.7**	**-127.1**	**-136.0**	**-145.1**
Exports, f.o.b.	11.3	14.2	13.6	16.1	11.6	16.9	13.3	14.9	15.4
Cocoa	7.9	11.0	8.6	12.0	6.4	13.0	8.3	9.0	9.3
Re-export	2.2	2.0	3.2	2.9	3.7	2.6	3.5	4.3	4.4
Imports, f.o.b.	-118.9	-112.3	-119.1	-129.2	-126.7	-140.6	-140.4	-151.0	-160.5
Of which : food	-34.3	-32.2	-36.1	-34.0	-38.9	-35.5	-40.6	-42.5	-43.6
Petroleum products	-31.3	-22.1	-21.7	-26.1	-29.1	-28.1	-30.5	-33.4	-35.6
Investment goods	-27.9	-30.0	-31.2	-40.7	-28.0	-48.0	-36.9	-39.4	-42.3
Oil sector related investment goods	0.0	-2.1	0.0	-2.1	0.0	-2.1	0.0	0.0	0.0
Services and income (net)	**9.5**	**1.0**	**16.7**	**3.6**	**14.5**	**3.9**	**22.9**	**25.8**	**29.4**
Exports of nonfactor services	78.6	82.1	82.9	90.4	87.6	96.7	93.4	99.5	106.2
Of which : travel and tourism	62.2	70.0	69.2	77.7	73.7	83.3	78.7	84.0	89.8
Imports of nonfactor services	-68.1	-79.7	-67.2	-85.7	-75.3	-91.7	-72.8	-76.1	-79.3
Factor services (net)	-1.0	-1.4	1.0	-1.2	2.2	-1.2	2.3	2.4	2.5
Of which: oil related	0.0	0.0	0.0	0.1	0.2	0.1	0.1	0.1	0.1
Private transfers (net)	**18.1**	**14.1**	**15.9**	**15.0**	**17.0**	**16.0**	**18.5**	**18.8**	**19.8**
Official transfers (net)	**40.0**	**51.6**	**51.9**	**52.4**	**37.8**	**55.2**	**55.4**	**59.2**	**64.6**
Of which : project grants	27.6	42.0	40.2	43.2	29.0	45.9	43.2	47.5	52.1
HIPC Initiative-related grants	6.0	6.7	2.9	6.8	3.7	6.8	3.8	4.4	4.6
Current account balance									
Including official transfers	-40.0	-31.4	-20.9	-42.2	-45.8	-48.6	-30.3	-32.2	-31.3
Excluding official transfers	-80.0	-82.9	-72.9	-94.5	-83.6	-103.8	-85.7	-91.5	-95.8
Capital and financial account balance	**43.9**	**30.4**	**-2.3**	**45.0**	**44.7**	**52.7**	**33.1**	**28.8**	**25.2**
Financial account	43.9	30.4	-2.3	45.0	44.7	52.7	33.1	28.8	25.2
Direct foreign investment	25.8	23.4	20.7	17.5	42.9	24.0	11.2	12.4	13.7
Of which: Oil signature bonuses	2.4	2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Petroleum related investment	24.2	15.0	19.3	3.2	43.6	3.2	0.0	0.0	0.0
Recovery of oil capital expense	-24.2	-15.0	-19.3	-3.2	-43.6	-3.2	0.0	0.0	0.0
Portfolio Investment (net)	0.3	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	17.9	7.1	-23.2	27.5	1.8	28.7	21.9	16.4	11.4
Assets	9.5	-12.0	-10.9	0.0	0.0	0.0	0.0	0.0	0.0
Public sector (net)	32.1	10.1	6.2	8.2	15.2	11.2	13.7	13.9	10.4
Project loans	33.6	14.7	6.4	11.6	19.1	16.0	17.6	17.6	14.5
Program loans	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0	0.0
Amortization	-1.4	-3.3	-1.2	-3.3	-2.4	-3.6	-2.6	-4.1	-4.4
Other investment	-0.1	-1.2	1.0	-1.1	-1.6	-1.2	-1.4	0.3	0.3
Of which : transfers to JDA	-0.2	-0.5	-0.4	-0.5	-0.2	-0.5	-0.4	-0.4	-0.4
Private sector (net)	-23.7	8.9	-18.6	19.3	-13.4	17.5	8.2	2.5	1.1
Commercial banks	-9.7	2.0	-13.8	1.8	-0.9	0.5	1.4	1.0	0.1
Short-term private capital	-14.0	6.9	-4.8	17.4	-12.4	17.0	6.8	1.5	1.0
Errors and omissions	**14.6**	**0.0**	**18.7**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**18.5**	**-0.9**	**-4.6**	**2.9**	**-1.1**	**4.2**	**2.8**	**-3.4**	**-6.1**
Financing	-18.5	0.9	4.6	-2.8	1.1	-4.2	-2.8	-1.9	-0.9
Change in official reserves, excl. NOA (increase= -)	-18.2	1.1	4.9	-6.1	-0.3	-7.2	-5.2	-3.2	-2.0
Use of Fund resources (net)	0.0	1.0	0.9	1.1	1.6	1.2	1.4	-0.3	-0.3
Purchases	0.9	1.8	1.8	1.8	1.8	1.8	1.8	0.0	0.0
Repurchases (incl. MDRI repayment)	-0.9	-0.7	-0.9	-0.6	-0.2	-0.5	-0.4	-0.3	-0.3
National Oil Account (increase = -)	-0.4	-1.2	-1.3	2.2	-0.2	1.8	1.1	1.7	1.4
Financing Gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	5.3	7.0
Memorandum items:									
Current account balance (percent of GDP)									
Before official transfers	-25.2	-23.6	-20.8	-25.2	-22.3	-25.8	-20.5	-19.9	-19.0
After official transfers	-12.6	-8.9	-6.0	-11.3	-12.2	-12.1	-7.2	-7.0	-6.2
Debt service ratio (percent of exports) [1]	3.8	6.8	3.4	6.0	4.7	5.6	4.7	5.5	5.2
Gross international reserves [2]									
Millions of U.S. dollars	61.9	58.7	55.9	63.9	58.7	68.9	64.4	67.1	68.5
Months of imports of goods and nonfactor services [3]	4.8	4.2	4.0	4.3	4.0	4.3	4.2	4.1	3.9

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] Percent of exports of goods and nonfactor services.

[2] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements, for new licensing, and for meeting capital requirements.

[3] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

Table 6b. São Tomé and Príncipe: Balance of Payments, 2015–20

(Percent of GDP)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Prel.	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Trade balance	**-33.9**	**-27.9**	**-30.1**	**-30.2**	**-30.7**	**-30.7**	**-30.4**	**-29.6**	**-28.8**
Exports, f.o.b.	3.6	4.1	3.9	4.3	3.1	4.2	3.2	3.2	3.1
Cocoa	2.5	3.1	2.5	3.2	1.7	3.2	2.0	1.9	1.9
Re-export	0.7	0.6	0.9	0.8	1.0	0.6	0.8	0.9	0.9
Imports, f.o.b.	-37.4	-32.0	-34.0	-34.5	-33.8	-34.9	-33.6	-32.8	-31.9
Of which : food	-10.8	-9.2	-10.3	-9.1	-10.4	-8.8	-9.7	-9.2	-8.7
Petroleum products	-9.8	-6.3	-6.2	-7.0	-7.8	-7.0	-7.3	-7.3	-7.1
Investment goods	-8.8	-8.5	-8.9	-10.9	-7.5	-11.9	-8.8	-8.6	-8.4
Oil sector related investment goods	0.0	-0.6	0.0	-0.6	0.0	-0.5	0.0	0.0	0.0
Services and income (net)	**3.0**	**0.3**	**4.8**	**1.0**	**3.9**	**1.0**	**5.5**	**5.6**	**5.8**
Exports of nonfactor services	24.7	23.4	23.6	24.1	23.4	24.0	22.3	21.6	21.1
Of which : travel and tourism	19.6	19.9	19.7	20.7	19.7	20.7	18.8	18.3	17.8
Imports of nonfactor services	-21.4	-22.7	-19.1	-22.9	-20.1	-22.8	-17.4	-16.5	-15.8
Factor services (net)	-0.3	-0.4	0.3	-0.3	0.6	-0.3	0.5	0.5	0.5
Of which: oil related	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private transfers (net)	**5.7**	**4.0**	**4.5**	**4.0**	**4.5**	**4.0**	**4.4**	**4.1**	**3.9**
Official transfers (net)	**12.6**	**14.7**	**14.8**	**14.0**	**10.1**	**13.7**	**13.3**	**12.9**	**12.8**
Of which : project grants	8.7	12.0	11.5	11.5	7.7	11.4	10.3	10.3	10.3
HIPC Initiative-related grants	1.9	1.9	0.8	1.8	1.0	1.7	0.9	1.0	0.9
Current account balance									
Including official transfers	-12.6	-8.9	-6.0	-11.3	-12.2	-12.1	-7.2	-7.0	-6.2
Excluding official transfers	-25.2	-23.6	-20.8	-25.2	-22.3	-25.8	-20.5	-19.9	-19.0
Capital and financial account balance	**13.8**	**8.7**	**-0.7**	**12.0**	**11.9**	**13.1**	**7.9**	**6.3**	**5.0**
Financial account	13.8	8.7	-0.7	12.0	11.9	13.1	7.9	6.3	5.0
Direct foreign investment	8.1	6.6	5.9	4.7	11.4	6.0	2.7	2.7	2.7
Of which: Oil signature bonuses	0.8	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Petroleum related investment	7.6	4.3	5.5	0.9	11.6	0.8	0.0	0.0	0.0
Recovery of oil capital expense	-7.6	-4.3	-5.5	-0.9	-11.6	-0.8	0.0	0.0	0.0
Portfolio Investment (net)	0.1	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	5.6	2.0	-6.6	7.3	0.5	7.1	5.2	3.6	2.3
Assets	3.0	-3.4	-3.1	0.0	0.0	0.0	0.0	0.0	0.0
Public sector (net)	10.1	2.9	1.8	2.2	4.0	2.8	3.3	3.0	2.1
Project loans	10.6	4.2	1.8	3.1	5.1	4.0	4.2	3.8	2.9
Program loans	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0	0.0
Amortization	-0.4	-0.9	-0.3	-0.9	-0.6	-0.9	-0.6	-0.9	-0.9
Other investment	0.0	-0.3	0.3	-0.3	-0.4	-0.3	-0.3	0.1	0.1
Of which : transfers to JDA	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Private sector (net)	-7.5	2.5	-5.3	5.1	-3.6	4.3	2.0	0.5	0.2
Commercial banks	-3.1	0.6	-3.9	0.5	-0.3	0.1	0.3	0.2	0.0
Short-term private capital	-4.4	2.0	-1.4	4.7	-3.3	4.2	1.6	0.3	0.2
Errors and omissions	**4.6**	**0.0**	**5.3**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**5.8**	**-0.3**	**-1.3**	**0.8**	**-0.3**	**1.0**	**0.7**	**-0.8**	**-1.2**
Financing	-5.8	0.3	1.3	-0.8	0.3	-1.0	-0.7	-0.4	-0.2
Change in official reserves, excl. NOA (increase= -)	-5.7	0.3	1.4	-1.6	-0.1	-1.8	-1.3	-0.7	-0.4
Use of Fund resources (net)	0.0	0.3	0.3	0.3	0.4	0.3	0.3	-0.1	-0.1
Purchases	0.3	0.5	0.5	0.5	0.5	0.4	0.4	0.0	0.0
Repurchases (incl. MDRI repayment)	-0.3	-0.2	-0.3	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1
National Oil Account (increase = -)	-0.1	-0.3	-0.4	0.6	0.0	0.4	0.3	0.4	0.3
Financing Gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.2	1.4
Memorandum items:									
Debt service ratio (percent of exports) [1]	3.8	6.8	3.4	6.0	4.7	5.6	4.7	5.5	5.2
Gross international reserves [2]									
Millions of U.S. dollars	61.9	58.7	55.9	63.9	58.7	68.9	64.4	67.1	68.5
Months of imports of goods and nonfactor services [3]	4.8	4.2	4.0	4.3	4.0	4.3	4.2	4.1	3.9

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] Percent of exports of goods and nonfactor services.

[2] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements, for new licensing, and for meeting capital requirements.

[3] Imports of goods and nonfactor services excluding imports of investment goods and technical assistance.

Table 7. São Tomé and Príncipe: External Financing Requirements and Sources, 2015–20
(Millions of U.S. Dollars)

	2015	2016		2017		2018		2019	2020
		EBS/16/114		EBS/16/114		EBS/16/114			
	Actual	2nd Rev	Prel.	2nd Rev	Proj.	2nd Rev	Proj.	Proj.	Proj.
Gross financing requirements	**-100.6**	**-87.1**	**-69.0**	**-105.8**	**-87.9**	**-116.3**	**-95.3**	**-98.8**	**-102.2**
Current account, excluding official transfers	-80.0	-82.9	-72.9	-94.5	-83.6	-103.8	-85.7	-91.5	-95.8
Exports, f.o.b.	11.3	14.2	13.6	16.1	11.6	16.9	13.3	14.9	15.4
Imports, f.o.b.	-118.9	-112.3	-119.1	-129.2	-126.7	-140.6	-140.4	-151.0	-160.5
Services and income (net)	9.5	1.0	16.7	3.6	14.5	3.9	22.9	25.8	29.4
Private transfers	18.1	14.1	15.9	15.0	17.0	16.0	18.5	18.8	19.8
Financial account	-2.4	-5.3	-1.1	-5.1	-4.1	-5.3	-4.3	-4.1	-4.4
Scheduled amortization	-1.4	-3.3	-1.2	-3.3	-2.4	-3.6	-2.6	-4.1	-4.4
IMF repayments	-0.9	-0.7	-0.9	-0.6	-0.2	-0.5	-0.4	-0.3	-0.3
Other public sector flows (net)	-0.1	-1.2	1.0	-1.1	-1.6	-1.2	-1.4	0.3	0.3
Change in external reserves (-ve = increase)	-18.2	1.1	4.9	-6.1	-0.3	-7.2	-5.2	-3.2	-2.0
Available funding	**100.6**	**87.0**	**69.0**	**105.8**	**87.9**	**116.2**	**95.3**	**98.8**	**102.2**
National Oil Fund (net)	2.0	1.3	-1.3	2.2	-0.2	1.8	1.1	1.7	1.4
Oil signature bonuses	2.4	2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Saving (-ve = accumulation of oil reserve fund)	-0.4	-1.2	-1.3	2.2	-0.2	1.8	1.1	1.7	1.4
Expected disbursements	73.6	66.3	58.4	65.1	56.8	71.2	73.1	76.9	79.1
Multilateral HIPC interim assistance	6.0	6.7	2.9	6.8	3.7	6.8	3.8	4.4	4.6
Grants	34.0	44.9	49.0	45.6	34.0	48.4	51.6	54.8	60.0
Concessional loans	33.6	14.7	6.4	12.7	19.1	16.0	17.6	17.6	14.5
Project loans	33.6	14.7	6.4	11.6	19.1	16.0	17.6	17.6	14.5
Program loans	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0	0.0
Private sector (net)	24.1	17.7	10.1	36.8	29.5	41.5	19.4	14.9	14.8
IMF	0.9	1.8	1.8	1.8	1.8	1.8	1.8	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	5.3	7.0
Exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Residual financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	5.3	7.0

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

Table 8a. São Tomé and Príncipe: Current Schedule of Disbursements under the ECF Arrangement, 2015–18

Date[1]	Disbursement conditions	SDR Amount	Percent of Quota
07/13/15	Board approval of arrangement.	634,285	4.29
06/10/16	Observance of continuous and end-December 2015 PCs and completion of the first review.	634,285	4.29
12/09/16	Observance of continuous and end-June 2016 PCs and completion of the second review.	634,285	4.29
04/15/17	Observance of continuous and end-December 2016 PCs and completion of the third review.	634,285	4.29
10/15/17	Observance of continuous and end-June 2017 PCs and completion of the fourth review.	634,285	4.29
04/15/18	Observance of continuous and end-December 2017 PCs and completion of the fifth review	634,285	4.29
06/15/18	Observance of continuous and end-March 2018 PCs and completion of the sixth review.	634,290	4.29
	Total	4,440,000	30

Source: International Monetary Fund.

[1] Board date, in the case of completed reviews.

Table 8b. São Tomé and Príncipe: Proposed Schedule of Disbursements under the ECF Arrangement, 2015–18

Date[1]	Disbursement conditions	SDR Amount	Percent of Quota
07/13/15	Board approval of arrangement.	634,285	4.29
06/10/16	Observance of continuous and end-December 2015 PCs and completion of the first review.	634,285	4.29
12/09/16	Observance of continuous and end-June 2016 PCs and completion of the second review.	634,285	4.29
04/15/17	Observance of continuous and end-December 2016 PCs and completion of the third review.	634,285	4.29
10/15/17	Observance of continuous and end-June 2017 PCs and completion of the fourth review.	634,285	4.29
04/15/18	Observance of continuous and end-December 2017 PCs and completion of the fifth review	634,285	4.29
10/15/18	Observance of continuous and end-June 2018 PCs and completion of the sixth review.	634,290	4.29
	Total	4,440,000	30

Source: International Monetary Fund.

[1] Board date, in the case of completed reviews.

Table 9. São Tomé and Príncipe: Indicators of Capacity to Repay the Fund, 2017–30

						Projections								
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Fund obligations based on existing credit (millions of SDRs)														
Principal	0.00	0.39	0.33	0.26	0.41	0.60	0.49	0.38	0.38	0.19	0.00	0.00	0.00	0.00
Charges and interest	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04
Fund obligations based on existing and prospective credit (millions of SDRs)														
Principal	0.00	0.39	0.33	0.26	0.41	0.60	0.81	0.89	0.89	0.70	0.51	0.19	0.00	0.00
Charges and interest	0.01	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04	0.04
Total obligations based on existing and prospective credit														
Millions of SDRs	0.01	0.43	0.37	0.30	0.45	0.64	0.85	0.93	0.93	0.74	0.55	0.23	0.04	0.04
Millions of U.S. dollars	0.01	0.61	0.52	0.42	0.63	0.90	1.20	1.31	1.31	1.04	0.77	0.00	0.00	0.00
Percent of exports of goods and services	0.01	0.57	0.46	0.35	0.49	0.64	0.80	0.82	0.77	0.57	0.40	0.00	0.00	0.00
Percent of debt service [1]	0.31	12.55	8.32	6.53	9.63	12.86	17.50	13.56	14.11	11.58	8.79	0.00	0.00	0.00
Percent of quota	0.07	2.91	2.50	2.03	3.04	4.32	5.74	6.28	6.28	5.00	3.72	1.55	0.27	0.27
Percent of gross international reserves [2]	0.02	0.94	0.78	0.62	0.91	1.27	1.63	1.72	1.68	1.31	0.96	0.00	0.00	0.00
Outstanding Fund credit														
Millions of SDRs	4.7	5.6	5.3	5.0	4.6	4.0	3.2	2.3	1.4	0.7	0.2	0.0	0.0	0.0
Millions of U.S. dollars	6.5	7.9	7.4	7.1	6.5	5.6	4.5	3.2	2.0	1.0	0.3	0.0	0.0	0.0
Percent of exports of goods and services	6.6	7.4	6.5	5.8	5.0	4.0	3.0	2.0	1.2	0.5	0.1	0.0	0.0	0.0
Percent of debt service [1]	146.6	163.2	118.1	108.9	98.1	80.0	65.3	33.2	21.2	11.0	3.0	0.0	0.0	0.0
Percent of quota	31.8	37.8	35.5	33.8	30.9	26.9	21.4	15.4	9.5	4.7	1.3	0.0	0.0	0.0
Percent of gross international reserves [2]	11.1	12.2	11.0	10.3	9.3	7.9	6.1	4.2	2.5	1.2	0.3	0.0	0.0	0.0
Memorandum items:														
Exports of goods and services (millions of U.S. dollars)	99.2	106.7	114.5	121.7	129.6	140.4	149.8	159.7	170.4	181.8	193.9	206.9	220.7	235.5
Debt service (millions of U.S. dollars)	4.4	4.8	6.3	6.5	6.6	7.0	6.8	9.7	9.3	9.0	8.8	8.6	8.5	8.9
Quota (millions of SDRs)	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8	14.8
Gross international reserves [2]	58.7	64.4	67.1	68.5	69.5	70.8	73.7	76.4	78.0	79.6	81.0	82.3	83.5	84.6
GDP (millions of U.S. dollars)	375	418	460	503	566	609	654	701	752	806	865	928	995	1067

Sources: São Tomé and Príncipe authorities' data and IMF staff estimates and projections.

[1] After HIPC and MDRI debt relief. Including IMF repurchases and repayments in total debt service.

[2] Gross international reserves exclude the National Oil Account and commercial banks' foreign currency deposits at the BCSTP in order to meet reserve requirements, for new licensing, and for meeting capital requirements.

Table 10. São Tomé & Príncipe: Millennium Development Goals

	1990	1995	2000	2005	2010	2012
Goal 1: Eradicate extreme poverty and hunger						
1.1 Poverty headcount ratio at $1.25 a day (PPP) (% of population)	--	--	28.18[5/]	--	--	--
1.1 Poverty headcount ratio at national povertyline, total (%)	--	--	53.8[5/]	--	66.2[10/]	--
1.2 Poverty gap at $1.25 a day (PPP) (%)	--	--	7.87[5/]	--	--	--
1.3 Income share held by lowest 20%	--	--	5.23[5/]	--	--	--
1.5 Vulnerable employment, total (% of total employment)	27[1/]	--	--	--	--	--
1.5 Unemployment rate, total	--	--	14.4	--	16.7[8/]	13.9
1.8 Malnutrition prevalence, weight for age (% of children under 5)	--	--	3.0	--	4.3[9/]	--
1.9 Prevalence of undernourishment (% of population)	22.6[2/]	24.4	14.8	8.9	7.5[9/]	7.7[11/]
1.9 Depth of hunger (kilocalories per person per day)	190[2/]	190[3/]	170[6/]	--	160[8/]	--
Goal 2: Achieve universal primary education						
2.1 Total enrollment, primary (% net)	97	--	98.30[6/]	99.35	98.64	99.56
2.1 Persistence to last grade of primary, total (% of cohort)	65	--	58.83[5/]	68.91[7/]	68.03[9/]	--
2.2 Primary completion rate, total (% of relevant age group)	79	--	61.58[6/]	74.34	85.31	99.14
2.3 Literacy rate, youth female (% of females ages 15-24)	92[1/]	--	94.85[5/]	--	95.94	--
2.3 Literacy rate, youth male (% of males ages 15-24)	96[1/]	--	95.97[5/]	--	94.72	--
Goal 3: Promote gender equality and empower women						
3.1 Ratio of female to male primary enrollment (%)	92	--	97[4/]	97	100	97
3.1 Ratio of female to male secondary enrollment (%)	--	--	--	107	103	113
3.1 Ratio of female to male tertiary enrollment (%)	--	--	--	--	98	--
3.2 Proportion of seats held by women in national parliaments (%)	12	7[3/]	9	9	18	18
3.3 Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	32[1/]	--	--	--	--	--
Goal 4: Reduce child mortality						
4.1 Mortality rate, under-5 (per 1,000)	96	94	93	91	89	89[11/]
4.2 Mortality rate, infant (per 1,000 live births)	62	61	60	59	58	58[11/]
4.3 Immunization, measles (% of children ages 12-23 months)	71	74	69	88	92	91[11/]
Goal 5: Improve maternal health						
5.1 Maternal mortality ratio (modeled estimate, per 100,000 live births)	150	120	110	87	70	--
5.2 Births attended by skilled health staff (% of total)	--	--	79	--	82[10/]	--
5.3 Contraceptive prevalence (% of women ages 15-49)	--	--	29	--	38[10/]	--
5.4 Adolescent fertility rate (births per 1,000 women ages 15-19)	--	94[3/]	86	72	60	55
5.5 Pregnant women receiving prenatal care (%)	--	--	91	--	98[10/]	--
5.6 Unmet need for contraception (% of married women, ages 15-49)	--	--	--	--	37[10/]	--
Goal 6: Combat HIV/AIDS, Malaria and other diseases						
6.1 Prevalence of HIV, total (% of population ages 15-49)	0.2	0.5	0.8	1.2	1.0	1.0[11/]
6.1 Prevalence of HIV, female (% ages 15-24)	--	--	--	--	--	0.3[11/]
6.1 Prevalence of HIV, male (% ages 15-24)	--	--	--	--	--	0.4[11/]
6.2 Condom use, population ages 15-24, female (% of females ages 15-24)	--	--	--	--	54[10/]	--
6.2 Condom use, population ages 15-24, male (% of males ages 15-24)	--	--	--	--	64[10/]	--
6.7 Use of insecticide-treated bed nets (% of under-5 population)	--	--	23	--	56[10/]	--
6.8 Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	--	--	61	--	8[10/]	--
6.9 Incidence of tuberculosis (per 100,000 people)	135	124	114	105	96	94[11/]
6.10 Tuberculosis case detection rate (all forms)	11	--	60	85	76	86[11/]
Goal 7: Ensure environmental sustainability						
7.1 Forest area (% of land area)	28	--	28	28	28	--
7.2 CO2 emissions (kg per PPP $ of GDP)			.54[5/]	0.59	0.41[9/]	--
7.2 CO2 emissions (metric tons per capita)	0.57	0.60	0.62	0.84	0.79[9/]	--
7.8 Improved water source (% of population with access)	--	75	79	85	89	--
7.9 Improved sanitation facilities (% of population with access)	--	20	21	24	26	--
Goal 8: Develop a global partnership for development						
8.1 Net ODA received per capita (current US$)	466	657	247	213	298	--
8.12 Debt service (PPG and IMF only, % of exports, excluding workers' remittances)	29	27[3/]	22	61	7	--
8.14 Telephone lines (per 100 people)	1.9	2.0	3.3	4.7	4.7	4.7[11/]
8.15 Mobile cellular subscriptions (per 100 people)	--	--	--	8	62	71
8.16 Internet users (per 100 people)	--	--	5	14	19	22
Other						
Fertility rate, total (births per woman)	5.4	5.0	4.6	4.1	3.7	3.5
GNI per capita, Atlas method (current US$)	--	--	--	750	1240	1350[11/]
GNI, Atlas method (current US$, millions)	--	--	--	114	205	227[11/]
Life expectancy at birth, total (years)	61	62	62	63	64	65
Literacy rate, adult total (% of people ages 15 and above)	73[1/]	--	84[5/]	--	89[10/]	--
Literacy rate, youth total (% of people ages 15-24)	94[1/]	--	95[5/]	--	95[10/]	--
Population, total (thousands)	116	128	141	153	165	169[11/]
Trade (% of GDP)	--	--	79	67	76	69[11/]

Source: World Bank Development Indicators.

1/ Correspond to 1991 2/ Correspond to 1992 3/ Correspond to 1997 4/ Correspond to 1999 5/ Correspond to 2001 6/ Correspond to 2002

7/ Correspond to 2004 8/ Correspond to 2007 9/ Correspond to 2008 10/ Correspond to 2009 11/ Correspond to 2011

Appendix I. Letter of Intent

São Tomé, November 16, 2017

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

Dear Ms. Lagarde:

The attached Memorandum of Economic and Financial Policies (MEFP) reviews recent economic developments and performance under the Extended Credit Facility (ECF) arrangement. It also updates the government's policies and objectives for the rest of 2017 and 2018. These policies are anchored by the government's medium-term development program, outlined in the National Development Plan (NDP) 2017-2021—our economic development document and the successor of our Second National Poverty Reduction Strategy Paper (PRSP-II, 2012-2016).

The government continues to make good progress towards achieving macroeconomic stability, fostering sustainable and inclusive growth, and reducing poverty. Macroeconomic stability has improved as evidenced by stable growth and lower inflation. The medium-term outlook is broadly positive, with real GDP growth projected to reach 5½ percent supported by robust activity in the construction, agricultural, and tourism sectors.

Despite our best efforts, significant challenges remain and continued Fund support will be needed. In particular, high debt levels, shortfall in external financing, large infrastructural needs, risks in the banking system, and weak competitiveness have undermined our economic development efforts. In addition, limited capacity constrains the pace of structural reforms, which could, in turn, delay much needed external financial support. Against the background of the current challenges, the government remains grateful to the IMF for financial support through the ECF, and hopes the program will catalyze financial support of other partners.

As documented in the attached MEFP, we have met all end-June 2017 performance criteria under the program after missing the fiscal targets at end-2016. The government missed the end-December 2016 performance criteria (PCs) on domestic primary balance and net bank financing of the central government. However, corrective measures adopted in late 2016 and in the revised 2017 budget have enabled the government to achieve the end-June 2017 targets. Moreover, the government took additional spending measures in September to ensure the achievement of the end-December 2017 targets. Our structural reform agenda is on course, albeit at a much slower pace than anticipated mainly due to capacity constraints and delays in technical assistance delivery.

Our economic and financial policies for 2017-18, as outlined in the MEFP, are anchored in the government's medium-term development program—the NDP. The main priorities for 2017/18 will be to consolidate macroeconomic stability, remove structural impediments to higher, sustained, and inclusive growth, and strengthen the financial sector. In macroeconomic policy, as indicated above, the government will implement measures to address the fiscal slippage in 2016. In addition, we have taken steps to reduce large losses of a state-owned enterprise, are implementing measures to avoid arrears accumulation and repay past arrears, and are doubling our effort to complete the liquidation of Banco Equador to safeguard financial stability and minimize fiscal cost. We will continue to undertake ambitious structural fiscal reforms aimed at supporting the fiscal consolidation and unleashing growth potential while attracting additional donor financing.

Based on the performance in implementing the economic program and on the strength of our future policy commitments, particularly the achievement of all end-June 2017 PCs and measures taken to meet end-2017 targets, the government requests that the third and fourth reviews under the ECF arrangement be completed and a disbursement in the amount of SDR 1.3 million be approved. In completing the review, the government is requesting: (i) waivers for the missed end-December 2016 PCs on domestic primary balance and net bank financing of the central government; (ii) modification of the PCs on net international reserves for end-December 2017; (iii) modification of the PC on external arrears from stock to flow to clarify that the PC captures the accumulation of new external arrears; (iv) further clarifications included in the TMU; (v) extension of the program to end-December 2018; and (vi) rephasing the end-March 2018 test date and targets to end-June 2018 with updates.

The implementation of the ECF-supported program will continue to be monitored by quantitative performance criteria and structural benchmarks, and semi-annual reviews. Definitions of key concepts and indicators, as well as reporting requirements, are set out in the accompanying updated Technical Memorandum of Understanding (TMU). The government expects the fifth review to be completed by mid-June 2018 based on end-December 2017 and other relevant performance criteria.

The government believes that measures and policies described in the July 2015 MEFP and its subsequent supplements, together with the attached supplementary MEFP, provide an adequate basis for attaining the economic policy objectives of the government. However, the government stands ready to take any additional measures that may be required to meet our program objectives, including addressing the shortfall in external financing. We will consult with the IMF, in advance, on the adoption of these measures and on any revisions to the policies contained in this supplementary MEFP, in accordance with the Fund policies on such consultation. We will hold timely discussions with the IMF staff on the terms of large external borrowing to ensure that such borrowing meets the concessionality requirement under the program, does not jeopardize debt sustainability, and is in line with the Fund's debt limit policy.

The government will also provide the IMF staff with all the relevant information required to complete program reviews and monitor performance on a timely manner as outlined in the TMU. During the program period, the government will not introduce or strengthen any exchange controls and multiple currency practices, or import restrictions for balance of payments purposes, nor conclude any bilateral payment agreements in violation of Article VIII of the Fund's Articles of Agreement.

The government agrees to make public this Letter of Intent, along with the attached supplementary MEFP and TMU, and the entire IMF staff report on the combined third and fourth reviews. We hereby authorize their publication and posting on the IMF website, once the IMF Executive Board approves the completion of the combined third and fourth reviews under the three-year ECF arrangement.

Sincerely yours,

/s/
Mr. Américo d'Oliveira Ramos,

Minister of Finance, Commerce and the Blue Economy

/s/
Mr. Hélio Silva Almeida,

Governor of the Central Bank of São Tomé and Príncipe

Attachments:

I. Memorandum of Economic and Financial Policies.
II. Technical Memorandum of Understanding.

Attachment I. Supplementary Memorandum of Economic and Financial Policies for 2017–18

INTRODUCTION

1. The Executive Board of the International Monetary Fund on July 13, 2015 approved a three-year arrangement under the Extended Credit Facility (ECF) in support of São Tomé and Príncipe's economic reform program to promote sustainable growth and reduce poverty, underpinned by the Second National Poverty Reduction Strategy Paper (PRSP-II). The overall objectives of the program are to lay the foundation for stronger, more inclusive growth, and to catalyze financial support from bilateral and multilateral partners. Key aspects of the program include actions to strengthen public finances, reduce balance-of-payments vulnerabilities, and clear large domestic arrears.

2. This supplementary Memorandum of Economic and Financial Policies (MEFP) reviews recent economic developments and performance under the ECF-supported program and updates the supplementary MEFP for the second review approved by the IMF Executive Board on December 8, 2016. It describes recent macroeconomic developments, implementation of the ECF-supported program, the economic outlook and risks, and macroeconomic policies for the rest of 2017 and for 2018.

RECENT ECONOMIC DEVELOPMENTS

3. Economic activity has remained stable, while inflation has risen. Real GDP grew by 4.1 percent in 2016, and is expected to expand at about the same rate of 4 percent in 2017. Imports of capital goods and oil products increased by 30 percent and 25 percent respectively in the first six months of 2017, while tourist arrivals and cocoa exports remained broadly constant over the same period. For the full year, the effect of a rise in externally financed projects, as reflected in increased imports of capital goods, is likely to be moderated by fiscal consolidation. Meanwhile, price pressures are coming to the fore, with the 12-month inflation rising to 6.5 percent at end-August 2017 from 5.1 percent at end-December 2016, driven mainly by increased prices of locally-produced goods resulting from higher than usual rainfall.

4. Fiscal performance in the first half of 2017 improved after a challenging year in 2016. The domestic primary deficit (DPD) reached 4 percent of GDP in 2016 against the program target of 2 percent of GDP, as taxes from oil imports fell short by 1½ percent of GDP, and expenditure cuts identified during the second review failed to materialize. The government has since implemented corrective measures, including those identified during the second review. During the first 6 months of 2017, tax measures, including a new tax on imported alcoholic beverages, yielded close to 0.2 percent of GDP, while expenditure was reduced by 0.4 percentage points of GDP relative to 2016. As a result, the DPD during the first half of 2017 reached 1.4 percent of GDP, below the programmed ceiling of 1.5 percent of GDP.

5. Nevertheless, the revenue outturn as of end-August 2017 was significantly lower than expected under the budget largely due to unanticipated developments. Tax receipts from imports were significantly lower than expected partly due to a decline in imports of key commodities such as vehicles, lower than projected oil prices, and delayed payment by ENCO of about 50 billion dobras. While necessary, a correction of the personal income tax (PIT) formula implemented this year has also had a larger impact on PIT revenue than foreseen. As a result, the DPD rose to 1.8 percent of GDP in August.

6. Implementing the arrears reduction plan continues to be a challenge. The government was not able to pay 63 billion dobras in planned arrears clearance to CST and other suppliers in 2016 and accumulated new arrears of 78 billion dobras in 2016. Meanwhile, the stock of outstanding government debt to ENCO was revised upwards by US$12.7 million to US$53.1 million as of end-2015 after overdue bills are accounted in dollars, per the contract, instead of in dobras. On a positive note, favorable oil price developments have reduced the stock of government arrears to ENCO by US$11 million from end-2015 through end-August 2017.

Domestic Payables/Arrears 2015-17, Stocks

	2015 Actual	2016 Original plan	2016 Actual	Jun-17 Original plan	Jun-17 Actual
Treasury to suppliers	364.5	301.4	442.7	288.8	452.4
EMAE (STD bn)	0.0	0.0	55.1	0.0	51.6
CST (STD bn)	79.6	68.1	98.6	63.1	111.9
Other suppliers (STD bn)	284.9	233.3	288.9	225.7	288.9
Treasury to ENCO (USD m)	53.1	52.1	43.9	…	41.9
EMAE to ENCO (USD m)	46.8	…	60.4	…	66.6

7. In the banking sector, excess liquidity is high and credit growth remains anemic. Broad money (M3) declined by 4.4 percent year-on-year in June 2017 reflecting lower net foreign assets while credit to the domestic economy grew by 3.6 percent during the same period. The central bank lowered the policy rate by 100 basis points to 9 percent in June to stimulate economic activity.

8. The banking system remains well capitalized but non-performing loans are high. The risk-weighted capital adequacy ratio increased from 28 percent in 2016 to 30 percent in June 2017, well above the regulatory minimum of 12 percent. The continuous supervision enforcement, including on proper loan classification according to the regulation, contributed to a more accurate measurement of non-performing loans. Furthermore, banks with capital shortages injected additional capital in accordance with current regulations. Overall banking system profitability improved slightly.

9. The current account worsened in the first half of 2017 after an improvement in 2016, mainly due to increased imports of capital goods and oil products. Exports remained broadly constant in the first semester of 2017 after an increase of 8 percent in 2016, which was mainly boosted by the removal of the visa requirement and the increased number of tourists. On the other hand, imports increased by almost 10 percent in the first half of 2017 after remaining broadly constant in 2016. Meanwhile, gross international reserves rose to $67 million (4.6 months of imports) after a decline in 2016.

PROGRAM PERFORMANCE

10. Performance during the first half of 2017 was positive even though end-December 2016 targets were missed. Specifically, the end-December 2016 PCs on DPD and net bank financing of the central government were missed. However, corrective measures implemented, as discussed previously, have yielded results as the end-June 2017 PC on DPD was met. The other PCs for end-June 2017—net international reserves and net bank financing—were also met. Two fiscal indicative targets for end-June 2017 were missed, namely the indicative target (IT) on tax revenues and the IT on non-accumulation of domestic arrears. The shortfall in tax revenue was due to partial payment on import duties by ENCO. The BCSTP also missed the IT on dobra base money. Pro-poor spending target was missed by a small margin, as the budget has been revised down while the target was unchanged (Table 1).

11. Progress has been made in implementing the structural reforms under the program (Table 2). The government completed the assessment of regulation and supervision of BCSTP and enhanced the mandate of the audit board for the BCSTP to international standards. A reform plan of EMAE, which is consistent with full cost recovery over the medium term, was also adopted by the government. Three structural benchmarks were, however, not completed mainly due to capacity constraints and delays in technical assistance (TA) delivery. These are the submission of VAT law to the National Assembly, now expected by end-2017; the completion of the Public Investment Management Assessment (PIMA), a streamlined version that is better aligned to our needs is being planned by the World Bank; and the submission of a draft Public Private Partnership (PPP) law to the National Assembly, now expected at the end of 2017.

ECONOMIC OUTLOOK AND RISKS

12. The economic outlook for 2017 and the medium term is favorable despite some risks. Real GDP growth is expected to remain at 4 percent in 2017 and average around 5½ percent in the medium term, supported by robust activity in construction, agriculture, and tourism. In particular, the expansion of the airport and construction of highways supported by our development partners are expected to start as soon as 2018, which will not only increase construction activities, but also lay the foundation for the growth of tourism and agro-processing industries. Annual inflation is expected to pick up to 6 percent in 2017 and fall to around 5 percent over the medium term as forecasts for lower international food and oil prices offset the impact of the weak domestic production.

13. However, the outlook is subject to significant downside risks. Uncertainties, concerning external financing and lower tourist arrivals from constraints in airport and service capacity, could weaken medium-term growth prospects. Weak domestic implementation capacity could delay the implementation of structural reforms and associated external financing. The forthcoming legislative elections of July 2018 could disrupt policy implementation as pressures to overspend heighten in the run-up to the elections. High non-performing loans could disrupt the recent resumption of lending with negative consequences on economic growth.

POLICY OBJECTIVES FOR 2017-18

The main priorities for 2017/18 will be to consolidate macroeconomic stability, remove structural bottlenecks to higher, sustained, and inclusive growth, and strengthen the financial sector.

A. Fiscal Policy

14. The government has made strong effort to bring fiscal policy in line with the program after slippages in 2016. Recognizing the fiscal excesses in 2016, the government swiftly introduced revenue measures in the revised 2017 budget with revenue yield previously estimated at about 1 percent of GDP. These measures include higher duties on selected imported commodities and reduction in expenditures on goods and services, transfers, and capital projects. However, as noted above, revenue outturns as of end-August were significantly lower than programmed, and the higher duty on alcoholic beverages that took effect in July had a substantial dampening effect on the import volume of these items, partially offsetting the gains from the higher duty and the new consumption tax. The government recognizes that, on current trend, measures of about 2.4 percent of GDP in 2017 relative to the revised budget would be needed to meet the end-2017 target.

15. The government has identified additional measures to address less buoyant than projected tax revenues (Table below). In particular, agreements have been reached with ENCO to pay the balance of taxes owed and stay current in 2017 (close to 50 billion dobras). Agreements have also been reached with two other large private taxpayers and SOEs based on tax audits to pay in installments tax arrears accumulated until end-June 2017, including income taxes on salaries withheld at the source, and consumption tax. Close to 22 billion dobras have already been paid by the private large taxpayers during July and August, and an additional 8.5 billion dobras will be paid over the remainder of the year, while 5 billion dobras are expected from the state-owned enterprises (SOEs) in 2017. These agreements will be supported by stringent penalties, including halting transfers to public institutions, if they do not comply. At the same time, expenditure cuts of 1.4 percent of GDP were identified, of which 0.6 percent from primary current expenditure and 0.8 percent in non-priority capital expenditures. Cautious implementation of the budget to-date to match revenue collection has made these cuts feasible. Strict implementation of the measures described above will ensure achieving the needed savings. In addition, agreements are also being pursued with other taxpayers with significant arrears, which could provide a buffer to meet the target.

Impact of Fiscal Measures
(in percent of GDP)

	2017 Additional Measures
Total revenue gains	1.0
Payment of duty by ENCO	0.8
Collection of tax arrears based on signed agreements	0.2
Total domestic expenditure cuts	1.4
Cuts in primary current expenditure	0.6
of which : Cuts in goods and services	0.2
Cuts in transfers	0.3
Cuts in capex	0.8
Total savings	2.4

16. For the rest of 2017, the government will monitor closely the outlook for revenue and budget support and continue to match expenditure with the available resource envelope to meet the domestic primary deficit target. This is especially important in light of the postponement of the World Bank program support of two $5 million disbursements from 2017-18 to 2018-19 relative to the projection at the second review and the uncertainly associated with the EU disbursement of €4.5 million also in 2017. To smooth out the impact of the postponed World Bank disbursement in 2017, the floor for domestic financing was raised by the equivalent of $3 million, the rest of the shortfall will be addressed by rephasing unpaid arrears clearance in 2016 to 2018-20, instead of paying all in 2017. The accumulation of new arrears will be avoided.

17. Fiscal consolidation will continue in 2018 and beyond in an environment of dwindling external budget support and high debt levels. Submission to Parliament of a 2018 budget, which is in line with the program, is a prior action for the combined third and fourth reviews. Specifically:

- The DPD target is set at 1 percent of GDP in view of the buildup of domestic debt and rephasing of arrears clearance in 2017, and lower external budget grant support in 2018 than projected at the time of the second review. This assumes budget support grants in 2018 of $5 million from the World Bank and €3 million from the EU, and no privatization proceeds. The government will seek to achieve such additional consolidation through various measures, notably by suspending temporarily Article 74 of the tax law regarding the deductible of the PIT and withholding PIT on salaries from transfers to public institutions to secure tax payment with an estimated total gain of 20 billion dobras, and by limiting current expenditure increases, especially in wages, while safeguarding social spending. Specifically, the nominal public wage bill will grow below GDP growth through keeping wages largely frozen to free resources for new hiring to fill priority needs in the education, health, and security sectors, costing about 0.2 percent of GDP, while at the same time seeking savings through rationalization and higher efficiency in these sectors.

- The government is also committed to make up for delayed clearance of arrears to suppliers to bring the arrears clearance plan back on track by 2020. Due to the shortfall in revenue and external financing experienced in 2017-18, arrears repayment is budgeted for now at about 10 and 40 billion dobras in 2017 and 2018 respectively. However, the government views the repayment of arrears as a high priority and will prioritize arrears clearance if additional resources, including privatization proceeds, tax revenue or budget support, materialize.

18. Reducing fiscal risk posed by the state-owned utility company, EMAE, remains high on the government's agenda. EMAE's arrears to ENCO increased by $6 million to $67 million during the first half of 2017 after increasing by $14 million (4¼ percent of GDP) last year. The government, with the support of the World Bank and the European Investment Bank (EIB), is implementing a project to help EMAE achieve cost recovery over the medium term with a focus on improving collection, reducing technical losses, and expanding the development of renewable energy. Adoption of a financial management plan and least cost energy-production plan for EMAE to become financially sustainable over the medium term is proposed as a new structural benchmark.

19. To demonstrate commitment to reform EMAE and to contain costs while medium-term solutions are being implemented, the government will take immediate steps to realign the tariff structure to raise the revenue, reduce EMAE's personnel costs, and set savings targets for the state utility. To guide the reduction of personnel costs, the government has commissioned the Court of Auditors to conduct a specialized audit of the employment and salary levels of EMAE, while a more comprehensive audit of all SOEs is being carried out with the support of the World Bank. Other short-term reform measures that will be implemented by the government include:

- Ensuring that government ministries and agencies pay their electricity bills regularly;
- Reaching a restructuring agreement with consumers in payment arrears;
- Improving service quality to gain public acceptance for any future tariff increases;
- Enforcing antitheft legislation that allows for disconnection and prosecution of those who steal electricity;
- Installing meters for all EMAE clients;
- Publishing the list of debtors of EMAE;
- Expanding the coverage of the payment of electricity bills through the banking system; and
- Promoting energy efficiency programs.

20. Enhancing domestic revenue mobilization through legislative and tax administration reforms will continue in 2017 and 2018. The focus will be placed on the finalization of the VAT law and its approval by Parliament at the same time as the approval of the Budget Law for 2018 in December 2017. The VAT will be implemented in early 2019. According to the collaboration agreement between Ministry of Finance, Commerce and Blue Economy (MOF) and the IMF Fiscal Affairs Department (FAD) (RMTF project), administration reforms will emphasize: (i) hiring and training of 25 new employees; (ii) providing adequate space, including furniture and computers to all staff, including new hires by June 2018; (iii) adopting a clear organizational structure along functional lines and/or taxpayer segments for the tax administration by April 2018; (iv) adopting a modern computer information system with key functionalities, such as automatic notification of taxpayers in default, extraction of statistical data, surveillance, and oversight support by July 2018; and (v) implementing a customer services area and a taxpayers education program by April 2018. To improve domestic revenue mobilization in the medium term, and in line with the recommendations of the March 2017 FAD TA on tax administration, the government will implement a more systematic inspection of large taxpayers and a wider surveillance coverage of taxpayers through a computer-based selection process, and improved risk management.

21. The government will continue to strengthen public financial management. The government, with the support of African Development Bank (AfDB), has already completed a diagnostic study of the electronic information management system (SAFEe). It has also extended the oversight to the general inspection finance entity and is working on extending oversight to the Court of Public Accounts. In this context, it will accelerate the submission of the state's accounts for 2015 and 2016 to the Court of Auditors by December 2017. The government will also move to a centralized framework for monitoring and evaluating projects to ensure value for money. This will be done through the prioritization of capital projects and the adoption of public investment management assessment framework, and medium-term fiscal and expenditure frameworks. Additional TA will be needed in this regard. The government will implement the recommendations of a recent IMF TA mission on public financial management, including strengthening revenue forecasting and ensuring the coherence of the financial programming and macroeconomic framework in budget preparation and management, and limit the accumulations of arrears.

22. Structural reforms to strengthen the fiscal position will be accelerated to enable access to additional financing from development partners. The government remains committed to effectively apply the automatic fuel price adjustment mechanism. A Public Private Partnership (PPP) law has also been completed and will be submitted to the National Assembly for approval before the end of the year (*end-June 2017 structural benchmark*). The government has taken steps to rein in arrears. Postpaid telecommunication has been eliminated and pre-paid services reduced thereby reducing the government telephone bill by more than 20 percent. Recommendations by a working group to assess the appropriate limits for water and electricity in different government units will be adopted in the 2018 budget.

B. Monetary and Financial Sector Policies

23. The BCSTP is committed to further improving liquidity management and forecasting. Steps have already been taken to develop the securities market and the BCSTP is currently amending the regulations to allow for a secondary market and longer-term instruments. The BCSTP is also working closely with the Treasury to improve liquidity forecasting needs, and inform the timing and amount of new security issuance. Forecasts will be updated regularly and used systematically in liquidity management decision making. A schedule of Treasury bill issuance that aligns with cash flow and borrowing plans of the government will also be developed. To further develop the money market, the BCSTP will review the functioning of the market, assess experiences with the issuance of securities with different rates, durations and amounts, and explore market-based approaches to rate determination.

24. The BCSTP will redenominate the domestic currency, effective January 1, 2018. Given the success in reducing inflation since the adoption of the euro peg, the central bank will eliminate three zeros from the dobra (which is now 24,500 to the euro) and issue new bills and coins for use next year. The new bills include innovative features to make them secure against counterfeiting and the redenominated exchange rate will be 24.50 dobras for 1 euro. The BCSTP is implementing an extensive awareness campaign, using radio, television, billboards, posters, workshops and seminars, and social media to smooth the transition and support this monetary reform plan.

25. The BCSTP will continue to reduce banking sector vulnerabilities through frequent monitoring and enhanced supervision. The central bank conducted asset quality assessments that have resulted in correct loan accounting classifications and led to an increase in NPLs. Given its main objectives of promoting financial stability and efficiency of financial intermediation, the BCSTP is making intensive and concerted efforts in the implementation of three important instruments, namely the Financial Sector Development Implementation Plan (FSDIP), the BCSTP Strategic Plan, and the NPL Reduction Strategy. It hopes to help the financial sector to reach the appropriate levels of development to better contribute to the growth and development of the country. In this context, the BCSTP will step up risk-based supervision of the banking system and closely monitor vulnerable banks for potential insolvency. Furthermore, efforts will continue to focus on reducing the high NPLs in the banking sector. It is expected that these strategies will facilitate the sale or restructuring of loans and monetization of collateral through market development; reform the debt management enforcement and insolvency regimes; introduce out of court settlements; and improve banks' capacity to monitor NPLs and clients' credit risk via an updated version of the credit registry system.

26. The government will continue to monitor the liquidation of Banco Equador with the objective of monetizing the remaining assets of the bank and minimizing fiscal cost. After the delays following the court's strike, the liquidator took office in September 2017 and has adopted mechanisms for the beginning of the work involved in the liquidation process. Under the jurisdiction of the courts, the liquidator shall apply the net proceeds of the liquidation to reimburse the bank's closing costs in accordance with the priority of claims provided for in civil law.

27. Plans are advanced to conduct an Asset Quality Review (AQR) of the banking system with the support of the World Bank (structural benchmark, end-December 2017). The BCSTP has finalized the terms of reference for the AQR after receiving comments from both the World Bank and IMF, and the call for tenders for an external consultant to conduct the assessment was issued in September 2017. The AQR is now planned to be completed by end-June 2018 due to delays in identifying financing.

28. The BCSTP is implementing the recommendations of the last safeguards assessment. The independent oversight of the audit policy, internal controls, and financial reporting at the BCSTP was established. Moreover, the BCSTP Audit Board Regulations were revised in line with advice from the IMF Finance Department and approved in March 2017 (*end-December 2016 structural benchmark*). IFRS implementation has been delayed due to difficulties in receiving planned TA from the Central Bank of Brazil. However, the BCSTP has been gradually adopting certain accounting policies that are aligned with International Accounting Standards (IAS), such as the full adoption of the accrual basis of recording assets, reclassification of financial statement items, and reconfiguration of the IT system to align with the new presentation and disclosure rules. The central bank will continue to liaise with the IMF to benefit from available TA in this area.

C. External Sector Policies

29. The government will seek grants and concessional borrowing to reduce the risk of debt distress. The debt sustainability analysis shows that the risk of debt distress is high and the ratios of the present value of debt to GDP, exports, and revenue exceed their thresholds in the early projection period but decline below the thresholds in the long term with prudent fiscal policy. The government will continue its fiscal consolidation program and work to diversify the economy and expand the export base. In addition, the government will limit concessional borrowing to about 4 percent of GDP in the medium term and eschew non-concessional loans to help reduce the high risk of debt distress to ensure that debt is sustainable. The government achieved debt relief of $18.4 million when signing the Economic Agreement with China and is actively seeking debt rescheduling agreements with Angola, Brazil, and Equatorial Guinea.

Borrowing Plan 2017–19
(Millions of U.S. dollars)

New public debt contracted or guaranteed	2017 Volume 1/	2017 Present value 1/
Sources of debt financing	22.0	14.3
Concessional debt of which 2/	22.0	14.3
Non-concessional debt of which 2/	0.0	0.0
Semi-concessional debt 3/	0.0	0.0
Commercial terms 4/	0.0	0.0
Uses of debt financing	22.0	14.3
Memorandum items		
Indicative projections		
2018	17.0	11.1
2019	18.0	11.7

1/ Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate.
2/ Debt with a grant element that exceeds a minimum threshold of 35 percent.
3/ Debt with a positive grant element below the minimum grant element.
4/ Debt without a positive grant element. For commercial debt, the present value would be defined as the nominal/face value.

30. The government will implement measures to strengthen debt management, improve the management of its current loan portfolio, and manage the acquisition of new loans. The National Assembly approved an updated medium-term debt management strategy, together with the 2017 budget, which is in line with the above-mentioned objectives. A new Debt Management Performance Assessment (DeMPA) was completed with the support of the World Bank in November 2016. The DeMPA noted some progress made since the last assessment in 2011, notably the approval of a public debt law in 2013, the development of a medium-term debt management strategy, and the establishment of a T-bill market. The main recommendations of the DeMPA include improving the debt service projections, conducting risk analyses, reporting more detailed information on the debt stock, and migrating the database from Excel to CS-DRMS.

31. The government has secured a grant from China to complement a Kuwait loan in financing the Dr. Ayres Menezes Hospital. The financing package will have a grant element of well above the 35 percent threshold required under the program. The Kuwaiti loan itself has a grant element of 34 percent. This project will bring significant benefits to our people by improving health services.

D. The Implementation of Other Structural Reforms

Business Climate

32. **The government is committed to creating a conducive environment for private sector development.** To this end, our structural reforms agenda prioritizes export diversification and cost competitiveness to support growth and external stability. The government is working with the World Bank on finalizing a national export diversification strategy (*end-December 2017 structural benchmark*), centered on sustainable tourism growth. In addition, the government will pursue strategies to address the unreliable supply and high cost of electricity, including the development of cheaper energy sources. As discussed previously, the government will follow through on plans to reform the state electricity company (EMAE), eliminate cross-subsidies, and move to full cost recovery of electricity tariffs.

Poverty Reduction

33. **Our National Development Plan (NDP) 2017-2021, which succeeds the Second National Poverty Reduction Strategy Paper (PRSP-II, 2012-2016), elaborates our development strategy over the medium term.** The plan is aligned with the sustainable development goals and continues to make poverty reduction an absolute priority of the various public policies aimed at improving the living conditions of the population. The NDP is based on two pillars—(1) accelerating sustainable growth (for job creation, poverty reduction and food security) and (2) strengthening social cohesion and the country's credibility abroad—that are the focus of this 5-year plan, underpinning the broader and longer-term Transformation Agenda (to 2030) and the Vision "São Tomé and Príncipe 2030: The Country We Want to Build." The development priorities are (i) political stability; (ii) sustainable economic growth; (iii) quality education accessible to all; (iv) a strong and modern state and a more solid democracy; (v) adequate infrastructure to promote national development; (vi) a quality health system with national coverage; (vii) decent jobs; (viii) a functioning judicial system accessible to all; and (ix) food and nutrition security. Building on lessons gathered from the implementation of PRSP-II, as poor monitoring and evaluation were identified as one of the main shortcomings, several monitoring committees have been set-up to monitor performance.

Capacity Development

34. **Capacity development remains a priority of the government and continued IMF support will be needed.** The key areas for capacity development include domestic revenue mobilization, public financial management, public investment management, public debt management, and financial sector regulation and supervision. Significant progress has been made from well-tailored TA missions, particularly from peripatetic short-term experts visits that provide much needed hands-on support. Some successful reforms have been initiated, including the implementation of an automatic fuel price adjustment mechanism, the approval of the banking

resolution law, and the introduction of the interbank market. However, weak domestic capacity has slowed the implementation of TA recommendations, requiring more hands-on support. The government will continue working with the IMF and other development partners to achieve our capacity development objectives. The government will particularly welcome increased hands-on follow-up support on the implementation of TA recommendations to improve the impact of TA.

E. Statistics

35. Efforts to address data shortcomings in economic statistics will continue. There is scope to improve balance of payments statistics and extend the coverage of the international investment position. The national statistics institute (INE) has completed the rebasing of the national accounts to 2008 and a new CPI, reflecting price movements in a broader basket of goods and services, using 2014 as the base year. The next steps include splicing the pre–and post–2008 GDP and pre–and post–2014 CPI series, and improving the statistics by developing data on the components of GDP on the demand side and quarterly GDP, including high frequency indicators of economic activity.

PROGRAM MONITORING

36. The performance criteria (PCs), indicative targets (ITs), and structural benchmarks for the remainder of 2017 and for 2018 are presented in Tables 3 and 4. We request an extension of the program to end-2018 and rephasing targets accordingly to allow more time for implementing reforms needed to achieve program objectives of promoting sustainable growth and poverty reduction. The definitions of quantitative PCs and ITs are provided in the attached TMU, which also defines the scope and frequency of data reporting for program monitoring purposes. The fifth review is expected to be completed on or after April 15, 2018, and the sixth review on or after October 15, 2018.

Table 1a. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2016, Preliminary

(Billions of dobras, cumulative from beginning of year, unless otherwise specified)

	2016					
	September		December			
	Indicative Target	Actual	Performance Criteria [1]	Performance Criteria w/ adjustments	Actual	Status
Performance criteria:						
Floor on domestic primary balance (as defined in the TMU) [2]	-100	-250	-155	-155	-314	Not met
Ceiling on changes in net bank financing of the central government (at program exchange rate) [3, 4, 5]	0	220	0	-61	84	Not met
Floor on net international reserves of the central bank (US$ millions) [2, 4]	51	50	49	46	51	Met
Ceiling on central government's outstanding external payment arrears (stock, US$ millions) [5, 6, 7, 8]	0	0	0	...	0	Met
Ceiling on the contracting or guaranteeing of new nonconcessional external debt by the central government or the BCSTP (US$ millions) [5, 6, 7, 8, 9]	0	0	0	...	0	Met
Ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP (stock, US$ millions) [5, 7, 8, 9]	0	0	0	...	0	Met
Indicative targets:						
Ceiling on change of central government's new domestic arrears	0	-8	0	...	55	Not met
Ceiling on dobra base money (stock) [10]	1,102	1,402	1,465	...	1,492	Not met
Floor on pro-poor expenditures	359	409	448	...	482	Met
Floor on tax revenue	783	562	1,170	...	949	Not met
Memorandum items:						
New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the BCSTP (US$ millions) [5, 7, 8, 11]	14	3	18	...	15	...
Transfer from NOA to the budget (US$ millions)	1.6	2.1	1.6	...	2.0	...
Net external debt service payments [12]	107	115	233	...	146	...
Official external program support [12]	88	196	205	...	194	...
Treasury-funded capital expenditure	50	40	101	...	50	...

Sources: São Tomé and Príncipe authorities; and IMF staff estimates and projections.

[1] Performance at the December 2016 test date is assessed on the third review.

[2] The floor will be adjusted upward or downward according to definitions in the TMU.

[3] The ceiling will be adjusted downward or upward according to definitions in the TMU.

[4] Excluding the National Oil Account (NOA) at the Central Bank.

[5] The term "central government" is defined as in ¶ 5 of the TMU, which excludes the operations of state-owned enterprises.

[6] This criterion will be assessed as a continuous performance criterion.

[7] The term "external" is defined on the basis of the residency of the creditor per paragraph 5 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014).

[8] This performance criterion or memorandum item applies not only to debt as defined in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014), but also to commitments contracted or guaranteed for which value has not been received. For further details on the definition of debt and external arrears refer to the TMU, ¶¶ 6 and 13.

[9] Only applies to debt with a grant element of less than 35 percent. For further details refer to the TMU, ¶ 17.

[10] Proposed for changing to a memorandum item.

[11] Only applies to debt with a grant element of at least 35 percent.

[12] As defined in the TMU, valued at the program exchange rate.

Table 1b. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2017, Preliminary (continued)

(Billions of dobras, cumulative from beginning of year, unless otherwise specified)

	2017					
	March		June			
	Indicative Target	Actual	Performance Criteria [1]	Performance Criteria w/ adjustments	Actual	Status
Performance criteria:						
Floor on domestic primary balance (as defined in the TMU) [2]	-74	-98	-124	...	-115	Met
Ceiling on changes in net bank financing of the central government (at program exchange rate) [3, 4, 5]	0	17	0	...	-46	Met
Floor on net international reserves of the central bank (US$ millions) [2, 4]	50	52	50	...	54	Met
Ceiling on central government's outstanding external payment arrears (stock, US$ millions) [5, 6, 7, 8]	0	0	0	...	0	Met
Ceiling on the contracting or guaranteeing of new nonconcessional external debt by the central government or the BCSTP (US$ millions) [5, 6, 7, 8, 9]	0	0	0	...	0	Met
Indicative targets:						
Ceiling on change of central government's new domestic arrears	0	0	0	...	12	Not met
Ceiling on dobra base money (stock) [10]	1,206	1,474	1,254	...	1,415	Not met
Floor on pro-poor expenditures	171	169	301	...	289	Not met
Floor on tax revenue	206	234	520	...	508	Not met
Memorandum items:						
New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the BCSTP (US$ millions) [5, 7, 8, 11]	22	0	22	...	2	
Transfer from NOA to the budget (US$ millions)	2.3	3	2.3	...	3	
Net external debt service payments [12]	33	61	49	...	83	
Official external program support [12]	0	0	8	...	0	
Treasury-funded capital expenditure	25	9	25	...	15	

Sources: São Tomé and Príncipe authorities; and IMF staff estimates and projections.

[1] Performance at the June 2017 test date is assessed on the fourth review.

[2] The floor will be adjusted upward or downward according to definitions in the TMU.

[3] The ceiling will be adjusted downward or upward according to definitions in the TMU.

[4] Excluding the National Oil Account (NOA) at the Central Bank.

[5] The term "central government" is defined as in ¶ 5 of the TMU, which excludes the operations of state-owned enterprises.

[6] This criterion will be assessed as a continuous performance criterion.

[7] The term "external" is defined on the basis of the residency of the creditor per paragraph 5 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014).

[8] This performance criterion or memorandum item applies not only to debt as defined in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014), but also to commitments contracted or guaranteed for which value has not been received. For further details on the definition of debt and external arrears refer to the TMU, ¶¶ 6 and 13.

[9] Only applies to debt with a grant element of less than 35 percent. For further details refer to the TMU, ¶ 17.

[10] Proposed for changing to a memorandum item.

[11] Only applies to debt with a grant element of at least 35 percent.

[12] As defined in the TMU, valued at the program exchange rate.

Table 2. São Tomé and Príncipe: Structural Benchmarks Under ECF Program, December 2016 - June 2017

Policy Objectives and Measures	Timing	Macro Rationale	TA Involved	Status
Strengthening Public Finances				
Adopt a plan to reform EMAE (state-owned electricity and water utilities company) to ensure full cost recovery.	End-December 2016	To support arrears clearance plan	With World Bank and EU support	Met.
Submit to the National Assembly a new VAT law.	End-December 2016	To support the introduction of VAT	Forthcoming FAD/LEG TA	Not met. *(Proposed for reset to a later date.)*
Complete a public investment management assessment (PIMA) and submit to staff a reform plan to strengthen public investment management practices.	End-December 2016	To enhance capacity for efficient public investment decision-making	With World Bank support	Not met. (*The World Bank will provide a streamlined PIMA more suitable to STP.)*
Submit the draft public private partnership (PPP) law to the National Assembly.	End-June 2017	To enhance capacity for efficient public investment decision-making	No TA involved	Not met. *(Draft PPP law prepared but not yet presented to the National Assembly.)*
Enhancing Monetary Policy and Financial Stability				
Establish an Audit Board for BCSTP that specifies a role similar to a conventional audit committee, with responsibilities for oversight of internal and external audit mechanisms, and financial reporting.	End-December 2016	To enhance independent oversight of the audit and control mechanisms	No TA involved	Implemented with delay (March 2017).
Complete assessment of regulation and supervision in lieu of a full assessment of compliance with Basel Core Principles.	End-December 2016	To improve soundness of financial system	MCM TA	Met.

Table 3. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2017-18, Preliminary

(Billions of dobras, cumulative from beginning of year, unless otherwise specified)

	2017			2018		
	September	December		March	June	December
	Indicative Target	Performance Criteria [1]		Indicative Target	Performance Criteria [1]	Indicative Target
	2nd Review	2nd Review	Revised	Proposed		
Performance criteria:						
Floor on domestic primary balance (as defined in the TMU) [2]	-173	-152	-152	-48	-90	-97
Ceiling on changes in net bank financing of the central government (at program exchange rate) [3, 4, 5]	0	0	66	50	75	65
Floor on net international reserves of the central bank (US$ millions) [2, 4]	50	54	51	52	52	54
Ceiling on the accumulation of central government's new external payment arrears (US$ millions) [5, 6, 7, 8]	0	0	0	0	0	0
Ceiling on the contracting or guaranteeing of new nonconcessional external debt by the central government or the BCSTP (US$ millions) [5, 6, 7, 8, 9]	0	0	0	0	0	0
Indicative targets:						
Ceiling on change of central government's new domestic arrears	0	0	0	0	0	0
Ceiling on dobra base money (stock) [10]	1,290	1,540	…	…	…	…
Floor on pro-poor expenditures	417	501	501	188	289	551
Floor on tax revenue	817	1,237	1,066	238	535	1,211
Memorandum items:						
New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the BCSTP (US$ millions) [5, 7, 8, 11]	22	22	22	17	17	17
Transfer from NOA to the budget (US$ millions)	2.3	2.3	2.3	1.5	1.5	1.5
Net external debt service payments [12]	57.7	107.2	55.0	34.0	68.0	136.0
Official external program support [12]	8	205	147	45	85	218
Budget support grants	…	…	110	45	66	181
Treasury-funded capital expenditure	25	94	27	6	13	28
Ceiling on dobra base money (stock)	…	…	…	1,553	1,578	1,574

Sources: São Tomé and Príncipe authorities; and IMF staff estimates and projections.

[1] Performance at the December 2017 and proposed June 2018 test dates is assessed on the fifth and sixth reviews, respectively.

[2] The floor will be adjusted upward or downward according to definitions in the TMU.

[3] The ceiling will be adjusted downward or upward according to definitions in the TMU.

[4] Excluding the National Oil Account (NOA) at the Central Bank.

[5] The term "central government" is defined as in ¶ 5 of the TMU, which excludes the operations of state-owned enterprises.

[6] This criterion will be assessed as a continuous performance criterion.

[7] The term "external" is defined on the basis of the residency of the creditor per paragraph 5 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014).

[8] This performance criterion or memorandum item applies not only to debt as defined in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014), but also to commitments contracted or guaranteed for which value has not been received. For further details on the definition of debt and external arrears refer to the TMU, ¶¶ 6 and 13.

[9] Only applies to debt with a grant element of less than 35 percent. For further details refer to the TMU, ¶ 17.

[10] Proposed for changing to a memorandum item.

[11] Only applies to debt with a grant element of at least 35 percent.

[12] As defined in the TMU, valued at the program exchange rate, excludes HIPC-related amortization.

Table 4. São Tomé and Príncipe: Structural Benchmarks Under ECF Program, December 2017 - June 2018, Preliminary

Policy Objectives and Measures	Timing	Macro Rationale	TA involved
Prior action			
Adopt a 2018 budget that is consistent with the program parameters *(newly proposed, ¶17).*	End-November 2017	To demonstrate commitment to fiscal consolidation	No TA involved
Strengthening Public Finances			
Adopt measures to contain EMAE's loss in the near term *(newly proposed, ¶19).*	End-December 2017	To contain fiscal risk	No TA involved
Adopt financial management plan and least cost energy-production plan for EMAE *(newly proposed, ¶18).*	End-June 2018	To contain fiscal risk	With World Bank support
Submit to the National Assembly a new VAT law *(proposed to reset to a later date).*	End-June 2018	To support the introduction of VAT	Forthcoming FAD/LEG TA
Submit the draft public private partnership (PPP) law to the National Assembly *(proposed to reset to a later date).*	End-December 2017	To enhance capacity for efficient public investment decision-making	No TA involved
Enhancing Monetary Policy and Financial Stability			
Complete an independent detailed asset quality review of banks *(proposed to reset to a later date).*	End-June 2018	To support financial sector stability and	With World Bank support
Facilitating Business Activities			
Develop and submit to the National Assembly a National Export Diversification Strategy document *(proposed to reset to a later date).*	End-June 2018	To promote economic diversification and employment opportunities	With World Bank support

Attachment II. Technical Memorandum of Understanding, November 2017

1. **This Technical Memorandum of Understanding (TMU) contains definitions and adjuster mechanisms that clarify the measurement of quantitative performance criteria and indicative targets in Table 3**, which are attached to the Memorandum of Economic and Financial Policies for 2017 and 2018. Unless otherwise specified, all quantitative performance criteria and indicative targets will be evaluated in terms of cumulative flows from the beginning of each calendar year.

2. **The program exchange rate** for the purposes of this TMU[1] will be 20,299 dobra per U.S. dollar, 24,500 dobra per euro, and 29,236 dobra per SDR for both 2017 and 2018.

PROVISION OF DATA TO THE FUND

3. **Data with respect to all variables subject to performance criteria and indicative targets will be provided to Fund staff on the frequency described below** (paragraph 24) with a lag of no more than four weeks for data on net international reserves of the Central Bank of São Tomé and Príncipe (BCSTP) and six weeks for other data. The authorities will transmit promptly to Fund staff any data revisions. For variables that are relevant for assessing performance against program objectives but are not specifically defined in this memorandum, the authorities will consult with Fund staff as needed on the appropriate way of measuring and reporting. Performance criteria included in the program are defined below, specifically (i) the floor on domestic primary balance; (ii) the ceiling on changes in net bank financing of the central government; (iii) the floor on net international reserves of the central bank; (iv) the ceiling on central government's outstanding external payments arrears; and (v) the ceiling on the contracting or guaranteeing of new non-concessional external debt by the central government or the BCSTP.

DEFINITIONS

4. **For the purposes of this TMU**, **external** and **domestic** shall be defined on a residency basis.

5. **Central government is defined for the purposes of this TMU** to comprise all governmental departments, offices, establishments, and other bodies that are agencies or instruments of the central authority of São Tomé and Príncipe. The central government does not include the operations of state-owned enterprises.

6. **Debt is defined as in paragraph 8 of the Guidelines on Public Debt Conditionality in Fund Arrangements, adopted by Decision No. 15688 of the Executive Board (Dec. 5, 2014).** "Debt will be understood to mean a current, i.e., not contingent, liability, created under a contractual agreement through the provision of value in the form of assets (including currency) or services, and

[1] Data refer to the mid-point exchange rates published on the BCSTP's webpage for the last day of 2014.

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."

7. Government domestic revenue (excluding oil revenue) comprises all tax and non-tax revenue of the government (in domestic and foreign currencies), excluding: (1) foreign grants, (2) the receipts from the local sale of in-kind grants (e.g., crude oil received from Nigeria, food aid, etc.), and (3) any gross inflows to the government on account of oil signature bonus receipts and accrued interest on the National Oil Account (NOA). Revenue will be measured on a cash basis as reported in the table of government financial operations prepared by the Directorate of Budget and the Directorate of Treasury in the Ministry of Finance, Commerce and the Blue Economy (MOF).

8. Domestic primary expenditure comprises all government spending assessed on a commitment basis (*base compromisso*), excluding (1) capital expenditure financed with external concessional loans and project grants and (2) scheduled interest payments. Reporting of government domestic expenditure will be based on the state budget execution prepared every month by the Directorate of Budget and the Directorate of Treasury in the MOF. The portion of EU budget support grants that is used to finance capital expenditures in the areas linked to the conditionality of the grants, specifically on improving water supply and sanitation, is treated as project grants.

Official External Program Support

	2017	2018 H1	2018	Currency Unit
Projected budgetary support grants				
World Bank	0.0	2.5	5.0	million US dollars
European Union	4.5	1.5	3.0	million euros
IMF ECF program	1.3	0.6	1.3	million SDR

PERFORMANCE CRITERIA

9. Performance criterion on the floor on domestic primary balance. This performance criterion refers to the difference between government domestic revenue (excluding oil revenue) and domestic primary expenditure. For reference, this balance for end 2016 was -314 billion dobra, broken down as follows:

Domestic Primary Balance (2016, billions of dobra)		
I	Total revenue (=1+2)	1130
I.A	**of Which: Government Domestic Revenue (=I-2.1)**	**1056**
1	Tax revenue	949
2	Nontax revenue	181
2.1	*of which: oil revenue*	74
II	Total Domestic expenditure (=4+5+6)	1403
II.A	**Of which: Domestic primary expenditure (=I-4.2)**	**1370**
4	Current expenditure	1334
4.1	Personnel costs	684
4.2	Interest due	34
4.3	Goods and services	249
4.4	Transfers	282
4.5	Other current expenditure	84
5	Domestic capital expenditure	50
5.1	Financed by the Treasury	50
5.2	Financed by privatization proceeds	0
6	HIPC Initiative-related social expenditure	19
III	**Domestic primary balance (= I.A - II.A)**	**-314**

10. Performance criterion on the ceiling on <u>changes</u> in net bank financing of the central government (NCG). This performance criterion refers to the increase (decrease) of net bank financing of the central government, which equals the stock of all outstanding claims on the central government held by the BCSTP and by other depository corporations (ODCs), less the stock of all deposits held by the central government with the BCSTP and with ODCs. The balance of the National Oil Account (NOA), deposits from project grants and loans, contingent liabilities, and social security operations are not included in NCG. All foreign exchange-denominated accounts will be converted to dobra at the program exchange rate. The relevant data are reported monthly by the BCSTP to the IMF staff. For reference, at end-2016, outstanding net bank financing of the central government (excluding NOA) was 40 billion dobra, as follows:

Net Banking Financing (Billions of dobra)			
		2015	2016
I	**Net credit to government by the BCSTP (=I.1-I.2)**	**...**	**161**
I.1	BCSTP credit, including use of IMF resources:	...	386
I.2	Government deposits with the BCSTP (excluding NOA)	...	225
	Treasury dobra-denominated accounts	...	14
	Treasury foreign currency-denominated accounts	...	129
	Counterpart deposits	...	82
II	**Net credit to government by ODCs**	**...**	**-120**
II.1	ODC's credit to the government	...	38
II.2	Government deposits with ODCs (including counterpart funds)	...	158
III	**Net bank financing of the government (excluding NOA) (=I-II)**	**-43**	**41**
IV	**Changes during 2016 in net bank financing of the central government (NCG)**		**84**

11. Performance criterion on the floor on net international reserves (NIR) of the BCSTP. The NIR of the BCSTP are defined for program-monitoring purposes as short-term (i.e., original maturities of one year or less), tradable foreign assets of the BCSTP minus short-term external liabilities, including liabilities to the IMF. All short-term foreign assets that are not fully convertible external assets nor readily available to and controlled by the BCSTP (i.e., they are pledged or otherwise encumbered external assets, including but not limited to the HIPC umbrella SDR account and assets used as collateral or guarantees for third-party liabilities) will be excluded from the definition of NIR. Securities whose market value on the last day of the year differs by over 20 percent from their original nominal issue price will be assessed at their market value as reported by the BCSTP's Markets Department. The balance of (1) NOA at the BCSTP, (2) banks' deposits related to capital or licensing requirements, and (3) banks' reserves denominated in foreign currency are excluded from the program definition of NIR. All values are to be converted to U.S. dollars at the actual mid-point market exchange rates prevailing at the test date. For reference, at end 2016 NIR was 1,188 billion dobra (or $50.7 million, using the exchange rate of 23,438 dobra per U.S. dollar), calculated as follows:

International Reserves
(End-2016, billions of dobra)

I	**Gross international reserves**	**1481**
	Cash	16
	Demand deposits	407
	Term deposits (incl. banks' deposits in foreign currency)	188
	Securities other than shares	840
	Portuguese Treasury Bond I	234
	Portuguese Treasury Bond II	248
	Rede Ferroviaria Nacional bonds	126
	US Treasury Bill I	116
	US Treasury Bill II	117
	Accrued interest on securities	15
	Reserve position in the Fund	0
	SDR holdings	15
II	**Foreign Exchange Liability**	**293**
	Short-term bilateral liabilities	23
	Liabilities to the IMF	121
	Banks' reserves denominated in foreign currency	149
	Banks' guaranteed deposits denominated in foreign currency	0
III	**Net international reserves (NIR) (=I - II)**	**1188**
IV	**Net other foreign assets**	**169**
	Other foreign assets	392
	Medium and long-term liabilities (including SDR allocation)	223
IV	**Net foreign assets (III+IV)**	**1357**
	Memorandum item: National Oil Account (NOA)	271

12. Performance criterion on the ceiling on the contracting or guaranteeing of new nonconcessional external debt by the central government or the BCSTP. This is a continuous performance criterion that refers to the contracting or guaranteeing of new external debt of any maturity (including overdraft positions but excluding normal import and supplier credits) by the government and/or the BCSTP. Debt is considered nonconcessional if it includes a grant element less than 35 percent. The grant element is the difference between the nominal value of the loan and its net present value, expressed as a percentage of the nominal value. The net present value of the debt at the date on which it is contracted is calculated by discounting the stream of debt service payments at the time of the contracting. The discount rate used for this purpose is 5 percent. A loan comes into effect on the signature date of the contract, unless it is specified in the contract that it becomes effective upon ratification by the parliament. For the program monitoring purpose, a loan contract is treated to be in effect on the date of the first disbursement if that is earlier than the date of signature or ratification of the contract. With respect to the precautionary line of credit from Portugal to support the pegging of the dobra to the euro, unpaid balances outstanding during the first three quarters of a given calendar year will be excluded from this ceiling. However, outstanding balances at the end of a given calendar year will be included in the assessment of compliance with this performance criterion. This performance criterion does not apply to IMF facilities. Debt being rescheduled or restructured is excluded from this ceiling. Medium- and long-term debt will be reported by the Debt Management Department of the MOF (as appropriate), measured in U.S. dollars at the prevailing exchange rates published by the BCSTP. The government should consult with IMF staff before contracting or guaranteeing new medium– or long–term debt obligations.

13. Performance criterion on the ceiling on the accumulation of central government's new external payment arrears. This is a continuous performance criterion. New central government 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 agreement, subject to any applicable grace period. This performance criterion does not apply to arrears resulting from the nonpayment of debt service for which a clearance framework has been agreed or for which the government is actively seeking a rescheduling agreement.

INDICATIVE TARGETS

14. Ceiling on change of central government's new domestic arrears is set on the difference between expenditure on a commitment basis and cash payments (amounts past due after 40 days and unpaid).

15. Within domestic primary expenditure, the floor on pro-poor expenditure refers to the floor on government outlays recorded in the budget that have a direct effect on reducing poverty, as agreed with the IMF and World Bank staffs. These expenditures, which include both current and capital outlays, are defined as follows:

a. **Pro-poor current spending:** These cover the following functional classifications and expenditure categories (by budget code) as described in the matrix below:

Code	Economic classification of current expenditure	Education	Health	Social Security and Assistance	Housing and Community Services	Culture and Sport	Fuel and Energy	Agriculture and Fisheries
310000	Personnel Expenses	x	x					
331210	Specialty Durable Goods	x	x					
331290	Other Durable Goods	x	x					
331120	Fuels and Lubricants[1]	x	x					
331130	Foodstuffs, Food[1] and Accommodation	x	x					
331140	Specialized Current Consumable Materials (Specific to Each Sector)	x	x					
331190	Other Consumer Non Durable Goods	x	x					
332110	Water and Energy Services	x	x					
332120	Communication Services	x	x					
332130	Health services	x	x					
332220	Maintenance and Conservation Services	x	x					
353900	Other Miscellaneous Current Expenses	x	x	x				
352200	Transfers to non-profit institutions (private)		x	x				
352310	Retirement Pension and Veterans		x	x				
352320	Family Benefit		x	x				
352330	Scholarships	x						
352390	Other Current Transfers to Families		x	x				
353100	Unemployment Fund		x	x				
Code	**Economic classification of capital expenditure**							
411110	Feasibility Study and Technical Assistance	x	x	x	x	x	x	x
411120	Procurement and Construction of Real Estate	x	x	x	x	x	x	x
411200	Rehabilitation Works and Facilities	x	x	x	x	x	x	x
411300	Means and Equipments of Transportation	x	x	x	x	x	x	x
411400	Machinery and Equipment	x	x	x	x	x	x	x
411900	Other Fixed Capital Goods	x	x	x	x	x	x	x
412000	Stocks	x	x	x	x	x	x	x

Source: Diário da Republica de São Tome e Principe No. 21 - May 7, 2008, pages 12-13.

[1] Expenditures on fuels and lubricants (*combustíveis e lubrificantes*) that are affected for administrative purposes are excluded. Likewise, food (*alimentação*) and clothing and shoes (*roupas e calçados*) supplied to administrative staff are excluded.

b. **Pro-poor treasury-funded capital spending:** This covers projects that are deemed to have a direct impact on alleviating poverty in the following sectors: education, health, social safety nets, agriculture and fisheries, rural development, youth and sports, provision of potable water, and electrification.

16. Floor on tax revenue is set on tax revenue that includes direct and indirect taxes as well as recovery of tax arrears and additional collection efforts.

MEMORANDUM ITEMS

17. New concessional external debt contracted or guaranteed by the central government or the BCSTP measures such debt with a grant element of at least 35 percent.

18. Net external debt service payments by the central government are defined as debt service due less the accumulation of any new external payment arrears, as defined under the performance criterion on the ceiling on central government's outstanding external payment arrears.

19. Official external program support is defined as budget support grants and loans, including disbursements from the IMF under the ECF arrangement and in-kind aid when the products are sold by the government and the receipts are earmarked for a budgeted spending item, and other exceptional financing provided by foreign official entities and incorporated into the budget.

20. Treasury-funded capital expenditure is classified as part of domestic primary expenditure and covers public investment projects that are not directly financed by project grants and concessional loans or that have to be partially co-financed with government resources. It includes spending on new construction, rehabilitation, and maintenance. Expenditure on wages and salaries and the purchase of goods and services related to the projects will not be classified as capital expenditure.

21. Ceiling on dobra base money is set on the sum of currency issued—which consists of currency outside depository corporations and cash in vaults—and banks reserves denominated in dobra. Bank reserves refer to reserves of commercial banks (in dobra) held with the central bank and include reserves in excess of the reserve requirements.

USE OF ADJUSTERS

22. The performance criterion on the domestic primary balance will have one adjuster. The floor on the domestic primary balance will be adjusted downward if the government receives more than projected budget support grants (excluding any portion of the additional EU grant used to finance capital expenditure on water and sanitation, which will be included in project grant financed capital expenditure) and privatization receipts in 2017 and 2018 ; this adjuster will be capped at 77.7 billion dobra (about 1 percent of 2016 GDP) for 2017 and 38.8 billion dobra for the first semester of 2018.[2] For program purpose, the projected privatization proceeds are 0 in 2017 and 2018.

23. The performance criteria on net bank financing of the central government and net international reserves of the central bank will be subject to the following adjusters based on deviations calculated cumulatively from end-December 2016 or end-December 2017, as appropriate (MEFP Attachment I, Table 3):

- ***Adjusters on ceilings on changes in net bank financing of the central government (NCG)***: Quarterly differences between actual and projected receipts of budget transfers from the NOA, budgetary support grant, net external debt service payments, and domestic arrears will be converted to dobra at the program exchange rate and aggregated from end-December 2016 or end-December 2017, as appropriate, to the test date. The ceilings will be adjusted:
    - (i) downward (upward) by cumulative deviations downward (upward) of actual from projected net external debt service payments (exclude HPIC),
    - (ii) downward (upward) by deviation upward (downward) in budget transfers from the NOA,
    - (iii) downward by deviation upward of budgetary support grants in excess of 77.7 billion dobra and upward for the full deviation downward of budgetary support grants.

[2] Grants and related expenditures to cover the cost of the elections will be excluded from the measurements of the domestic primary deficit.

- (iv) downward by deviation upward of domestic arrears.

The combined application of all adjusters at any test date is capped at the equivalent to US$3 million at the program exchange rate.

- ***Adjusters for the floor on net international reserves (NIR) of the BCSTP***: Quarterly differences between actual and projected receipts of budget transfers from the NOA, official external program support, net external debt service payments, and domestic arrears in dobra, will be converted to U.S. dollars at the program exchange rate and aggregated from end-December 2016 or end-December 2017, as appropriate, to the test date. The floor will be adjusted upward (downward):

    - (i) by the cumulative deviation downward (upward) of actual from projected net external debt service payments of the central government;
    - (ii) by deviations upward (downward) for budget transfers from the NOA, and
    - (iii) by deviations upward (downward) of official external program support. Budget support loans in 2017 and 2018 are projected to be 0.

The combined application of all adjusters at any test date is capped in such a way that the adjusted floor does not fall short of US$46 million in 2017 and US$50 million in 2018.

DATA REPORTING

24. The following information will be provided to the IMF staff for the purpose of monitoring the program.

1) **Fiscal Data:** The Directorate of Treasury and Directorate of Budget at the MOF will provide the following information to IMF staff, within six weeks after the end of each month or quarter, except for the public investment program (PIP), which will be provided three months after each quarter:

    - Monthly data on central government operations for revenues, expenditure, and financing, including detailed description of net earmarked resources (*recursos consignados*), on commitment (*compromisso*) and cash payments (*caixa*);
    - Monthly data on net credit to the government by the BCSTP, recorded account by account in a format fully compatible with the monetary accounts of the BCSTP;
    - Monthly detailed data on tax and nontax revenues;
    - Monthly detailed data on domestically financed capital expenditure on commitment (compromisso) and cash payments (caixa);
    - Monthly data on domestic arrears by type and by creditor;

- Quarterly data on implicit arrears to ENCO on account of fuel retail prices eventually not covering import costs, distribution margins and applicable taxes;
- Quarterly data on EMAE's arrears to ENCO;
- Monthly data on official external program support (non-project);
- Quarterly data on the execution of the public investment program (PIP) by project and sources of financing;
- Quarterly data on the execution of Treasury-funded capital expenditure by project type, amount, timetable of execution, and progress of execution;
- Quarterly data on project grant and loan disbursement (HIPC and non-HIPC);
- Quarterly data on bilateral HIPC debt relief;
- Quarterly information on the latest outstanding petroleum price structures and submission of new pricing structures (within a week of becoming available).
- Quarterly pro-poor expenditure.

2) **Monetary Data:** The BCSTP will provide the IMF staff, within three weeks from the end of each month, the monetary accounts of the BCSTP. Other monetary data will be provided within six weeks after the end of each month for monthly data, within two months after the end of each quarter for quarterly data, and within two months after the end of the year for annual data. The BCSTP will provide the following information to IMF staff:

- Daily data on exchange rates, to be posted on the central bank's web site;
- Daily data on interest rates, to be posted on the central bank's web site;
- Daily liquidity management table, including dobra base money and currency in circulation, to be posted on the central bank's web site;
- Daily net international reserve position, to be posted on the central bank's web site;
- Monthly balance sheet data of BCSTP (in IMF report form 1SR, with requested memorandum items);
- Monthly consolidated balance sheet data of other depository corporations (in IMF report form 2SR);
- Monthly consolidated depository corporations survey (in IMF survey 3SG);
- Monthly central bank foreign exchange balance (Orçamento cambial);
- Quarterly table on bank prudential ratios and financial soundness indicators;

- Quarterly data on the BCSTP's financial position (profit and loss statement, deficit, budget execution, etc.).

3) **External Debt Data:** The Directorate of Treasury at the MOF will provide the IMF staff, within two months after the end of each month the following information:

- Monthly data on amortization and interest on external debt by creditor; paid, scheduled, in arrears, and subject to debt relief or rescheduled;

- Quarterly data on disbursements for foreign-financed projects and program support loans;

- Annual data on future borrowing plans.

4) **National Accounts and Trade Statistics:** The following data will be provided to the IMF staff:

- Monthly consumer price index data, provided by the National Institute of Statistics within one month after the end of each month;

- Monthly data on imports (value of imports, import taxes collected, and arrears) and commodity export values, provided by the Customs Directorate at the MOF, within two months after the end of each month;

- Monthly data on petroleum shipments and consumption (volumes and c.i.f. prices, by product), provided by the Customs Directorate.

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

November 27, 2017

THIRD AND FOURTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, EXTENSION OF THE ARRANGEMENT, AND MODIFICATION OF PERFORMANCE CRITERIA—INFORMATIONAL ANNEX

Prepared By

The African Department
(in Consultation with Other Departments)

CONTENTS

RELATIONS WITH THE FUND

(As of September 30, 2017)

Membership Status

Joined: September 30, 1977; Article XIV

General Resources Account:	**SDR Million**	**% Quota**
Quota	14.80	100.00
Fund holdings of currency	14.80	100.02
Reserve tranche position	0.00	0.00

SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	7.10	100.00
Holdings	0.06	0.85

Outstanding Purchases and Loans:	**SDR Million**	**% Quota**
ECF Arrangements	3.44	23.21

Latest Financial Arrangements:

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
ECF[1]	07/13/2015	07/12/2018	4.44	1.90
ECF[1]	07/20/2012	07/13/2015	2.59	1.11
ECF[1]	03/02/2009	03/01/2012	2.59	0.74

1/ Formerly PRGF.

Projected Payments to Fund[2]

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2017	2018	2019	2020	2021
Principal		0.39	0.33	0.26	0.41
Charges/Interest	0.01	0.04	0.04	0.04	0.04
Total	0.01	0.42	0.37	0.30	0.45

2/ When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	December 2000
Assistance committed	
by all creditors (US$ million)[1]	124.30
Of which: IMF assistance (US$ million)	1.24
(SDR equivalent in millions)	0.82
Completion point date	March 2007
Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	0.82
Interim assistance	…
Completion point balance	0.82
Additional disbursement of interest income[2]	0.04
Total disbursements	0.87

1/ Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

2/ Under the enhanced framework, an additional disbursement is made corresponding to interest income earned on the amount of HIPC assistance committed but not disbursed.

Implementation of Multilateral Debt Relief Initiative (MDRI):

MDRI-eligible debt (SDR Million)[1]	1.43
Financed by: MDRI Trust	1.05
Remaining HIPC resources	0.38

Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGT**	**Total**
December 2007	N/A	0.38	0.38
March 2007	N/A	1.05	1.05

1/ The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

Safeguards Assessments:

The 2015 safeguards assessment found that severe capacity constraints contributed to a weak safeguards framework at the BCSTP. In particular, financial reporting practices lacked transparency; independent oversight on audit, financial reporting and control mechanisms required strengthening; and the BCSTP's legal framework needed to be revised to align it with leading practices for central banks. Notwithstanding, external audits conducted by a reputable audit firm continue to serve as a critical safeguard. In addition, the BCSTP has taken steps to implement independent oversight on the audit and control mechanisms by establishing a new Audit Board with revised roles and responsibilities, and the drafting of legal reforms has been initiated. However, ongoing institutional development will be needed to strengthen capacity, especially in the area of financial reporting.

Exchange Arrangements:

The de jure and de facto exchange rate arrangement is a conventional peg against the euro. Since January 2010 São Tomé and Príncipe has pegged the dobra to the euro at a rate of dobra 24,500 per euro. The organic law of the BCSTP authorizes it to make decisions regarding exchange rate policy. The commission on foreign exchange sales cannot be higher than 2 percent for the euro and 4 percent for other currencies. Purchases of euro must be done at the rate published by the BCSTP and no commissions are allowed. The official euro–U.S. dollar cross rate is based on the European Central Bank (ECB) reference rate of the previous day. The BCSTP finances current international transactions at the official exchange rate only after verification of the documentation establishing the bona fide nature of the bank's request. Access to foreign exchange is limited to institutions having a net position in the transaction currency of less than 12 percent of qualified capital, a net position in total foreign currency less than 25 percent of qualified capital, and which are in compliance with the central bank's regulations on bank liquidity and capital adequacy. Financial institutions are allowed access to the central bank's facilities regardless of the above conditions if the foreign exchange is to be used for importation of goods and services in periods of crisis or for the importation of fuel. Commercial banks that meet these requirements can buy foreign exchange directly from the central bank, which can charge up to 1.5 percent commission on sales of euro and up to a 0.5 percent commission on purchases of euro. The buying rate is mainly indicative because the BCSTP rarely makes purchases. The current exchange rate system has effectively eliminated the multiple currency practice related to the existence of numerous exchange rate markets with differing exchange rates for spot transactions that existed in previous years.

São Tomé and Príncipe continues to avail itself of the transitional arrangements under Article XIV, but it does not maintain restrictions under Article XIV. However, it maintains one measure subject to Fund approval under Article VIII: an exchange restriction arising from Article 3(i) and Article 10.1(b) of the Investment Code (Law No. 7/2008) regarding limitations on the transferability of net income from investment. The restriction results from the requirement that taxes and other obligations to the government have to be paid/fulfilled as a condition for transfer, to the extent the requirement includes the payment of taxes and the fulfillment of obligations unrelated to the net income to be transferred.

Article IV Consultation:

São Tomé and Príncipe is currently under a 24-month consultation cycle. The Executive Board concluded the last Article IV consultation on June 10, 2016.

Financial Sector Assessment Program (FSAP), Reports on Observance of Standards and Codes (ROSCs), and Offshore Financial Center (OFC) Assessments:

None.

Resident Representative:

The Fund has not had a Resident Representative office in São Tomé and Príncipe since October 2006.

Technical Assistance 2011-17:

Date of Delivery	Department/Purpose
August 2017	AFRITAC mission on government finance statistics
July 2017	FAD mission on budget execution and control
March 2017	FAD mission on revenue administration
March 2017	FAD mission on arrears management
March 2017	STA mission on national accounts statistics
February 2017	MCM mission on banking supervision and regulation
November 2016	MCM mission on bank resolution and liquidation
August 2016	MCM mission on banking supervision and regulation
August 2016	FAD/LEG mission on tax policy
April 2016	FAD mission on arrears management
March 2016	MCM mission on banking supervision
November 2015	STA mission on national accounts statistics
November 2015	FAD mission on automatic fuel pricing mechanism
September/October 2015	FIN mission on safeguards assessment
September 2015	MCM mission on banking supervision
July 2015	FAD mission on tax administration
June 2015	STA mission on balance of payments and IIP
April 2015	FAD mission on medium-term fiscal framework
March 2015	FAD mission on tax administration
March 2015	MCM mission on banking supervision
November 2014	MCM mission on banking supervision
September 2014	STA mission on national accounts statistics
September 2014	MCM mission on liquidity management

Date of Delivery	Department/Purpose
April 2014	STA mission on balance of payments and IIP
April 2014	MCM mission on liquidity management
March 2014	MCM mission on banking supervision
February 2014	FAD mission on public accounting
December 2013	FAD short-term expert visit on public accounting
November 2013	MCM mission on banking supervision
August 2013	FAD mission on revenue administration
August 2013	MCM mission on banking supervision
June 2013	FAD mission on public accounting
March 2013	MCM mission on banking supervision
January 2013	MCM mission on liquidity management
January 2013	FAD mission on public accounting
November 2012	FAD mission on medium-term fiscal framework
November 2012	FIN mission on safeguards assessment
November 2012	LEG follow-up mission on AML/CFT
October 2012	MCM mission on banking supervision
October 2012	FAD diagnostic mission on customs
October 2012	FAD mission on public accounting
September 2012	MCM mission on liquidity management
July 2012	LEG diagnostic mission on AML/CFT
April 2012	FAD mission on revenue administration
March 2012	FAD mission on public financial management
March 2012	STA mission on balance of payments
February 2012	LEG diagnostic mission on AML/CFT
February 2012	FAD mission on implementation of SAFEe
January 2012	FAD diagnostic mission on tax administration
November 2011	MCM TA needs assessment mission
November 2011	MCM mission on liquidity management
November 2011	FAD mission on public accounting
October 2011	FAD mission on public financial management
August 2011	FAD mission on public accounting
June 2011	MCM mission on liquidity management
June 2011	FAD mission on public accounting
February 2011	MCM mission on bank resolution framework
January 2011	FAD mission on public accounting

RELATIONS WITH THE WORLD BANK GROUP

Joint Managerial Action Plan (JMAP) for São Tomé and Príncipe

(As of October 20, 2017)

1. The IMF and World Bank São Tomé and Príncipe teams held regular meetings to discuss their respective work programs and macro critical structural reforms for São Tomé and Príncipe. The two institutions' teams met in the context of the supervision for the current ECF-supported program that discusses policies and financing during the prospective program period 2015–18.

2. The World Bank's work program is guided by a Country Partnership Framework (CPF) for the fiscal years 2014 to 2018, approved in FY14, that focuses on supporting growth and job creation through two broad themes: macroeconomic stability and national competitiveness, and reducing vulnerability and strengthening human capacity. Gender, partnership, and capacity building are elements that cut across all the proposed engagements. A two-year extension of the current CPF is being sought to incorporate the results of the Performance and Learning Review, and the new household survey in the new Systematic Country Diagnosis (SCD) to the new CPF. A Debt Management and Performance Assessment (DeMPA) report was completed in November 2016.

3. The IMF's work program included the Executive Board's consideration of the second review under the ECF-supported program in December 2016, a staff visit in July 2017, and a review mission in September 2017 to supervise the ECF-supported program, and assistance with capacity development in the areas of public financial management, revenue administration, and banking supervision.

4. The Bank and the Fund are providing complementary support to help São Tomé and Príncipe strengthen public financial management and make progress towards debt sustainability. Regarding the latter, the teams prepared a Joint IMF-World Bank Debt Sustainability Analysis (DSA) update in 2017 to accompany the ECF-supported program review to the Board in December 2017.

Work Program for Period 2017–18			
Title	*Products*	*Provisional timing of missions*	*Expected delivery date*
	A. Mutual information on relevant work programs		
World Bank work program in the next 12 months	• STP Power Sector Recovery Project • 2nd Development Policy Operation • PER • Support to the new Household survey • Payment system & financial inclusion • Bank resolution • Support to business environment reforms • Transport Sector Development Project • Quality Education for All • Adaption to Climate Change Project • Institutional Capacity Project • Social Protection and Skills Development	Oct 2017 Nov 2017 Nov 2017 Nov 2017 Nov 2017 Nov 2017 Oct 2017 Jan 2018 Nov 2017 Jan 2018 Nov 2017 Nov 2017	Approved FY2018 FY2018 FY2018 FY2019 FY2019 FY2017 FY2019 Approved Approved FY2018 FY2019
IMF work program in the next 12 months	• ECF combined third and fourth review • ECF fifth review and Article IV • Technical Assistance from FAD/LEG/AFRITAC: ○ Tax policy (VAT) ○ Tax law - VAT legislation ○ Revenue administration ○ PFM • MCM: ○ Bank resolution ○ Banking Supervision	Sep-Oct 2017 Mar-Apr 2018 Sep-Nov 2017 Nov 2017 FY2018 FY2018 Nov 2017 Dec 2017	FY2018 FY2019 FY2018 FY2018 FY2018 FY2018 FY2018 FY2018
	B. Requests for work program inputs		
Fund request to Bank	• Information on Bank budget support operations and disbursement schedule • Economic development document (EDD) assessment	To support the 2017 -18 fiscal program	Ongoing Completed
Bank request to Fund	• Collaboration on providing full set of macroeconomic framework and tables		Ongoing

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP

(As of October 20, 2017)

1. The Bank Group commenced lending operations in São Tomé and Príncipe in 1978. To date, the Bank approved loans and grants, amounting to a cumulative commitment of about UA 135 million (US$191 million).

2. As of October 2017, the Bank's active portfolio in São Tomé and Príncipe consisted of five operations, amounting to roughly UA 25 million (US$35 million). These are: Infrastructure Rehabilitation for Food Security (PRIASA II); the Public Finance Management Project (PAGEF); the National Planning Scheme study; the Trade Facilitation project (second phase of ASYCUDA); and the Payment System (Table 1). The portfolio is relatively young. The average age of the portfolio is 2.6 years and the cumulative disbursement rate is 26 percent after the closure of two projects (i.e., PRIASA I with a disbursement rate of 100 percent and National Program for Drinking Water Supply and Rural Sanitation with 85 percent disbursement rate). In terms of sectoral distribution, the agriculture and fisheries sector dominates the portfolio with 57 percent, followed by the multi-sector operations with 37 percent and finance with 6 percent. There is no ongoing private sector or multinational projects. The portfolio is largely funded by African Development Fund loan (81 percent), followed by the Global Environmental Fund (GEF) (10 percent), the Transition Support Facility (TSF) (8 percent), and the African Trade Facilitation Fund (1.5 percent). The Bank also conducted analytical work focused in the areas of energy, agriculture, public financial management, and the private sector development strategy 2015-2024.

3. The AfDB current involvement in STP is guided by the Country Strategy Paper (CSP) 2012–16, approved in July 2012. The strategy was focused on two pillars: Pillar I - Strengthening Governance; and Pillar II - Promotion of Agriculture Infrastructure. The CSP's main objective was to prepare the authorities for the forthcoming oil production era and the associated challenges and risks to the country's socio-economic development, as well as to help the government address the issue of food security. In September 2017, the Committee on Development Effectiveness approved the CSP completion report prepared to guide the preparation of CSP 2017-2021. In this context, two pillars were identified as potential intervention areas for the Bank: Pillar I - Energy and Water Infrastructure, and Pillar II - Capacity Building for Improved Economic Management. Both pillars are consistent with the authorities' priorities as well as with the AfDB's priorities outlined in the 2013–2022 strategy, and the High 5 agenda.

4. As part of its strategy and knowledge products, the AfDB also envisages to undertake the following economic and sector work: (i) fragility assessment; (ii) governance profile (an update); (iii) agriculture statistics strategy; (iv) national strategy for youth employment and human capital; (v) study on the constraints and potentials of blue economy; and (vi) preparation of a gender strategy 2017-2022. These studies will inform the preparation of future projects and provide support to the government's policy reform efforts.

5. STP reached the Highly-Indebted Poor Countries (HIPC) decision and completion points in 2000 and 2007, respectively. As a result, in March 2007, the country achieved the completion point and benefited from debt relief under HIPC and Multilateral Debt Relief Initiative (MDRI), amounting to US$327 million. About 73 percent of the debt relief was made by multilateral institutions—of which, 40 percent from the African Development Bank, 29 percent from the World Bank, and 27 percent from bilateral partners (11 percent from Paris Club countries and 16 percent from non-Paris Club countries)[1]. The country's outstanding debt to the AfDB is projected to reach US$0.11 million by the end of 2017.

Table 1. AfDB Ongoing Projects (Millions of UA)

Description	Approval Date	Completion Date	Net commitments (UA million)	Disbursement Rate (%)	Window
Food Security Support Project (PRIASA II)	10/06/2015	31/12/2020	11.50	19	ADF loan
			2.48	0	GEF
National Planning Scheme (PNAT)	25/01/2016	31/12/2018	2.00	4	ADF loan
Total Agriculture			**15.98**	**14**	
Trade Facilitation	14/10/2014	30/06/2017	0.31	64	Africa Trade Fund
Economic and Financial Management Project (PAGEF)	14/01/2013	29/06/2018	5.00	43	ADF grant
			2.00	89	TSF grant
Total Multisector			**7.31**	**56**	
Payment System Infrastructure and Financial Inclusion (SPAUT)	03/02/2017	31/12/2021	1.50	0	ADF loan
Total Finance Sector			**1.50**	**0**	
Total Portfolio			**24.79**	**26**	

[1] Data from the Government.

STATISTICAL ISSUES

(As of October 26, 2017)

I. Assessment of Data Adequacy for Surveillance
General: Economic data are broadly adequate for surveillance. At the same time, serious financial, human, and technological resource constraints have delayed efforts to strengthen the statistical system.
National Accounts: The authorities compile and publish an annual GDP time series, using an outdated base year (2001) and inadequate source data. National accounts data are not timely as the latest estimate of GDP is for calendar year 2014. Quarterly estimates of GDP are not compiled. The authorities have produced a revised estimate of GDP for 2008; a preliminary, but incomplete, rebased GDP time series; and are currently working to finalize a complete rebased GDP time series and will consider publication by the end of calendar year 2017. The latest technical assistance mission (March 2017) progressed this objective and recommended additional resources to enhance the capacity of the national statistical office (INE) and enable collection of appropriate source data.
Consumer Price Statistics: The INE began to disseminate a new CPI (base: 2014 = 100) from January 2016. With the assistance of AFRISTAT, the product mix was changed and the weights were updated, using the results of a household expenditure survey conducted in 2010. Due to financial constraints, the new CPI only covers the capital city. A technical assistance mission in FY2018 is planned to review the re-referenced index, perform diagnostics on the entire series, link the pre- and post-rebased series to produce an analytical series for the IMF database and statistical purposes, and consider INE's plans for further updates to the CPI upon completion of the new HES that is underway.
Government Finance Statistics: Detailed revenue and expenditure data are compiled and reported to AFR. The main areas that need to be strengthened are: (i) monitoring of expenditures on projects financed by donors; and (ii) financing operations. All project loans (financed by donors) are programmed in the budget, but some are executed independently. The government has requested development partners to help in recording all external financing in the budget. The recording of financing operations and stocks is expected to improve since the debt data management capacity is expected to be strengthened. The 2010-14 government accounts have been finalized and presented to the Court of Audit. The authorities are working on the 2015 and 2016 government accounts. Past technical assistance in government finance statistics (GFS) has helped the Ministry of Finance to compile and disseminate GFS for the budgetary central government in accordance with the *Government Finance Statistics Manual 2001 (GFSM 2001)*. The authorities now report GFS data to STA on a consistent basis and submitted a time series of summary annual GFS for 2002–2016. However, the data include significant statistical discrepancies between above-the-line and below-the-line data and there are discrepancies between GFS data reported to STA and fiscal data provided to AFR. Faster statistical progress is hampered by an inadequate accounting system.

STP has recently joined the AFRITAC Central project aimed at developing GFS. The first diagnostic mission took place in August 2017. The mission identified the priorities in terms of the GFS compilation and suggested to the authorities a migration path towards the full adoption of the *Government Finance Statistics Manual 2014 (GFSM 2014)* principles.
Monetary and Financial Statistics: STA missions provided technical assistance on monetary statistics in December 2004, April/May 2006, June 2007 and September 2010. As a result, the accuracy and timeliness of the monetary data reported in the standardized report forms (SRF) for the central bank and the other depository corporations' data improved significantly. The BCSTP has resumed reporting monthly data to STA for the central bank and other depository corporations (ODCs) on a regular basis. The BCSTP monthly trial balance sheet is broadly adequate to compile monetary statistics in line with the *Monetary and Financial Statistics Manual and Compilation Guide (MFSMCG).* A new plan of accounts for ODCs was introduced in January 2010. The September 2010 mission reviewed the new plan of accounts for the financial system, and found it adequate for a proper classification, sectorization, and valuation of financial instruments, and in line with the methodology of the *MFSMCG*. However, the mission detected serious shortcomings in the information reported by some banks and an inconsistent approach in the way banks report to the BCSTP. Following the mission's recommendations, the BCSTP worked towards eliminating those problems. The central bank has begun to collect data from insurance companies that opened in the past few years. The asset sizes of insurance companies remain small enough not to warrant inclusion in monetary statistics at this time. The central bank produces a quarterly FSI table. MCM TA missions on banking supervision have helped expand the coverage of the table and improved the data quality. The additional information compiled could permit the beginning of stress testing exercises in the near future. STA contacted the BCSTP to receive FSI data on a regular basis according to the methodology of the *FSI Compilation Guide* for their posting on the IMF's website.
External Sector Statistics: The BCSTP compiles quarterly balance of payments (BOP) and international investment position (IIP) statistics consistent with the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)*. The BCSTP conducts quarterly surveys to collect BOP and IIP data from the private nonfinancial sector and from the oil and gas sector. However, the response rates are low and the coverage of these sectors needs to improve. There is room to improve the compilation of external sector statistics, particularly to improve timeliness and lower large errors and omissions. The BCSTP has worked to improve the compilation of financial transactions and IIP statistics. However, further work is needed to expand the coverage, improve reliability and ensure consistency between IIP and BOP data. A technical assistance mission is planned for this purpose in FY2018.

A June 2015 mission recommended improving coordination and data sharing among data-producing agencies, increasing staff dedicated to the compilation and collection of external sector statistics, and discussing with the Joint Development Authority the establishment of mechanisms for receiving regular data on production sharing agreement contracts. The National Petroleum Agency has started submitting regular data.
II. Data Standards and Quality
São Tomé and Príncipe has participated in the Fund's General Data Dissemination System (GDDS) since April 20, 2004. Currently, it is in its successor data dissemination initiative, eGDDS.

Democratic Republic of São Tomé and Príncipe: Table of Common Indicators Required for Surveillance

(As of October 2017)

	Date of Last Actual Observation	Date Received	Frequency of Data[6]	Frequency of Reporting	Frequency of Publication
Exchange rates	Oct. 2017	Oct. 2017	D	D	D
International reserve assets and reserve liabilities of the monetary authorities[1]	Oct. 2017	Oct. 2017	D	D	D
International investment position	Mar. 2017	Jun. 2017	Q	Q	Q
Reserve/base money	Oct. 2017	Oct. 2017	D	D	D
Broad money	Aug. 2017	Sep. 2017	M	M	M
Central bank balance sheet	Aug. 2017	Sep. 2017	M	M	M
Consolidated balance sheet of the banking system	Aug. 2017	Sep. 2017	M	M	M
Interest rates[2]	Aug. 2017	Sep. 2017	M	M	M
Consumer Price Index	Aug. 2017	Sep. 2017	M	M	M
Revenue, expenditure, balance and composition of financing[3] – general government[4]	Aug. 2017	Sep. 2017	M	M	M
Revenue, expenditure, balance and composition of financing[3] – central government	Aug. 2017	Sep. 2017	M	M	M
Stocks of central government and central government-guaranteed debt[5]	Sept. 2017	Oct. 2017	M	Q	Q
External current account balance	Jun. 2017	Sep. 2017	Q	Q	Q
Exports and imports of goods	Aug. 2017	Oct. 2017	M	M	M
GDP/GNP[6]	2014	Sep. 2017	A	A	A
Gross external debt	Sep. 2017	Oct. 2017	M	Q	Q

[1] Includes reserve asset pledged or otherwise encumbered as well as net derivative positions.
[2] Central bank's reference rate.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra-budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); not available (NA).

INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

November 27, 2017

THIRD AND FOURTH REVIEWS UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, EXTENSION OF THE ARRANGEMENT, AND MODIFICATION OF PERFORMANCE CRITERIA—DEBT SUSTAINABILITY ANALYSIS[1]

Approved By
David Owen and Kevin Fletcher (IMF) and Paloma Anos-Casero (IDA)

Prepared by:
International Monetary Fund and International Development Association staffs in collaboration with the authorities of São Tomé and Príncipe.

São Tomé and Príncipe is at a high risk of debt distress according to this joint Bank-IMF low-income country debt sustainability analysis (DSA). *This assessment is unchanged from the previous DSA completed in May 2016. Similar to the previous DSA, the ratios of present value of debt to GDP, exports, and revenue under the baseline exceed their thresholds for high risk of debt distress early in the projection period with a declining trend in the long run. The debt service ratios stay below the thresholds under all scenarios. Domestic arrears were added for the first time to the public debt stock. The rapid increase in the debt ratios under the historical scenario underscores the importance of continuing fiscal consolidation, eschewing non-concessional loans, and working to diversify the economy and expand the export base. A customized scenario shows that it is vital to seek grant and equity financing for a large part of extremely large infrastructure projects because even concessional loans when contracted too rapidly would threaten debt sustainability.*

[1] The DSA update was prepared by IMF and World Bank staff in collaboration with the authorities of São Tomé and Príncipe. The analysis updates the previous Joint DSA dated May 20, 2016 (IMF Country Report No. 16/174). The DSA follows the IMF and World Bank Staff Guidance Note on the Application of the Joint Fund-Bank Debt Sustainability Framework for Low-Income Countries (November 5, 2013). The DSA uses the unified discount rate of 5 percent set out in Decision No. 15462 (October 11, 2013). For the purpose of defining debt burden thresholds under the Debt Sustainability Framework (DSF), São Tomé and Príncipe is classified as a weak policy performer. São Tomé and Príncipe's average rating on the World Bank's Country Policy and Institutional Assessment (CPIA) for the period 2014-16 is 3.07. The corresponding indicative thresholds are: 30 percent for the NPV of debt-to-GDP ratio; 100 percent for the net present value (NPV) of debt-to-exports ratio; 200 percent for NPV of debt-to-revenue ratio; 15 percent for the debt service-to-exports ratio; and 18 percent for the debt service-to-revenue ratio.

BACKGROUND

1. **The previous full debt sustainability analysis (DSA) for São Tomé and Príncipe was undertaken as part of the 2015 request for a three-year arrangement under the Extended Credit Facility (IMF Country Report No. 15/196). An updated DSA was subsequently completed in May 20, 2016, during the second review of the program (IMF Country Report No. 16/174).** Both DSAs concluded that São Tomé and Príncipe was at a high risk of debt distress.

2. **São Tomé and Príncipe reached the completion point under the enhanced Heavily Indebted Poor Country (HIPC) initiative in March 2007, received topping-up assistance in December 2007 and HIPC/Multilateral Debt Relief Initiative (MDRI) debt relief later.** The MDRI, in particular, brought substantial debt relief as 54 percent of the pre-HIPC-completion-point debt was with IDA, AfDB, and IMF. Paris Club members also helped improve the country's debt profile. The external debt ratio decreased from 415 percent of GDP in 2001 to 19 percent in 2008 (without pre-HIPC legacy arrears).

Text Table 1. São Tomé and Príncipe: Public Debt Stock

(As of end-June 2017)	Million USD	Share of GDP (%)
Total PPG debt	**225.4**	**59%**
Total PPG external debt	**176.5**	**46%**
Multilateral Creditors	**40.8**	**11%**
IDA	13.3	**3%**
BADEA	10.6	**3%**
FIDA	6.0	**2%**
AfDB	4.4	**1%**
IMF	4.3	**1%**
OPEC	2.2	**1%**
Bilateral Creditors	**123.9**	**32%**
Portugal	57.2	**15%**
Angola	50.0	**13%**
China[1]	10.0	**3%**
Brazil[1]	4.3	**1%**
Equatorial Guinea	1.6	**0%**
Belgium	0.8	**0%**
External suppliers' debt	**11.8**	**3%**
Domestic arrears	**48.9**	**13%**
ENCO (oil importing compan	41.9	**11%**
CST (telecom)	4.8	**1%**
EMAE (water and electricity)	2.2	**1%**
Memorandum items:		
Pre-HIPC legacy arrears	**55.1**	**14%**
Italy[1]	24.3	**6%**
Angola	30.8	**8%**
Arrears from EMAE to ENCO	**66.6**	**17%**

Sources: Country authorities and IMF staff estimates

[1] Commercial debt guaranteed by the government.

3. **Total public and publicly guaranteed (PPG) debt, including domestic arrears to suppliers, is estimated at 59 percent of GDP ($225.4 million) in June 2017, with medium and long-term PPG external debt accounting for 46 percent of GDP ($176.5 million) (Text Table 1).** The pre-HIPC initiative legacy arrears are excluded from the DSA on the assumption of expected forgiveness. These pre-HIPC legacy arrears amount to 14 percent of GDP. Similarly, a disputed loan from Nigeria was also excluded from the debt stock. On the other hand, the current DSA adds domestic arrears, mainly from the central government to the oil importing company ENCO, to the debt stock of 2016. At the time of the previous DSA update, these arrears were still being audited and were not yet recognized by the government. Text table 2 lists the types of arrears and how they are treated in the DSA. The World Bank is providing technical assistance to São Tomé and Príncipe to improve its debt and state-owned enterprise (SOE) management, which will help to reduce the incidence of external and domestic arrears. A peripatetic debt management expert is working together with the debt management unit to improve the weaknesses highlighted in the 2016 Debt Management Performance Assessment (DeMPA) report. At the same time, the World Bank has developed an SOE reform

plan and is implementing energy sector reform. Inefficiencies in the energy sector are the main source of the cross-arrears between SOEs and the government.

Text Table 2. Arrears and Disputed Debt

(As of end-June 2017)

Type	**Description**	**DSA Treatment**
Pre-HIPC legacy (14 percent of GDP)	São Tomé and Príncipe has pre-HIPC legacy arrears to Angola ($30.8 million) and Italy ($24.3 million). São Tomé and Príncipe is making best efforts to reach an agreement consistent with the representative Paris Club agreement. In 2017 São Tomé and Príncipe was able to secure relief from pre-HIPC legacy arrears to China of $18.4 million.	Not included in the DSA.
Post-HIPC bilateral arrears (2 percent of GDP)	São Tomé and Príncipe has post-HIPC arrears to Angola ($2 million), Brazil ($4.3 million), and Equatorial Guinea ($0.7 million). Negotiations on rescheduling agreements are already under way with Angola and Brazil, and São Tomé and Príncipe is actively seeking a rescheduling agreement with Equatorial Guinea. These arrears are the result of weak debt management and staff assesses that São Tomé and Príncipe has the capacity to repay them.	Included in the DSA.
Domestic arrears (13 percent of GDP)	São Tomé and Príncipe has domestic arrears to the oil-company ENCO ($41.9 million), the telecom company CST ($4.8 million), and the water and electricity company EMAE ($2.2 million). The government has a domestic arrears clearance plan.	Included in the DSA.
Disputed debt (8 percent of GDP)	A loan from Nigeria in the amount of $30 million was excluded from the debt stock as it is under dispute based on information provided by the São Tomé and Príncipe authorities. This loan was extended as advances on oil revenues in the context of the joint development zone between these two countries, but this project has stalled.	Not included in the DSA.

4. The largest disbursements during 2016 and the first half of 2017 were from Angola and Portugal ($9 million and $3 million, respectively). Disbursements in 2016 were lower than initially expected ($9.5 million vs $14.7 million), mainly due to the non-realization of the disbursements from Kuwait and Turkey. There are $75.7 million of debt already contracted which is expected to be disbursed between 2017 and 2021. The budget expects disbursements of $20.9 million in 2017, and Angola has already disbursed in the first semester. These expected disbursements are all included in the DSA. Preliminary information suggests that the economic agreement with China involves only grants in the near term.

Projected Loan Disbursement
(In USD millions)

	2017	2018-2021
Kuwait	1.7	14.7
EIB	0.0	12.7
AfDB	7.6	12.5
Portugal	2.2	6.8
BADEA	1.2	6.3
IMF	1.8	1.8
Angola	4.5	0.0
IFAD	1.9	0.0
Sum	**20.9**	**54.8**

5. In terms of composition, public sector debt is composed solely of debt contracted or guaranteed by the central government. SOEs do not have external debt. In terms of creditors, the composition has shifted after the HIPC completion point—the share of multilateral debt declined from nearly 60 percent before the completion point to 21 percent. Portugal and Angola are now the country's main bilateral creditors, and IDA is its main multilateral creditor.

MACROECONOMIC ASSUMPTIONS

6. The basic macroeconomic assumptions have changed slightly from those in the previous DSA. The key assumptions are:

Text Table 3. Macroeconomic Assumptions (Averages)

	2015 DSA[1]	2016 DSA[2]	2017 DSA		Historical	
	2015–35	2016–36	2016–36	2017-37	2006-16	2014-16
Real GDP growth (percent)	5.5	5.6	5.3	5.4	4.4	4.1
Inflation (percent average)	3.2	3.1	3.5	3.4	12.4	5.6
Domestic primary deficit (percent of GDP)	-1.3	-1.2	-1.4	-1.3	-4.3	-3.4
Grants (percent of GDP)	12.3	11.4	8.0	7.6	17.0	12.3
New borrowing (percent of GDP)	1.5	1.4	2.4	2.3	7.3	6.4
FDI (percent of GDP)	9.7	8.8	4.2	3.8	16.7	12.3
USD export growth (percent)	7.2	7.4	6.7	6.6	20.6	26.0
USD import growth (percent)	6.0	6.0	5.2	5.5	10.5	3.8
Current account balance, excluding grants (percent of GDP)	-25.0	-19.4	-13.8	-13.2	-37.7	-26.0
Current account balance, including grants (percent of GDP)	-12.7	-8.0	-5.8	-5.6	-20.6	-13.7

[1] IMF Country Report No. 15/196.
[2] IMF Country Report No. 16/174.

- ***Growth assumptions have remained largely unchanged from the last DSA.*** The economy is estimated to have grown by 4 percent in 2016, lower than previously assumed, as overall activity was constrained by lower-than-projected foreign-financed capital spending. Growth is expected to remain at 4 percent in 2017 and pick up to 5½ percent over the medium term. The main drivers of growth are expected to be construction, tourism, agriculture, and fisheries. Stronger macroeconomic policies, further measures to enhance the business climate, and successful implementation of a tourism development strategy would be needed to sustain growth at 5½ percent a year over the long term.

- **Inflation is assumed to remain around 3 percent over the long term**, reflecting continued fiscal prudence and the effects of the peg of the dobra to the euro, which has been in effect since January 2010. Inflation increased by 1.1 percentage points to 5.1 percent in 2016, driven by rising food prices and one-off factors, and is expected to increase further to 6 percent at the end of 2017. The GDP deflator in US dollar terms is projected to grow by 2.8 percent in 2017. It will, however, pickup to 6.1 percent in 2018 before settling at around 1.3 percent in the long run.

- ***A decline in the domestic primary deficit*** from 4.3 percent of GDP in 2016 to 1.8 percent of GDP in 2017 is consistent with the authorities' budgeted domestic primary deficit and with their commitment to enhancing revenue mobilization and limiting transfers and personnel expenditures. The domestic primary deficit is projected slightly higher than in the previous DSA and is expected to stay at 1.3 percent of GDP in the long run, financed by budget support grants and a drawdown of National Oil Account (NOA) deposits. Over the long term, expenditure bears the brunt of adjustment as budget support grants decline. No domestic borrowing is envisaged.

- ***Total grants are projected to remain at their current level*** of about 12 percent of GDP in 2017–22. In the long run, grants will decline in importance and average around 6 percent of GDP a year.

- Like the previous DSA, this assessment assumes a ***loan concessionality*** threshold of 35 percent. To fund the government's capital investment program, new borrowing will average about 3.4 percent of GDP a year from 2017–21 and about 2 percent of GDP thereafter. No financing from future privatization operations, commercial loans, domestic borrowing, and short-term loans are assumed throughout the DSA projection period.

- ***FDI* is projected to stabilize at around 4 percent of GDP** over the long term. The authorities expect continued investment in infrastructure projects to support tourism and agriculture development.

- The ***non-interest current account deficit*** (including official grants) is expected to maintain the low level of 6 percent of GDP observed in 2016 as the government further consolidates its position. Export growth will be driven by cocoa and palm oil production, and increased tourism as São Tomé and Príncipe rehabilitates its infrastructure (including the extension of the airport's runway) and benefits from the higher frequency of flights from Europe since 2014.

- ***Downside risks*** include difficulties in increasing revenue mobilization and in limiting spending, particularly that financed by non-concessional loans. The outlook could also be adversely impacted by supply shocks (leading to higher inflation and lower growth). A protracted period of slower growth in Europe could significantly depress exports, tourism, and FDI flows.

EXTERNAL DEBT SUSTAINABILITY

7. Like in the previous DSA, under the baseline scenario all three external debt stock indicators breach their indicative thresholds early in the projection period (Figure 1, blue lines).[2] The debt service ratios continue to stay below their thresholds under all scenarios. All indicators improve over time as a result of growth, fiscal consolidation, slower debt accumulation, expansion of the export base, and constrained imports.

8. Stress tests show that the most extreme shock extends the period of breach of thresholds for a few additional years beyond those observed in the baseline (Figure 1, solid black lines). As in the previous DSA, export based indicators are most sensitive to exports shocks, while the remaining indicators are most sensitive to a one-time depreciation shock. This highlights the need to keep future borrowing in check, maintain the credibility of the exchange rate peg, and maintain international reserves at prudent levels.

9. The external balance must improve through a combination of improved competitiveness and fiscal discipline to keep debt on a sustainable path. Slippages—for example, setting the non-interest current account deficit at their historical levels—would drastically worsen the debt trajectory relative to the baseline (Figure 1, red dotted line).

10. A customized DSA scenario shows that São Tomé and Príncipe has limited space for borrowing, even concessionally, particularly for extremely large infrastructure projects (Figure 1). This scenario assumes that $300 million (close to São Tomé and Príncipe's GDP) in concessional loans with a grant element of 35 percent are disbursed over the next four years (2017-20) to finance a part of the airport and deep sea port projects that have been reported in the media. Under these assumptions, the external debt-to-GDP ratio would reach 112 percent of GDP by 2020. In addition, under the baseline, the present value (PV) of debt ratios breach their respective thresholds during almost the entire projection period and the debt service ratios also breach their thresholds.

[2] São Tomé and Príncipe's quality of policies and institutions, as measured by the average World Bank's Country Policy and Institutional Assessment (CPIA) for the period 2014-16, is 3.07 (weak performer). The corresponding indicative thresholds are: 30 percent for the net present value (NPV) of debt-to-GDP ratio; 100 percent for the NPV of debt-to-export ratio; 200 percent for NPV of debt-to-revenue ratio; 15 percent for the debt service-to-exports ratio; and 18 percent for the debt service-to-revenue ratio.

PUBLIC DEBT SUSTAINABILITY

11. The assessment of São Tomé and Príncipe's public debt sustainability is largely unchanged relative to the last DSA despite the inclusion of domestic arrears. The PV of debt-to-GDP indicator breaches the threshold in the first four years of projection, but improves quickly and steadily afterwards, as depicted in the baseline scenario. As is the case in the previous DSA, the debt dynamics appear unsustainable under the historical and fixed primary balance scenarios, underscoring the importance of continued fiscal consolidation and fostering private sector led growth through structural reforms. All public debt indicators are most sensitive to a one-time 30 percent depreciation of the dobra.

DEBT DISTRESS QUALIFICATION AND CONCLUSIONS

12. São Tomé and Príncipe remains at a high risk of debt distress. The country is already in external arrears with some bilateral creditors, with whom it is actively seeking rescheduling agreements. Two other aggravating factors are that a large part of its domestic arrears, namely the ones to ENCO, is denominated in USD and there are considerable contingent liabilities coming from the state-owned enterprise EMAE,[3] which are not considered in this DSA as it focuses only on the central government. However, given that fiscal consolidation and prudence in contracting new debt are in place, all indicators improve in the long term. The current assessment is very similar to the previous one. In this context, the DSA underlines the need for measures to mitigate risks:

- Remain committed to maintaining the exchange rate peg and an adequate level of international reserves to boost confidence;
- Maintain fiscal prudence by enhancing revenue mobilization and expenditure control;
- Accelerate reforms to improve policy and institutional performance to enhance growth potential;
- Ensure favorable financing terms in the form of grants or highly concessional borrowing; and
- Develop and implement a comprehensive strategy to reduce the cost of doing business and attract private investment that can broaden the export base.

13. The biggest risks to external debt sustainability come from exchange rate, exports and primary balance shocks. Debt sustainability could deteriorate if protracted periods of slower growth in Europe significantly depress exports, tourism, and FDI flows. The risks appear manageable over the medium term if the authorities are able to move forward with the planned fiscal adjustment in the coming years and safeguard international reserves. These vulnerabilities also underscore the importance of sound macroeconomic policies to fulfill the country's growth potential on a sustained basis.
The development of sound public debt management, anchored in a medium-term debt management strategy and medium-term fiscal framework, will be essential to guide future development financing.

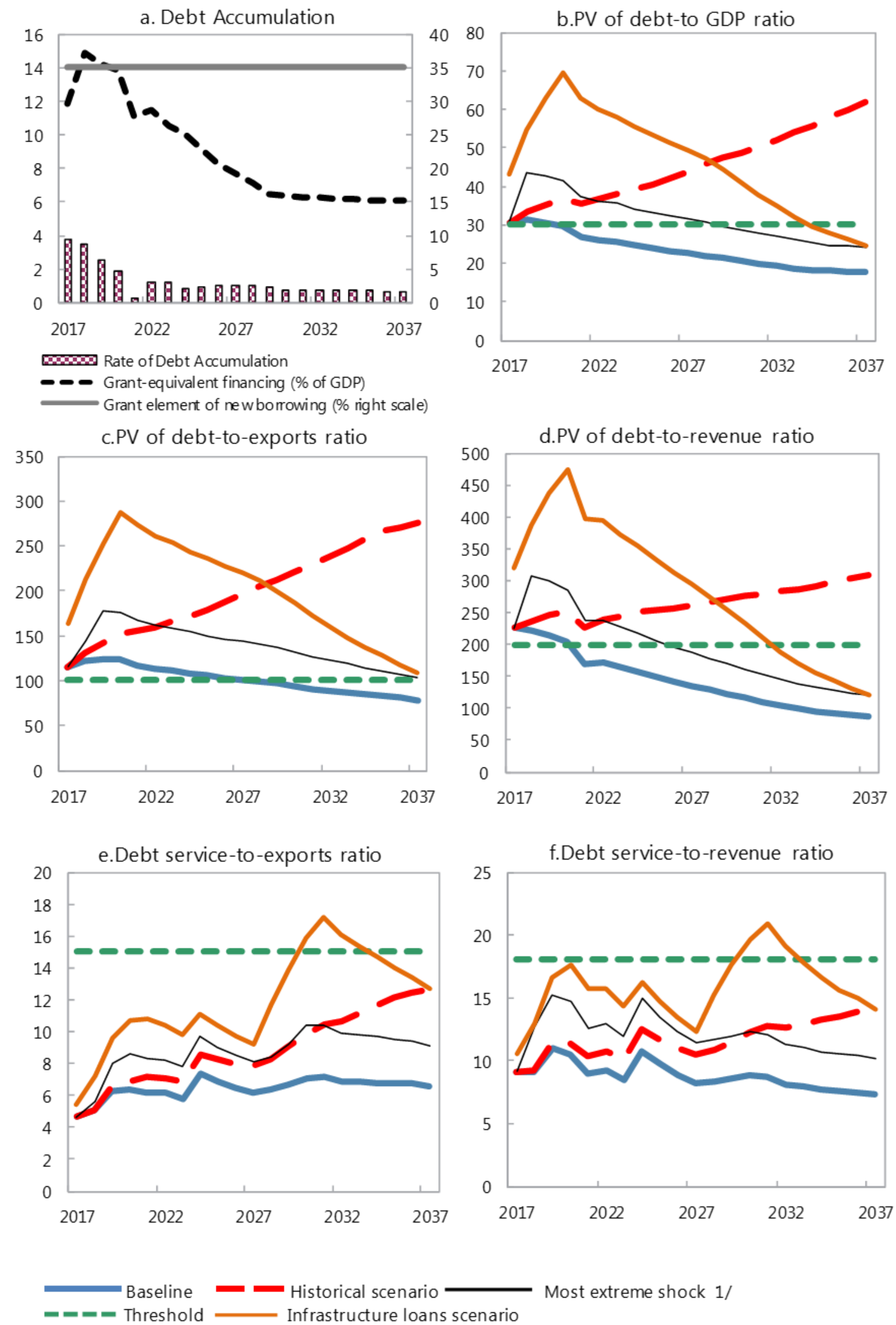
[3] EMAE's debt to ENCO is about 18 percent of GDP as of June 2017.

Additionally, with respect to the public investment plan, priority should be given to projects which would help generate high growth and employment as well as exports to help ensure debt service capacity in the future.

14. The existence of post-HIPC sovereign arrears (totaling 2 percent of GDP) to Angola, Brazil, and Equatorial Guinea would technically place São Tomé and Príncipe in debt distress. However, given assurances from these creditors that a regularization of the arrears, via a consensual process, is imminent, staff considers a high risk of debt distress rating to be more appropriate.

15. Authorities' views: In response to the staff presentation of this analysis in October 2017, the authorities reiterated their commitment to strive for debt sustainability and to actively seek restructuring of the current arrears. The authorities noted that the DSA results depend on uncertain macroeconomic assumptions and suggested that under a customized scenario with large infrastructure projects the growth rate could be higher than assumed, leading to a higher debt-carrying capacity. In this context, the authorities highlighted the need to allow for adjustment of the indicative limit for concessional borrowing for key projects that could unlock growth potential.

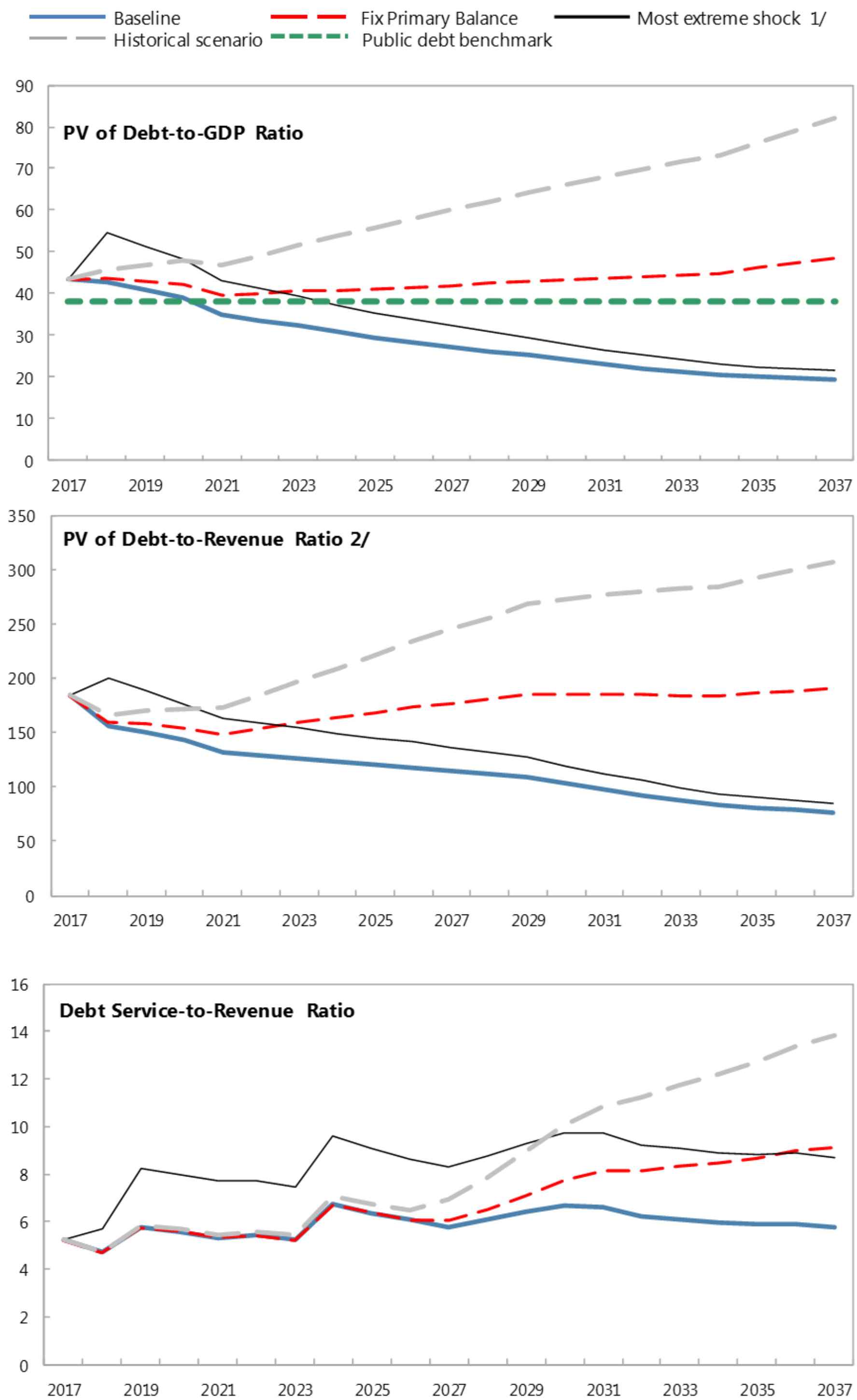
Figure 1. São Tomé and Príncipe: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2017–37



Sources: São Tomé and Príncipe's authorities, and IMF staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2027.

Figure 2. São Tomé and Príncipe: Indicators of Public Debt Under Alternative Scenarios, 2017–37



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2027.

2/ Revenues are defined inclusive of grants.

Table 1. São Tomé and Príncipe: External Debt Sustainability Framework, Baseline Scenario, 2014–37

(Percent of GDP, unless otherwise indicated)

	Actual			Historical [6/] Average	Standard [6/] Deviation	Projections									
	2014	2015	2016			2017	2018	2019	2020	2021	2022	2017-2022 Average	2027	2037	2023-2037 Average
External debt (nominal) 1/	**51.4**	**62.4**	**53.0**			**49.9**	**49.7**	**48.0**	**45.9**	**40.5**	**38.8**		**31.8**	**24.3**	
of which: public and publicly guaranteed (PPG)	51.4	62.4	53.0			49.9	49.7	48.0	45.9	40.5	38.8		31.8	24.3	
Change in external debt	7.6	11.0	-9.4			-3.1	-0.2	-1.7	-2.1	-5.4	-1.7		-1.1	-0.2	
Identified net debt-creating flows	9.6	9.5	-5.8			-1.2	2.3	1.8	1.1	3.0	1.3		0.1	-2.4	
Non-interest current account deficit	**21.6**	**12.3**	**5.7**	**21.1**	**8.5**	**11.7**	**6.7**	**6.4**	**5.6**	**7.5**	**5.7**		**4.1**	**1.4**	3.4
Deficit in balance of goods and services	40.6	30.6	25.6			27.4	25.5	24.5	23.5	23.1	21.2		16.0	12.0	
Exports	25.4	28.3	27.5			26.4	25.5	24.9	24.2	22.9	23.0		22.4	22.5	
Imports	66.0	58.9	53.1			53.8	51.0	49.4	47.6	46.0	44.2		38.4	34.5	
Net current transfers (negative = inflow)	-17.0	-18.3	-19.3	-20.2	3.7	-14.6	-17.7	-17.0	-16.8	-14.7	-14.6		-11.0	-9.9	-10.7
of which: official	-10.3	-12.6	-14.8			-10.1	-13.3	-12.9	-12.8	-10.9	-10.7		-7.0	-5.3	
Other current account flows (negative = net inflow)	-2.0	0.0	-0.5			-1.1	-1.1	-1.1	-1.1	-1.0	-0.9		-0.9	-0.8	
Net FDI (negative = inflow)	**-6.6**	**-8.1**	**-5.9**	**-14.0**	**12.2**	**-11.4**	**-2.7**	**-2.7**	**-2.7**	**-2.8**	**-2.8**		**-2.8**	**-2.9**	-2.9
Endogenous debt dynamics 2/	**-5.4**	**5.3**	**-5.6**			**-1.5**	**-1.7**	**-1.9**	**-1.8**	**-1.7**	**-1.6**		**-1.2**	**-0.8**	
Contribution from nominal interest rate	0.3	0.3	0.3			0.5	0.5	0.6	0.6	0.5	0.5		0.5	0.4	
Contribution from real GDP growth	-1.6	-2.2	-2.3			-2.0	-2.2	-2.5	-2.4	-2.2	-2.1		-1.7	-1.3	
Contribution from price and exchange rate changes	-4.1	7.2	-3.6			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**-2.0**	**1.5**	**-3.6**			**-1.9**	**-2.5**	**-3.5**	**-3.2**	**-8.3**	**-3.0**		**-1.2**	**2.2**	
of which: exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	31.5			30.5	31.2	30.7	29.8	26.9	26.1		22.6	17.6	
In percent of exports	...	...	114.3			115.4	122.1	123.3	123.5	117.2	113.3		101.0	78.5	
PV of PPG external debt	**...**	**...**	**31.5**			**30.5**	**31.2**	**30.7**	**29.8**	**26.9**	**26.1**		**22.6**	**17.6**	
In percent of exports	**...**	**...**	**114.3**			**115.4**	**122.1**	**123.3**	**123.5**	**117.2**	**113.3**		**101.0**	**78.5**	
In percent of government revenues	**...**	**...**	**229.6**			**225.4**	**220.4**	**213.8**	**203.7**	**170.1**	**170.9**		**135.1**	**87.6**	
Debt service-to-exports ratio (in percent)	**3.7**	**3.8**	**3.3**			**4.7**	**5.1**	**6.3**	**6.4**	**6.2**	**6.1**		**6.1**	**6.5**	
PPG debt service-to-exports ratio (in percent)	**3.7**	**3.8**	**3.3**			**4.7**	**5.1**	**6.3**	**6.4**	**6.2**	**6.1**		**6.1**	**6.5**	
PPG debt service-to-revenue ratio (in percent)	**6.5**	**7.8**	**6.6**			**9.1**	**9.1**	**10.9**	**10.5**	**9.0**	**9.2**		**8.2**	**7.3**	
Total gross financing need (Billions of U.S. dollars)	0.1	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Non-interest current account deficit that stabilizes debt ratio	13.9	1.3	15.1			14.8	6.9	8.1	7.8	12.8	7.4		5.3	1.5	
Key macroeconomic assumptions															
Real GDP growth (in percent)	4.1	4.0	4.1	4.3	1.8	4.0	5.0	5.5	5.5	5.5	5.5	5.2	5.5	5.5	5.5
GDP deflator in US dollar terms (change in percent)	10.5	-12.3	6.1	5.5	9.1	2.8	6.1	4.3	3.8	6.5	2.1	4.3	1.7	-0.4	1.3
Effective interest rate (percent) 5/	0.8	0.6	0.5	0.7	0.3	1.1	1.2	1.2	1.3	1.3	1.3	1.2	1.6	1.9	1.7
Growth of exports of G&S (US dollar terms, in percent)	64.3	1.7	7.4	21.9	25.4	2.7	7.6	7.3	6.3	6.5	8.4	6.5	6.7	6.7	6.7
Growth of imports of G&S (US dollar terms, in percent)	28.8	-18.6	-0.4	9.6	19.6	8.4	5.6	6.5	5.6	8.6	3.5	6.4	4.5	5.3	5.1
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	34.9	34.9	34.9	34.9	34.9	34.9	34.9	34.9	34.9	34.9
Government revenues (excluding grants, in percent of GDP)	14.5	13.9	13.7			13.5	14.1	14.4	14.7	15.8	15.3		16.8	20.1	17.8
Aid flows (in Billions of US dollars) 7/	0.1	0.1	0.1			0.1	0.1	0.1	0.1	0.1	0.1		0.1	0.1	
of which: Grants	0.0	0.0	0.1			0.0	0.1	0.1	0.1	0.1	0.1		0.1	0.1	
of which: Concessional loans	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			11.8	14.9	14.2	13.8	11.1	11.4		7.7	6.0	7.3
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			78.2	83.1	85.1	88.1	96.8	89.8		85.5	82.3	84.4
Memorandum items:															
Nominal GDP (Billions of US dollars)	0.3	0.3	0.4			0.4	0.4	0.5	0.5	0.6	0.6		0.9	1.7	
Nominal dollar GDP growth	15.0	-8.8	10.4			6.9	11.4	10.1	9.5	12.3	7.7	9.7	7.3	5.0	6.9
PV of PPG external debt (in Billions of US dollars)			0.1			0.1	0.1	0.1	0.2	0.2	0.2		0.2	0.3	
(PVt-PVt-1)/GDPt-1 (in percent)						3.7	3.5	2.6	1.9	0.3	1.2	2.2	1.1	0.7	0.9
Gross workers' remittances (Billions of US dollars)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.1	
PV of PPG external debt (in percent of GDP + remittances)	...	...	30.1			29.2	29.9	29.5	28.7	25.9	25.2		21.8	16.9	
PV of PPG external debt (in percent of exports + remittances)	...	...	98.1			98.5	104.0	105.9	106.2	100.5	97.2		85.7	65.2	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	2.8			4.0	4.3	5.4	5.5	5.3	5.3		5.2	5.4	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2a. São Tomé and Príncipe: Sensitivity Analysis of Key Indicators of Public and Publicly Guaranteed External Debt, 2017–37
(Percent)

	Projections							
	2017	2018	2019	2020	2021	2022	**2027**	2037
PV of debt-to GDP ratio								
Baseline	31	31	31	30	27	26	**23**	18
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	31	34	35	37	36	37	**44**	62
A2. New public sector loans on less favorable terms in 2017-2037 2	31	32	33	32	29	29	**27**	26
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	31	32	32	31	28	27	**24**	18
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	31	33	36	34	31	30	**26**	19
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	31	34	37	36	32	31	**27**	21
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	31	33	33	32	29	28	**24**	18
B5. Combination of B1-B4 using one-half standard deviation shocks	31	30	28	27	24	24	**21**	18
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	31	44	43	42	37	36	**31**	24
PV of debt-to-exports ratio								
Baseline	115	122	123	123	117	113	**101**	79
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	115	131	141	152	155	159	**195**	275
A2. New public sector loans on less favorable terms in 2017-2037 2	115	127	131	134	128	126	**122**	114
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	115	122	123	123	117	113	**101**	77
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	115	144	177	176	168	162	**144**	103
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	115	122	123	123	117	113	**101**	77
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	115	127	132	132	125	121	**107**	80
B5. Combination of B1-B4 using one-half standard deviation shocks	115	109	97	97	92	88	**79**	68
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	115	122	123	123	117	113	**101**	77
PV of debt-to-revenue ratio								
Baseline	225	220	214	204	170	171	**135**	88
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	225	237	245	251	225	240	**262**	307
A2. New public sector loans on less favorable terms in 2017-2037 2	225	229	228	221	186	189	**163**	127
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	225	226	226	214	179	179	**142**	91
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	225	233	247	234	196	197	**155**	93
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	225	243	255	242	202	203	**160**	103
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	225	230	229	217	181	182	**144**	89
B5. Combination of B1-B4 using one-half standard deviation shocks	225	213	195	186	155	155	**123**	88
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	225	308	299	284	237	237	**188**	120

Table 2b. São Tomé and Príncipe: Sensitivity Analysis of Key Indicators of Public and Publicly Guaranteed External Debt, 2017–2037 (concluded)

(Percent)

	Projections							
	2017	2018	2019	2020	2021	2022	**2027**	2037
Debt service-to-exports ratio								
Baseline	5	5	6	6	6	6	**6**	7
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	5	5	7	7	7	7	**8**	13
A2. New public sector loans on less favorable terms in 2017-2037 2	5	5	6	7	7	7	**7**	9
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	5	5	6	6	6	6	**6**	7
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	5	6	8	9	8	8	**8**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	5	5	6	6	6	6	**6**	7
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	5	5	6	7	6	6	**6**	7
B5. Combination of B1-B4 using one-half standard deviation shocks	5	5	6	6	5	5	**5**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	5	5	6	6	6	6	**6**	7
Debt service-to-revenue ratio								
Baseline	9	9	11	11	9	9	**8**	7
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	9	9	11	11	10	11	**11**	14
A2. New public sector loans on less favorable terms in 2017-2037 2	9	9	11	11	10	10	**10**	10
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	9	9	12	11	9	10	**9**	8
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	9	9	11	11	10	10	**9**	8
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	9	10	13	13	11	11	**10**	9
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	9	9	11	11	9	10	**8**	8
B5. Combination of B1-B4 using one-half standard deviation shocks	9	10	12	11	9	9	**8**	7
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	9	13	15	15	13	13	**11**	10
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	35	35	35	35	35	35	**35**	35

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 3. São Tomé and Príncipe: Public Sector Debt Sustainability Framework, Baseline Scenario, 2014–2037

(Percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2014	2015	2016	Average 5/	Standard Deviation 5/	2017	2018	2019	2020	2021	2022	2017-22 Average	2027	2037	2023-37 Average
Public sector debt 1/	51.4	62.4	68.2			62.8	61.3	58.4	55.2	48.6	46.2		36.4	26.1	
of which: foreign-currency denominated	51.4	62.4	53.0			49.9	49.7	48.0	45.9	40.5	38.8		31.8	24.3	
Change in public sector debt	7.6	11.0	5.9			-5.5	-1.4	-3.0	-3.2	-6.5	-2.5		-1.6	-0.3	
Identified debt-creating flows	5.3	10.0	0.1			-2.4	-1.7	-1.6	-1.8	-4.1	-2.5		-1.1	-0.6	
Primary deficit	5.6	8.6	3.3	9.3	6.1	5.4	2.8	3.4	2.5	1.1	0.5	2.6	1.0	0.3	0.5
Revenue and grants	24.5	25.4	28.5			23.6	27.4	27.2	27.5	26.7	26.0		23.7	25.5	
of which: grants	10.0	11.5	14.8			10.1	13.3	12.9	12.8	10.9	10.7		7.0	5.3	
Primary (noninterest) expenditure	30.1	34.0	31.8			29.0	30.2	30.6	30.0	27.8	26.5		24.7	25.8	
Automatic debt dynamics	-0.3	1.4	-3.2			-7.8	-4.5	-5.0	-4.4	-5.2	-2.9		-2.1	-0.9	
Contribution from interest rate/growth differential	-2.1	-2.2	-2.7			-3.3	-3.8	-4.0	-3.7	-3.5	-3.0		-2.3	-1.5	
of which: contribution from average real interest rate	-0.3	-0.2	-0.2			-0.6	-0.8	-0.8	-0.7	-0.6	-0.5		-0.3	-0.1	
of which: contribution from real GDP growth	-1.7	-2.0	-2.5			-2.6	-3.0	-3.2	-3.0	-2.9	-2.5		-2.0	-1.4	
Contribution from real exchange rate depreciation	1.7	3.5	-0.5			-4.5	-0.7	-1.0	-0.7	-1.8	0.1		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	2.3	1.0	5.7			-3.1	0.3	-1.3	-1.4	-2.4	0.0		-0.4	0.2	
Other Sustainability Indicators															
PV of public sector debt	...	...	46.7			43.4	42.8	41.0	39.1	34.9	33.5		27.2	19.4	
of which: foreign-currency denominated	...	...	31.5			30.5	31.2	30.7	29.8	26.9	26.1		22.6	17.6	
of which: external	...	...	31.5			30.5	31.2	30.7	29.8	26.9	26.1		22.6	17.6	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	6.6	9.7	4.2			6.7	4.1	4.9	4.1	2.5	1.9		2.4	1.8	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	163.9			183.9	156.0	150.7	142.3	130.9	128.6		114.8	76.4	
PV of public sector debt-to-revenue ratio (in percent)	...	...	341.0			320.6	302.5	285.8	266.9	221.2	219.0		162.5	96.6	
of which: external 3/	...	...	229.6			225.4	220.4	213.8	203.7	170.1	170.9		135.1	87.6	
Debt service-to-revenue and grants ratio (in percent) 4/	3.9	4.3	3.2			5.2	4.7	5.8	5.6	5.3	5.4		5.8	5.8	
Debt service-to-revenue ratio (in percent) 4/	6.5	7.8	6.6			9.1	9.1	10.9	10.5	9.0	9.2		8.2	7.3	
Primary deficit that stabilizes the debt-to-GDP ratio	-2.0	-2.4	-2.5			10.9	4.2	6.3	5.7	7.7	2.9		2.6	0.7	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	4.1	4.0	4.1	4.3	1.8	4.0	5.0	5.5	5.5	5.5	5.5	5.2	5.5	5.5	5.5
Average nominal interest rate on forex debt (in percent)	0.8	0.6	0.5	0.7	0.3	1.1	1.2	1.2	1.3	1.3	1.3	1.2	1.6	1.9	1.7
Average real interest rate on domestic debt (in percent)	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Real exchange rate depreciation (in percent, + indicates depreciation)	4.2	7.2	-0.9	-3.0	7.7	...	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	10.6	4.9	6.3	11.5	6.6	2.7	3.5	4.0	3.7	3.0	2.8	3.3	2.6	2.6	2.6
Growth of real primary spending (deflated by GDP deflator, in percent)	0.6	17.2	-2.4	1.6	5.5	-5.1	9.3	6.8	3.5	-2.2	0.5	2.1	4.3	6.7	5.3
Grant element of new external borrowing (in percent)	...	...	...	...	...	34.9	34.9	34.9	34.9	34.9	34.9	34.9	34.9	34.9	...

Sources: Country authorities; and staff estimates and projections.

1/ Public debt consists of central government debt. Gross debt is considered.

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4. São Tomé and Príncipe: Sensitivity Analysis of Key Indicators of Public Debt, 2017–37

	Projections							
	2017	2018	2019	2020	2021	2022	2027	2037
PV of Debt-to-GDP Ratio								
Baseline	43	43	41	39	35	33	27	19
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	43	46	47	48	47	49	60	82
A2. Primary balance is unchanged from 2017	43	44	43	42	39	40	42	49
A3. Permanently lower GDP growth 1/	43	43	41	40	36	34	29	26
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	43	44	44	42	38	37	32	26
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	43	48	51	49	44	42	35	24
B3. Combination of B1-B2 using one half standard deviation shocks	43	47	50	48	43	42	36	27
B4. One-time 30 percent real depreciation in 2018	43	55	51	48	43	41	32	22
B5. 10 percent of GDP increase in other debt-creating flows in 2018	43	47	45	43	38	37	30	21
PV of Debt-to-Revenue Ratio 2/								
Baseline	184	156	151	142	131	129	115	76
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	184	166	170	171	173	185	245	306
A2. Primary balance is unchanged from 2017	184	160	158	153	148	153	177	191
A3. Permanently lower GDP growth 1/	184	156	151	144	133	131	123	101
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	184	158	156	149	139	138	131	102
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	184	175	187	177	164	162	147	93
B3. Combination of B1-B2 using one half standard deviation shocks	184	171	180	171	160	158	149	106
B4. One-time 30 percent real depreciation in 2018	184	199	189	176	162	158	136	85
B5. 10 percent of GDP increase in other debt-creating flows in 2018	184	171	165	156	144	142	127	83
Debt Service-to-Revenue Ratio 2/								
Baseline	5	5	6	6	5	5	6	6
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	5	5	6	6	5	6	7	14
A2. Primary balance is unchanged from 2017	5	5	6	6	5	5	6	9
A3. Permanently lower GDP growth 1/	5	5	6	6	5	5	6	6
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	5	5	6	6	5	6	6	7
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	5	5	6	6	5	5	7	7
B3. Combination of B1-B2 using one half standard deviation shocks	5	5	6	6	5	6	7	7
B4. One-time 30 percent real depreciation in 2018	5	6	8	8	8	8	8	9
B5. 10 percent of GDP increase in other debt-creating flows in 2018	5	5	6	6	5	5	7	6

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Statement by Mr. Sembene, Executive Director, Mr. Nguema-Affane, Senior Advisor, and Mr. Carvalho da Silveira, Advisor, on Democratic Republic of Sao Tome and Principe

December 11, 2017

On behalf of the Sao Tomean authorities, we would like to thank staff for their candid report and the constructive policy dialogue held with the authorities in the context of the third and fourth ECF reviews. The authorities broadly agree with staff's assessment of macroeconomic challenges and welcome the policy recommendations.

The ECF-supported program has been instrumental in helping Sao Tome and Principe to maintain macroeconomic stability, unlock financing from other partners, and advance the needed reform agenda amidst decreasing external support, delays in the provision of technical assistance (TA), weak capacities, and high debt levels. While this challenging environment held back the implementation of some reforms, noticeable progress was made to achieve the broad objectives of the program.

Performance under the Program and Recent Economic Developments

Program performance since the last review was solid. All five end-June 2017 performance criteria (PCs) were met, including those related to net international reserves and net bank financing. On the structural front, three end-December 2016 structural benchmarks were implemented, with the aim of strengthening the financial situation of the state-owned electricity and water utilities company (EMAE), and strengthening monetary and financial policy frameworks. However, three were missed, largely because of weak capacities and developments outside the authorities' control. Other structural benchmarks that were missed are still on the authorities' agenda, notably the submission to the National Assembly of draft legislations on a new VAT and the completion of a Public Investment Management Assessment (PIMA). The two end-December 2017 structural benchmark on the submission of a draft public private partnership (PPP) and adoption of measures to contain EMAE's loss in the short-term have now been implemented.

Real GDP recorded another year of growth above 4% in 2016, underpinned by strong activity in the cocoa, tourism and construction sectors, and preliminary information indicate that economic activity remained buoyant in the first half of 2017. Inflation rose from 5.1 percent at end-December 2016 to 6.5 percent at end-August 2017, driven by increased prices of locally-produced goods resulting from heavier rainfall. After improving in 2016, the current account deficit widened in the first half of 2017 due to the increased imports of capital goods and oil product and was financed by higher FDI. The external position continues to be adequate with net international reserves at about 3.5 months of imports.

Outlook for the Rest of 2017 and Onwards

Sao Tome and Principe's near-to-medium term outlook is favorable but remains subject to significant downward risks. GDP growth is projected to continue to grow at around 4 percent in 2017, and this momentum is expected to be maintained in the medium term, boosted by strong activities in construction and tourism, as key infrastructure projects such as the airport expansion and hydroelectric plants come to life. The current account deficit is expected to continue to worsen in 2017 and in the medium term, as FDI related to large infrastructures project are projected to remain high. Inflation would moderate, as inflationary pressures from temporary food shortages fade away. The authorities agree that further delays in external financing and reform implementation due to capacity constraints and the upcoming legislative elections represent major downside risks to the outlook. Going forward, the authorities remain committed to taking necessary actions to enhance economic resilience and maintain the strong growth momentum and appreciate the continued close engagement with the Fund in this regard.

Policy and Reform Agenda

Our Sao Tomean authorities remain fully committed to the objectives of the ECF-supported program. Going forward, they will focus on ensuring greater fiscal discipline, strengthening the monetary policy framework, safeguarding financial sector stability, and advancing their structural reform program.

Ensuring fiscal discipline

After missing end-2016 primary deficit targets, the authorities issued a 2017 revised budget to put fiscal accounts back on track. The corrective measures that were implemented included, among others, (i) spending cuts of 30% on fuel by Government agencies, except for police, defense and health sectors, and (ii) reduction of 30% in salary top-ups and all other benefits at State-Owned Enterprises (SOEs) and autonomous agencies. In addition, an agreement was reached with two large private debtors and a few SOEs on gradually clearing their tax arrears. As a result, the domestic primary deficit (DPD) target narrowed down to 1.4 percent of GDP in line with the associated target for June 2017. As the outturns at end-August were lower than expected due to unforeseen developments, further measures were identified to close the resulting gap of 2.4 percent of GDP. These include planned arrears collection efforts which will help mobilize about 1 percent of GDP and additional expenditure cuts totaling 1.4 percent of GDP.

Sao Tome and Principe continues to be assessed at high risk of debt distress. The country's debt to GDP ratio has been revised up due to the inclusion of domestic arrears for the first time. Nevertheless, external debt to GDP ratio is expected to be 46 percent at end 2017, down from 62 percent in 2015-16. The authorities secured an agreement with China involving debt forgiveness for Sao Tome in the amount of $18.4 million in pre-HIPIC legacy arrears. They are also working towards reaching a debt rescheduling agreement regarding external arrears accumulated with other creditors. As noted in the report, the authorities also remain fully committed to reducing arrears and concurred to prioritize the payment if additional resources are mobilized. Looking ahead, the authorities reiterate their commitment to avoid accumulation of new arrears in 2017 and limit their external borrowing to concessional loans.

In line with the DPD target of 1 percent of GDP in 2018, the authorities have submitted to the Parliament the 2018 budget, which lays out their planned fiscal consolidation efforts. This budget includes both revenue-enhancing and expenditures-controlling measures, including the suspension of the personal income tax credit, wage growth freeze, and constrained hiring in nonpriority sectors.

On structural fiscal reforms, the authorities remain determined to pursue their fiscal consolidation efforts through revenue mobilization. Prompt steps will be taken to finalize the VAT law. In this connection, Fund technical assistance will be critical in setting up a single Tax Authority in the country. The authorities are also making progress in completing the Public Private Partnership (PPP) law which should support efforts in capacity building for efficient public investment decision making. The adoption of the automatic price adjustment mechanism has been serving the country well thus far and should help reduce fiscal risks.

The authorities will pursue the restructuring of the SOEs. In this regard, reforming EMAE is at the top of the authorities' agenda, given the risk it poses to the government finances. As noted in the staff report, major projects are underway to revamp EMAE in the medium-term, with the assistance of the World Bank and the European Investment Bank. In the short-term, the authorities have taken steps to contains fiscal risks, notably by (i) ensuring ministries and agencies pay electricity bills regularly; (ii) reaching an agreement with consumers with arrears; (iii) enforcing antitheft legislation; (iv) publishing the list of debtors of EMAE; (v) expanding payment of bills through the banking system.

Strengthening the monetary policy framework and safeguarding financial sector stability

The authorities have been making inroads in improving further the monetary policy framework and securing financial stability in recent years. However, they continue to face a number of challenges, including excess liquidity, anemic credit growth and high levels of NPLs. To address them, the BCSTP is currently working on the amendment of regulations that are required for the operation of a secondary market as well as longer-term instruments, while promoting transparent public reporting of banks' audited financial statements.

On November 2017, the Parliament approved the monetary reform law which will allow the redenomination of the currency to become effective on January 1, 2018. The authorities believe that the redenomination of the currency will be an important step toward improving money circulation, streamlining accounting and settlements, maintaining the optimal structure of money denominations, reducing public expenditures on servicing cash circulation, and combating counterfeiting. Preparation for this initiative has begun a while ago and the BCSTP is currently embarked on its final stages, notably by undertaking a number of awareness campaigns.

Financial soundness indicators improved in 2017. The capital adequacy ratio increased well above regulatory requirements, profitability rose, and NPL of banking institutions declined. Notwithstanding these positive developments, the authorities will continue their efforts towards financial sector reforms. To this end, the authorities have recently implemented the Financial Sector Development Implementation Plan, the BCSTP Strategic Plan and the NPL reduction strategy. The Asset Quality Review (AQR) was launched, the risk-based supervision will be revamped with TA from the Fund, and steps are being taken to implement the International Financial Reporting Standards with the support of the Central Bank of Brazil. Progress was also made toward developing an out-of-court settlement mechanism.

The liquidation of Banco Equador is advancing, and the authorities will continue to monitor closely the process notably with a view to containing fiscal risks.

Advancing Other Structural Reforms

The authorities reaffirm their commitment to operationalizing the 2030 Transformation Agenda. In this connection, the National Development Plan (NDP) 2017 – 2021 was completed and implemented in November 2017 with the support of the UNDP. The plan remains aligned with the sustainable development goals, and focused on accelerating sustainable growth, and strengthening social cohesion and the country's credibility abroad. Moreover, with the support of the World Bank, the authorities are finalizing a national export diversification strategy focused on tourism growth, and taking steps to address the unreliable supply and the high cost of electricity.

Concluding remarks

Notwithstanding the daunting policy challenges facing the country, the Sao Tomean authorities have shown a firm commitment to the program by implementing difficult corrective measures to keep the program on track. The Fund continued engagement will act as an important catalyst for other lenders, while providing an appropriate anchor for reforms aimed at achieving macroeconomic stability. The authorities welcome the Fund's valuable technical assistance and look forward to the institution's timely support for their capacity building efforts.

In light of the above, we would greatly appreciate Directors' support for the completion of the third and fourth reviews under the ECF and the authorities' request for extension of the arrangement and modification of performance criteria.