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REPUBLIC OF MADAGASCAR

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2019 ARTICLE IV CONSULTATION AND SIXTH REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR REPUBLIC OF MADAGASCAR

In the context of the Staff Report for the 2019 Article IV Consultation and Sixth Review Under the Extended Credit Facility Arrangement, 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 and summarizing the views of the Executive Board as expressed during its January 29, 2020 consideration of the staff report on issues related to the Article IV Consultation and the IMF arrangement.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on January 29, 2020, following discussions that ended on November 25, 2019, with the officials of the Republic of Madagascar on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on January 14, 2020.
- 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 Republic of Madagascar.

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

Letter of Intent sent to the IMF by the authorities of the Republic of Madagascar*
Memorandum of Economic and Financial Policies by the authorities of the Republic of Madagascar*
Technical Memorandum of Understanding*
Selected Issues

*Also included in Staff Report

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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COMMUNICATIONS DEPARTMENT

Press Release No. 20/25
FOR IMMEDIATE RELEASE
January 30, 2020

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Washington, D.C. 20431 USA

IMF Executive Board Completes Sixth Review Under the Extended Credit Facility (ECF) for the Republic of Madagascar and Concludes 2019 Article IV Consultation

On January 29, 2020, the Executive Board of the International Monetary Fund completed the sixth review under the ECF arrangement for Madagascar and the 2019 Article IV consultation. The completion of this review enables the disbursement of SDR 31.43 million (about US$43.2 million), bringing total disbursements under the arrangement to SDR 250.55 million (about US$344.5 million).

Madagascar's 40 month-ECF arrangement to support the country's efforts to reinforce macroeconomic stability and boost sustained and inclusive growth, was approved on July 27, 2016 (see Press Release No.16/370) for SDR 220 million (about US$305 million, or 90 percent of Madagascar's quota). Additional access of 12.5 percent of Madagascar's quota was approved by the Executive Board in June 28, 2017, bringing access to SDR250.55 million (about US$347 million) at that time. The Executive Board approved, in November 4, 2019, the authorities' request for a three-month Extension of the ECF arrangement to February 26, 2020, to allow time to conclude the discussions to complete the 6th and last review.

Following the Executive Board discussion, Mr. Mitsuhiro Furusawa, Deputy Managing Director and Acting Chair, made the following statement:

"Madagascar's performance under its economic program supported by the Extended Credit Facility (ECF) arrangement has been broadly satisfactory with solid growth, moderate single-digit inflation, and a robust external position. Going forward, a commitment to strong policies and an ambitious agenda to complete outstanding structural reforms remains crucial to mitigate internal and external risks, strengthen macroeconomic stability, and achieve higher, sustainable, and inclusive growth.

"The authorities' economic reform agenda summarized in the Plan Emergence Madagascar aims to raise economic growth through increased public and private investment, strengthening human capital, and improving governance. Creating additional fiscal space by further improving revenue mobilization through a medium-term tax revenue strategy, containing lower-priority spending, and enhancing investment implementation capacity is essential for scaling-up priority investment and social spending in education, health, and housing.

"Resolute actions are needed to contain risks to macroeconomic stability and debt sustainability, including reducing fiscal risks from the financial situation of the public utility JIRAMA and containing liabilities to fuel distributors. On the latter, the implementation of an automatic fuel pricing mechanism to avoid budget costs must be accompanied by mitigating measures to limit impact on the poorest, including by the on-going scaling up of social safety net programs.

"Effective and impartial enforcement of the new anti-corruption legal framework, now closer to international standards, is needed to improve the business climate and attract private investment. Continued progress to further strengthen public financial management is necessary to improve the governance of public resources. Measures to increase resilience to natural disasters also need to be prioritized.

"The authorities' ongoing reform agenda should continue to benefit from continued IMF engagement, including technical assistance."

The Executive Board also concluded the 2019 Article IV Consultation[1] with the Republic of Madagascar.

Madagascar is a low-income country facing important challenges to overcome fragilities, strengthen inclusive growth, and address long-standing development needs. Progress in macro-economic performance and structural agenda during the recent years has been supported by the 2016 ECF arrangement. After a smooth transition of power following the Presidential elections, and the conclusion of the Parliamentary elections in end-May economic developments have remained favorable with sustained growth, contained inflation, and sustainable fiscal and external positions.

The medium-term economic outlook remains favorable, with growth expected to gradually increase to about 5.5 percent, supported by public investment scaling-up and good prospects for private investment. The outlook remains subject to risks, however, associated with social fragility, materialization of fiscal risks, and vulnerability to exogenous shocks including to terms of trade and natural disasters.

In this context, renewed efforts and impetus for reforms, in line with the government's ambitious development strategy formalized in its Plan Emergence Madagascar, are needed to create fiscal space to finance investment and raise social spending; strengthen monetary and exchange rate policy effectiveness; improve financial sector development and resilience; and promote better governance and an improved business climate.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment[2]

Executive Directors welcomed the broadly satisfactory implementation of the economic reform program and peaceful political transition followed by solid macroeconomic performance. However, they regretted the slowdown in progress on structural reforms and continued underperformance on priority social spending. In light of Madagascar's long-standing challenges of high poverty, stagnant per capita income and vulnerability to natural disasters, Directors emphasized the need for further efforts to bring Madagascar onto a path of sustainable and inclusive growth. In this regard, they welcomed the authorities' ambitious development agenda summarized in the Plan Emergence Madagascar and their commitment to strengthen macroeconomic stability and debt sustainability and implement outstanding reforms. Directors noted that enhanced capacity development will be essential to support the authorities' objectives and welcomed the intention to start discussions on a successor arrangement.

Directors emphasized that fiscal policy should remain focused on efforts to create fiscal space to allow for scaling up of priority social and investment spending, notably in education, health and housing. In this context, they encouraged the authorities to continue their efforts to improve revenue mobilization through credible medium-term tax revenue mobilization plans, containment of lower-priority spending, and enhancement of the investment implementation capacity. To contain risks to macroeconomic stability and debt sustainability, Directors called for reducing transfers to the public utility company JIRAMA and finalizing and implementing its medium-term recovery plan, improving the sustainability of the civil servant pension fund, and containing liabilities to fuel distributors. They also encouraged the authorities to adopt the planned fuel pricing mechanism without further delays, while putting in place mitigating measures and social safety nets to limit the impact on the poorest.

Directors welcomed continued progress in improving the monetary framework and strengthening the financial sector. They called for continued efforts to improve foreign exchange market operations and gradually phase out the surrender requirement on export proceeds, as well as further steps to strengthen the bank supervisory framework. They encouraged the authorities to implement the new banking and financial stability laws, and to continue their efforts to improve financial inclusion.

Directors welcomed progress on governance reforms and the anti-corruption legal framework, and they urged its effective and impartial enforcement in order to strengthen the business climate and attract private investment. Directors also called for continued efforts to strengthen public financial management and for prioritizing measures to increase resilience to natural disasters.

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Table 1. Selected Economic Indicators, 2017-21

	2017	2018	2019	2020	2021
	Est.		Proj.		
	(Percent change; unless otherwise indicated)				
National account and prices					
GDP at constant prices	3.9	4.6	4.8	5.2	5.4
GDP deflator	8.6	8.6	5.9	7.2	6.5
Consumer prices (end of period)	10.6	6.9	6.0	6.2	5.9
Money and credit					
Broad money (M3)	17.8	11.2	12.3	16.2	14.9
	(Growth in percent of beginning of period money stock (M3))				
Net foreign assets	9.2	4.8	0.3	6.9	7.6
Net domestic assets	8.6	6.4	12.0	9.3	7.2
of which: Credit to the private sector	8.4	8.7	9.0	7.3	5.8
	(Percent of GDP)				
Public finance					
Total revenue (excluding grants)	10.3	10.5	10.6	11.2	11.7
of which: Tax revenue	10.0	10.2	10.4	10.9	11.3
Grants	2.5	2.5	2.4	2.5	1.4
of which: budget grants	0.7	0.9	0.8	0.7	0.0
Total expenditures	14.9	14.3	14.4	16.4	17.3
Current expenditure	10.2	9.3	9.3	8.9	8.9
Capital expenditure	4.7	5.0	5.0	7.6	8.3
Overall balance (commitment basis)	-2.1	-1.3	-1.4	-2.7	-4.2
Domestic primary balance[1]	-0.9	0.1	0.3	0.0	0.3
Total financing	2.0	2.0	1.7	2.7	3.8
Foreign borrowing (net)	1.2	1.5	1.2	2.2	3.3
Domestic financing	0.8	0.5	0.5	0.5	0.4
Financing gap	0.0	0.0	0.0	0.0	-0.5
Savings and investment					
Investment	18.1	18.8	19.1	22.0	23.0
Gross national savings	15.4	20.3	19.0	20.5	21.5
External sector					
Exports of goods, f.o.b.	21.3	21.9	19.5	19.0	20.1
Imports of goods, c.i.f.	27.4	27.6	26.6	27.0	27.3
Current account balance (exc. grants)	-2.9	-1.9	-2.6	-4.0	-2.9
Current account balance (inc. grants)	-0.4	0.7	-0.1	-1.5	-1.5
Public debt	40.0	39.9	40.1	39.8	40.8
External Public Debt	25.7	26.7	27.2	27.6	29.1
Domestic Public Debt	14.4	13.2	12.8	12.2	11.6
	(Units as indicated)				
Gross official reserves (millions of SDRs)	1086	1221	1238	1390	1552
Months of imports of goods and services	4.0	4.3	4.3	4.4	4.5
GDP per capita (U.S. dollars)	516	528	525	557	588

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] Primary balance excl. foreign-financed investment and grants. Commitment basis.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MADAGASCAR

January 9, 2020

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION AND SIXTH REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT

EXECUTIVE SUMMARY

Context. After a smooth transition of power completed with the Parliamentary elections in May 2019 and the installation of a new government, economic developments have remained favorable despite some slowdown in the first half of 2019, in the context of significant budget under-execution. Medium-term fiscal and external sustainability has been preserved.

Article IV consultations. There was broad agreement on policies for strengthening inclusive economic growth, especially scaling up investment and social spending; creating additional fiscal space—by boosting revenue and cutting lower priority spending; improving the monetary policy framework to promote stability and contain inflation; strengthening financial sector stability and increasing financial inclusion; and improving governance and the business climate, including by tackling corruption.

Program performance. The authorities met all end-June 2019 performance criteria, including for the domestic primary balance, the fiscal anchor of the program. Progress on the structural reform agenda has slowed during the last year of the program, with delays in several planned actions. Despite the slowing progress on the structural agenda, staff recommends the completion of the sixth and final review under the ECF arrangement based on the quantitative performance on the end-June 2019 targets and the authorities' commitment to complete the outstanding reforms. Completion of the review will lead to disbursement equivalent to SDR 31.43 million, bringing total disbursements under the program to SDR 250.55 million (about US$346 million).

Outlook and risks. The outlook is broadly positive. As a fragile, low-income country, Madagascar continues to face risks associated with weak implementation capacity, potential fiscal slippages (including losses at the public utility JIRAMA), social fragility in a context of widespread poverty, and vulnerability to exogenous shocks including to terms of trade and natural disasters. The authorities expressed their willingness to continue engagement with the IMF, including through a potential successor arrangement.

Approved By
David Owen and Zuzana Murgasova

Discussions on the authorities' economic and financial program took place in Antananarivo during November 11-25, 2019. The IMF staff team included Mr. Tsangarides (Head), Mr. Léost, and Ms. Cheptea (all AFR), Ms. Hlatshwayo (SPR), and Ms. Vu (FAD). The mission was assisted by Mr. Gerard (Resident Representative) and Ms. Rasoamanana (local economist). Mr. Nguema-Affane (OED) participated in the discussions. The IMF team met with President Rajoelina, Prime Minister Ntsay, Minister of Economy and Finance Randriamandrato, Interim Minister of Energy, Water, and Hydrocarbons Ramarolahy, outgoing Central Bank of Madagascar Governor Rasolofondraibe and new Governor Rabarijohn, senior officials, development partners, as well as representatives of the private sector and civil society.

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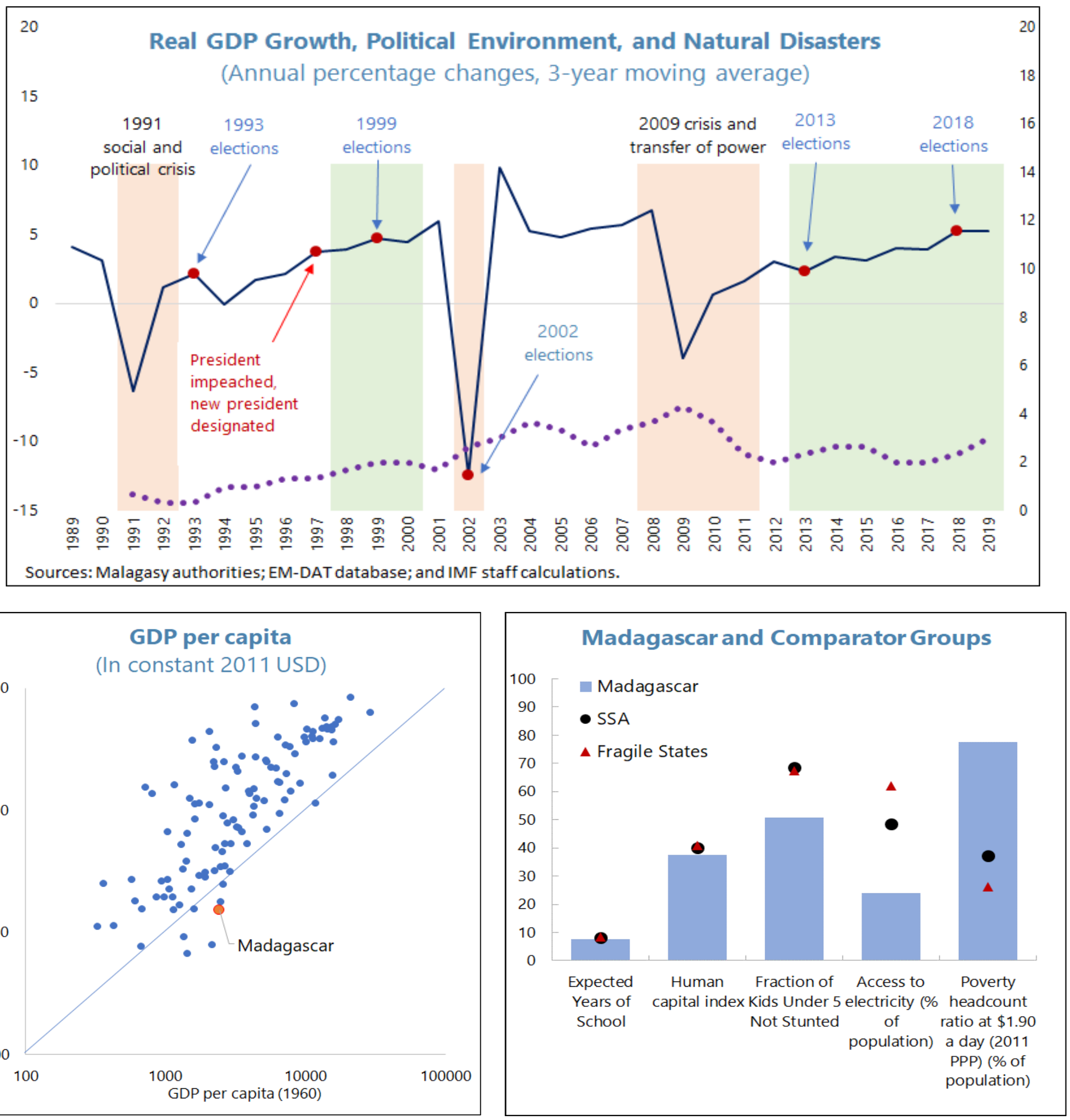
Glossary

AML/CFT	Anti-Money-Laundering and Combating the Financing of Terrorism
BFM	Central Bank (Banky Foiben'i Madagasikara)
DSA	Debt Sustainability Analysis
ECF	Extended Credit Facility
FAD	Fiscal Affairs Department
GDP	Gross Domestic Product
IFRS	International Financial Reporting Standards
IT	Indicative Target
JIRAMA	*Jiro sy rano malagasy*, public water and electricity company of Madagascar
LFR	Loi de Finances Rectificative (Revised Budget Law)
MEFP	Memorandum of Economic and Financial Policies
NDA	Net Domestic Assets
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Assets
PC	Performance Criterion
PEM	Plan Emergence Madagascar
PFM	Public Financing Management
RAM	Risk Assessment Matrix
REER	Real Effective Exchange Rate
SDGs	Sustainable Development Goals
SSA	Sub-Saharan Africa
SB	Structural Benchmark
VAT	Value Added Tax
TA	Technical Assistance
TMU	Technical Memorandum of Understanding

BACKGROUND

1. The transition of power after the election cycle proceeded smoothly. The first peaceful constitutional handover of power in decades after the Presidential election, and the conclusion of the Parliamentary elections in end-May, have strengthened political stability and begun to raise confidence. This successful transfer of power stands out in Madagascar's history considering prior recurrent episodes of political crises and associated economic volatility. The President's strong economic reform agenda formalized in the *Plan Emergence Madagascar* (PEM), aims to address long-standing development problems, raise growth, and improve living standards.

Figure 1. Madagascar: Growth and Development Outcomes



Sources: Malagasy authorities; Penn World Tables; and IMF.

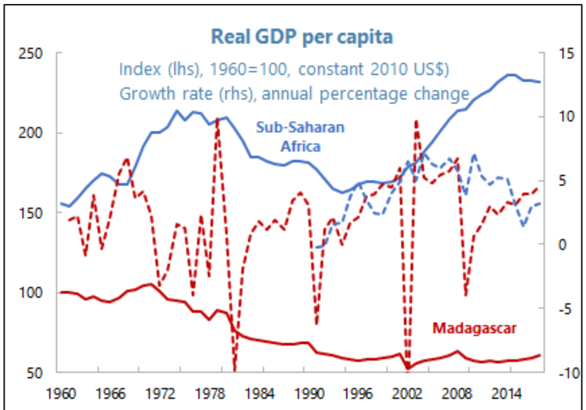
2. **Economic conditions continued to improve in 2019, and implementation of the Fund-supported program remained broadly satisfactory.** Growth continued to pick up, inflation remained moderate, the external position improved, and fiscal performance was broadly adequate despite budget execution slippages—including on social spending—partly explained by the reorganization of ministries after the Presidential election. Progress toward key program objectives has continued during the year—growth has continued to improve, inflation remains contained, tax revenue mobilization continues to increase, and international reserves have been steadily increasing—but there were mixed results in the implementation of the structural reform agenda.

3. **However, Madagascar's many dimensions of fragility present challenges for sustaining inclusive growth and improving social indicators.**[1] Historical trends of declining incomes, stagnating poverty levels, and continued exposure to natural disasters point to Madagascar's deep-rooted challenges. Madagascar is one of only eight countries with lower real per capita income today than in 1960 and its human capital is on a declining trend, jeopardizing Madagascar's potential to realize its demographic dividend afforded by a young population and declining fertility rates. With an average of three cyclones per year and several episodes of droughts and floods, Madagascar is among the countries most affected by extreme weather events and natural disasters in Africa, with an estimated cost of about 1 percent of GDP per year, on average.

4. **Progress in overcoming Madagascar's fragilities will require concerted efforts and a strong and continued reform agenda.** The authorities' PEM, whose priorities are consistent with the ECF-supported program objectives, aims to address long-standing development lags by promoting stronger, more inclusive, and more diversified growth.

RECENT ECONOMIC DEVELOPMENTS

5. **Despite a slowdown in the first half of the year, growth is expected to improve to 4.8 percent in 2019, and inflation to remain contained.** Growth accelerated in 2018 to 4.6 percent—the highest rate in 10 years. After losing some momentum in early-2019 due to weakening external demand and a wait-and-see attitude during the election period, growth has rebounded and is expected to improve to 4.8 percent for the year following a pickup in public investment execution, positive developments in mining, textile, transportation and services, rising business confidence indicators, and increased demand for private credit. Inflation has continued to steadily decelerate since its peak in late 2017 and is expected to be contained to 6 percent by end-2019.



Sources: Malagasy authorities; and IMF staff.

[1] Madagascar is a pilot for developing a Country Engagement Strategy (CES) following the 2018 Implementation Plan to strengthen IMF's engagement with fragile and conflict-affected states. Annex I summarizes the CES.

Box 1. Sustaining Madagascar's Growth Spell

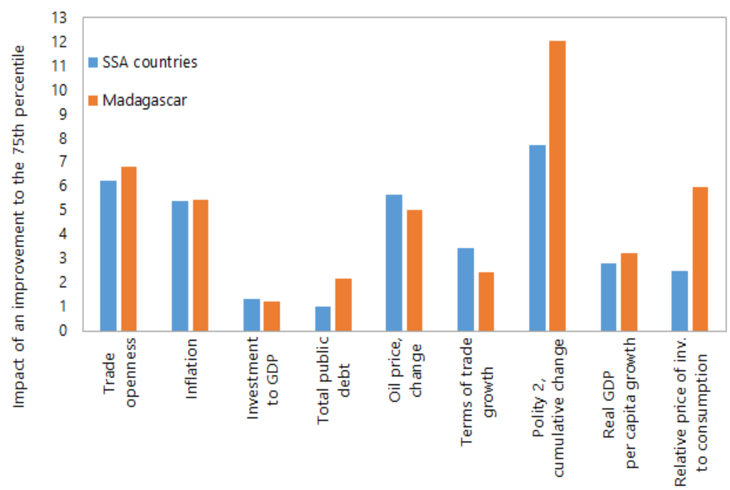
Growth in Madagascar since 1960 is generally characterized by high volatility and frequent shifts between periods of expansion and contraction. This pattern seems to have changed recently, following several years of robust economic growth and the recent peaceful transition of power. Could this be the beginning of a period of sustained growth?

A growing literature focuses on investigating turning points and the duration of sustained growth episodes or growth spells, and factors that influence these events.[1] Growth turning points are common in developing countries but from a policy perspective, growth turning points are of most interest when they lead to durable and sustained periods of growth: long-term poverty reduction and improvements in development outcomes require sustained periods of economic growth.

We investigate growth turning points and growth spells for Madagascar following the approach used in the Spring 2017 SSA Regional Economic Outlook (REO).[2] We begin by searching for structural breaks in Madagascar's economic growth, namely up-breaks—periods of higher growth than before, or growth accelerations—and down-breaks—periods of lower growth than before, or growth decelerations. An up-break can be identified in 2009, with growth after 2009 higher than the period before 2009.

Is 2009 the beginning of a growth spell? We can define a growth spell as the period that starts with an up-break and is followed by an average rate of per capita growth of at least 2 percent (and ends with a down-break). Since the 2009 up-break, per capita growth has averaged less than 2 percent; at least for now the period post 2009 cannot be considered a growth spell. (Per capita growth has averaged about 2 percent over the last four years, so if this growth performance continues, the period post 2009 *could be* characterized a growth spell in the future).

Figure 1. Madagascar and Sub-Saharan Africa: Impact on Spell Duration (Years)



Source: Authors' calculations. Each bar shows the change in the expected duration of a growth spell (in numbers of years) if a variable improves by 25 percentile points from the median value in the sample of sub-Saharan African countries, while holding other variables constant.

How can a growth spell in Madagascar be sustained? We follow the analysis in the REO to investigate how macroeconomic variables, exogenous shocks, and other factors influence the duration of growth spells, comparing Madagascar with the average SSA country. Figure 1 shows the importance of each factor or policy that can influence growth spell duration in the sample. In particular, it describes the change in the expected spell duration if a sub-Saharan African country (or Madagascar) improves in one factor or policy from its respective median value to the 75th percentile of the SSA countries, keeping all else constant. Results suggest that:

- *Better policies sustain growth spells for both SSA countries and Madagascar*. Increasing investment to GDP, reducing the debt-to-GDP ratio, increasing trade openness, and reducing inflation increase the expected length of the spell by an average of 3.5 and 4 years, in SSA and Madagascar, respectively.
- *A more favorable external environment is associated with longer spells* for both SSA and Madagascar.
- *Improving the quality of institutions and reducing market distortions increases spell duration*, with the effect significantly larger for Madagascar compared to the average of SSA.

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[1] See, for example, Haussman, Pritchett, and Rodrik (2005), Jermanowski (2006), Aizenman and Spiegel (2007), Jones and Olken (2008), and Berg, Ostry, and Zettlemeyer (2012).

[2] For details on the growth break and growth spell methodology see Berg et al. (2012), the SSA Spring 2017 Regional Economic Outlook, and Kourtellos and Tsangarides (2017).

6. Fiscal revenue continued to steadily increase in 2019, but planned budget spending was substantially under-executed. For the seventh year in a row, the net tax revenue-to-GDP ratio continued to increase. It is expected to reach about 10.4 percent of GDP in 2019, lower than budgeted for 2019 (10.8 percent of GDP in the revised budget law) due to difficulties to recover VAT payments from two big companies. Planned budget spending is significantly under-executed despite a gradual normalization after the adoption of the revised budget law in May, notably for investment and social spending (MEFP ¶3). This spending under-execution favored a sizeable domestic primary surplus during the first half of the year (¶10) and a comfortable cash-flow situation. It also created additional room, allowing the authorities to address an unexpected expenditure (arrears repayment to JIRAMA's suppliers of about 1 percent of GDP) without additional budgetary costs, thus preserving the objective of a primary surplus for the year.

7. The external position slightly weakened. The current account balance is projected to be -0.1 percent of GDP in 2019, down from a surplus of 0.7 percent of GDP in 2018. Export performance was impacted by a drop of 10 and 53 percent, respectively, in the price of vanilla and cobalt, and by a significant fall in clove export volumes due to cyclical production factors. Imports were also lower-than-anticipated due to under-execution in public investment. The nominal effective exchange rate depreciated by 4.2 percent year-on-year through end-October 2019, while the real effective exchange rate depreciated by 1 percent reflecting inflation differentials with trading partners. The central bank (Banky Foiben'i Madagasikara, BFM) intervened in late-September and early-October, using foreign currency sales to limit exchange rate volatility, which resulted in a reduction in the pace of reserve accumulation. Reserves stood at SDR 1.2 billion (4.2 months of imports) at end-November. The external position is assessed to be moderately stronger than estimates implied by fundamentals and desirable policies, while reserves are considered adequate based on the external sector assessment (Annex IV).

8. The monetary stance remains appropriate, with BFM continuing to successfully manage bank liquidity while containing inflation pressures. In the first half of 2019, the usual seasonality in bank liquidity related to the vanilla cycle was exacerbated by lower external pre-financing activities in this sector, the significant accumulation of government deposits, and some delayed repatriation of export proceeds. The BFM successfully carried out liquidity injection operations in July and August to maintain bank liquidity at an adequate level.

9. The financial sector remains largely dominated by banking activities, is healthy and increasingly contributes to economic development. Financial assets only account for about one-third of GDP, with the banking sector accounting for about 80 percent of total assets. Mostly foreign-owned, the banking sector is concentrated around four banks which hold more than 80 percent of total outstanding loans and credits. Banks remain profitable, adequately capitalized, well above the 8 percent capital adequacy ratio, and with ample liquidity buffers—as confirmed by annual stress tests conducted by the supervisor (see Selected Issues Paper III). Private credit growth accelerated to 20 percent year-on-year in September 2019, mostly driven by medium and long-term equipment loans as well as residential mortgages, albeit from a very low base (12.5 percent of GDP in 2018 to about 13 percent in 2019).

OUTLOOK AND RISKS

10. The medium-term economic outlook remains favorable. For the short-term (2020-21), growth is forecast to average about 5.3 percent, reflecting higher public investment— including the delayed impact of investment committed late in 2019—and an expected rebound in private sector activity based on high frequency data on credit growth; consistent increases in confidence documented in recent central bank surveys; and a positive outlook as relayed by both the private sector and commercial banks. Growth is expected to reach 5.6 percent in 2022-24 supported by continued public investment scaling-up and good prospects for private investment, including two hydropower plants financed by public-private partnerships; investments in the textile and apparel industry, including a new special economic zone for the promotion of the textile, clothing and accessories sector; an extension of an industrial area and a packaging plant; and expanding agribusiness including the development of agro-biological zones and a bio-seed multiplier center. Inflation is expected to converge to 5.5 percent per year, in line with the central bank target. Staff also anticipates an increase in tax revenue by about 0.5 percent of GDP per year, in line with recent years' achievements and planned reforms and strengthening of tax and customs administrations.

Selected Economic Indicators

	2019	2020	2021	2022	2023
Real GDP	4.8	5.2	5.4	5.6	5.6
Inflation (end of year)	6.0	6.2	5.9	5.4	5.6
Net tax revenue (percent of GDP)	10.4	10.9	11.3	11.7	12.2
Public investment (percent of GDP)	5.0	7.6	8.3	8.5	8.5
Private investment (percent of GDP)	13.9	14.4	14.7	15.2	15.4
Public debt (percent of GDP)	40.1	39.9	40.8	42.2	43.9
Gross official reserves (months of imports)	4.3	4.4	4.5	4.6	4.7

Source: Malagasy authorities; and IMF staff estimates and projections.

11. The ongoing investment scaling-up remains compatible with debt sustainability, while the current account is expected to gradually deteriorate. Larger construction-related imports and declining vanilla prices are expected to impact the trade deficit, resulting in a projected current account deficit of about 2 percent of GDP by 2023. Despite the planned increase in capital spending, an accompanying updated DSA shows that Madagascar remains at low risk of external debt distress and moderate risk of overall public debt distress.

12. The outlook remains subject to risks (RAM, Annex II)**.** Lower public investment could weigh on growth, while large transfers to state-owned enterprises (e.g., JIRAMA) could crowd out investment and other pro-growth spending. Delays in governance and corruption-related reforms could harm confidence. Madagascar remains highly vulnerable to terms-of-trade shocks including higher oil import bills and lower vanilla or mining export receipts and to natural disasters (Annex VII). Negative external developments such as weaker-than-expected global growth, rising protectionism, and a retreat from multilateralism could affect the outlook. Upside risks include larger private investment, higher public investment multiplier effects, and terms-of-trade gains unwinding more slowly than anticipated.

Authorities' Views

13. The authorities broadly agreed with staff's assessment of the risks facing the economy. They identified several external risks, including natural disasters such as cyclones and droughts, terms-of-trade shocks, and concurred with staff that restoring JIRAMA's operational and financial viability is crucial to limit associated fiscal risks. The authorities consider staff's medium-term projections pessimistic but understand the need for a more prudent baseline framework under the current ECF arrangement. They believe that a gradual acceleration of growth towards 7 percent in 2023 is feasible, driven by large increases in public and private investment toward more than 20 percent of GDP, including announced public-private partnership investment plans such as those for hydroelectricity.

Box 2. The Plan Emergence Madagascar (PEM), 2019–2023

A preliminary version of the authorities' Plan Emergence Madagascar (PEM) for 2019-2023, building on the electoral platform Initiative Emergence Madagascar, was presented to the donor community in late October. The PEM aims to address long-standing development problems through a significant increase in economic growth—while being inclusive, diversified, and sustainable. Following wide-ranging consultations with stakeholders, the authorities have revised the PEM.

The PEM envisions Madagascar's emergence based on social, economic and environmental pillars with governance as the cross-cutting theme. Specific PEM priorities are:

- Improving governance, described as a foundation for emergence, including through the fight against corruption, better security, and addressing regional challenges.
- Strengthening human capital, with strong focus on education, health, and housing.
- Accelerating economic growth by developing agriculture and tourism, and diversifying industries, through increasing public and private investment, and strengthening public-private sector partnerships.

The PEM is built on ambitious macro-assumptions, including an acceleration of growth to 7 percent in 2023 based on investment scaling-up, particularly private investment which is expected to reach 24 percent of GDP in 2023. Fiscal sustainability is preserved by continuous improvements in tax revenue mobilization, reaching 15 percent of GDP in 2023.

The implementation of the PEM can be complicated by absorptive capacity constraints and mobilization of resources. PEM's financing will critically depend on the mobilization of significant resources from the government, donors, and the private sector (including through PPPs). At this stage, while projects are mapped into 33 priorities supporting 13 commitments (which are linked to SDG-specific priorities) further clarifications are needed, including better project prioritization, proper costing over and above existing commitments, and medium-term programming of major projects.

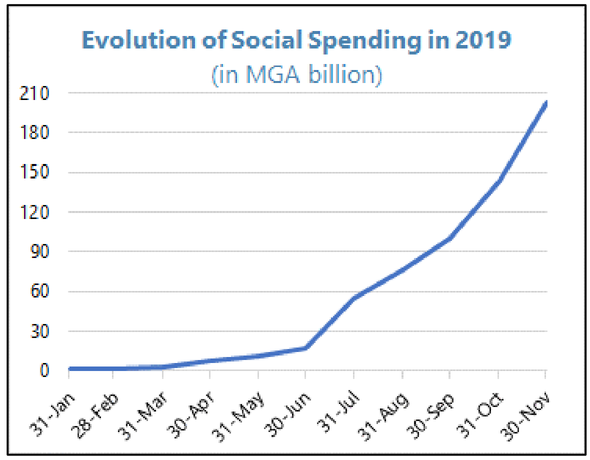
Selected Economic Indicators - PEM

	2020	2021	2022	2023
Real GDP	5.5	6.0	6.5	7.0
Inflation (average)	7.0	5.5	5.6	5.5
Net tax revenue (percent of GDP)	11.5	12.5	13.6	15.0
Public investment (percent of GDP)	8.7	8.3	8.6	8.7
Private investment (percent of GDP)	16.8	20.2	22.0	23.7

Source: Ministry of Economy and Finance, General Directorate of Economy and Plan

PROGRAM ISSUES

14. **All end-June 2019 performance criteria (PCs) were met** (Table 12)**.** The floor on NFA and ceiling on NDA were achieved, as well as the external debt PCs. The PC on the domestic primary balance—the fiscal anchor of the program—was met with a wide margin. All but one ITs were met, including the one on tax revenue. The exception was the IT on social spending, which was out of reach for end-June given the installation of the new government, the reorganization of ministries (including changes in their names and attributions), the late adoption of the revised budget and strengthened scrutinization of each spending line by the new government. Social spending has increased substantially since then with commitments reaching 40 percent of the total year-envelope by end-November compared to 3 percent at end-June. However, total priority social spending will likely remain under-executed for the year.



15. **There was mixed progress on the structural agenda during the last year of the program.** After progress in the first half of the year—notably in adopting the illicit asset recovery ordinance and establishing a new fuel reference price—there have been some signs of slowing reform implementation. Three of the six structural benchmarks for the 6th review were not met (Table 13): the financial stability law is still waiting submission to Parliament; JIRAMA signed one single source contract for fuel supply without notifying Fund and World Bank staff, thereby failing to meet a continuous benchmark (the authorities explained that the contract was signed as a matter of urgency in the context of severe electricity shortages in the capital city); and the implementation of the automatic fuel pricing mechanism is still pending (Box 5). The banking law (SB for end-December 2018) has been sent to Parliament after its adoption by the Council of Ministers on December 11, 2019.

16. **BFM continues to implement the recommendations of the July 2018 safeguards monitoring report,** and work is progressing in line with a commitment to fully adopt IFRS for the 2020 accounts (MEFP, ¶28). External audits continue to be finalized on a timely basis, and the FY2018 financial statements have been published. An updated safeguards assessment would need to be conducted in the event of a successor arrangement.

17. **Capacity to repay the Fund remains strong** (Table 14)**.** Outstanding obligations would peak in 2020 at 2.7 percent of GDP, and annual repayments, which increase in 2019 as Madagascar begins to repay the 2014 RCF-disbursement, should peak at 0.3 percent of GDP and 2.5 percent of government revenue in 2025.

18. **Data provision remains broadly adequate for surveillance and program purposes, with shortcomings being addressed gradually.** Rebased national accounts series are now in use (Informational Annex), as well as a reweighted consumer price index. The 2018 population census

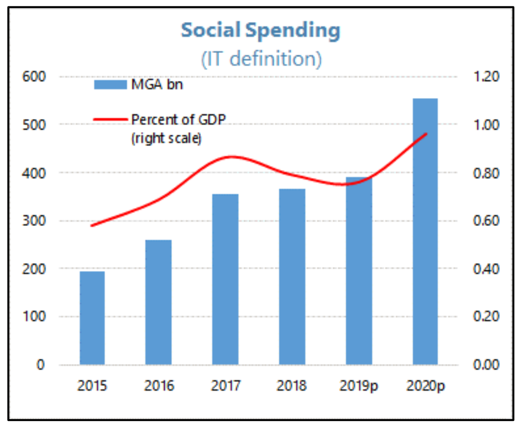
results are expected to be published by end-2019. Increasing staff resources would help to address shortcomings such as delays in the publication or the limited frequency in some data series.

Box 3. Social Spending

Priority social spending has been gradually increasing since 2016. Under the ECF, a specific definition of priority social spending was adopted (TMU, ¶22), limited to domestic spending on education, health, water and sanitation, and social safety nets, excluding externally financed investments and salaries. Even though externally financed investments represent a large share of social spending, they were not included to avoid an IT depending on disbursement decisions not fully under the authorities' control.

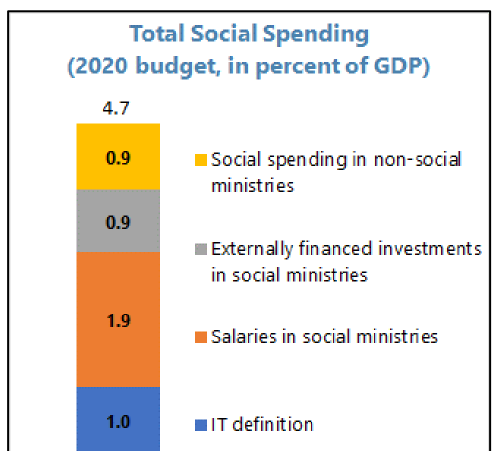
Under the definition of the program, priority social spending has been gradually increasing since 2016, but at a slower pace than planned. While priority social spending is expected to remain under-executed in 2019 at about 0.8 percent of GDP, this is still a significant increase compared to levels before the program.

Social spending (domestically financed, excluding salaries)	2019 revised budget	Executed*	2020 budget
WATER & SANITATION	**60.3**	**12.5**	**81.6**
Goods and services	0.3	0.3	0.2
Transfers	3.4	1.2	3.4
Domestically financed investments	56.6	11.0	77.9
HEALTH	**135.1**	**97.9**	**150.9**
Goods and services	30.6	23.6	19.2
Transfers	32.2	28.6	37.0
Domestically financed investments	72.3	45.6	94.7
POPULATION, SOCIAL PROTECTION & WOMEN EMPOWERMENT	**21.1**	**8.5**	**24.7**
Goods and services	5.2	3.6	4.7
Transfers	3.0	2.6	4.5
Domestically financed investments	12.9	2.3	15.5
EDUCATION	**300.2**	**84.5**	**298.1**
Goods and services	56.2	23.7	47.4
Transfers	77.1	48.7	65.4
Domestically financed investments	166.9	12.1	185.3
TOTAL	**516.7**	**203.4**	**555.2**



Sources: Malagasy authorities; IMF staff calculation.
* Executed at end-November 2019

Using a broader definition, social spending in Madagascar may be four to five times larger. Including salaries, externally financed social investments, and social spending in other ministries, planned social spending in the 2020 budget law is estimated at 4.7 percent of GDP. Some social projects are implemented by non-social ministries. This includes interventions on nutrition and health which are under the budget of the Prime Minister or the Presidency; projects overseen by the Ministry of Economy and Finance like the support for community and social development; the Ministry of Energy's projects to distribute solar kits to the poorest communities; and the Ministry of Agriculture's projects to assist the poorest rural areas (e.g., self-sufficiency agriculture and supporting women's work in agriculture).



Sources: 2020 budget law; IMF staff calculation.

Planning, execution and monitoring of social spending can be improved. In the context of the PEM, the government is emphasizing strengthening social policies in education, health and housing. In the budget law, spending is detailed by ministries, and in a multi-year framework for investments. It may be therefore possible, in the future, to consider a more comprehensive monitoring of social spending in all ministries, beyond the social ministries. With the recent progress on the wage bill management, it may also possible to more accurately track the number of positions dedicated to the social sectors, including teachers and medical staff.

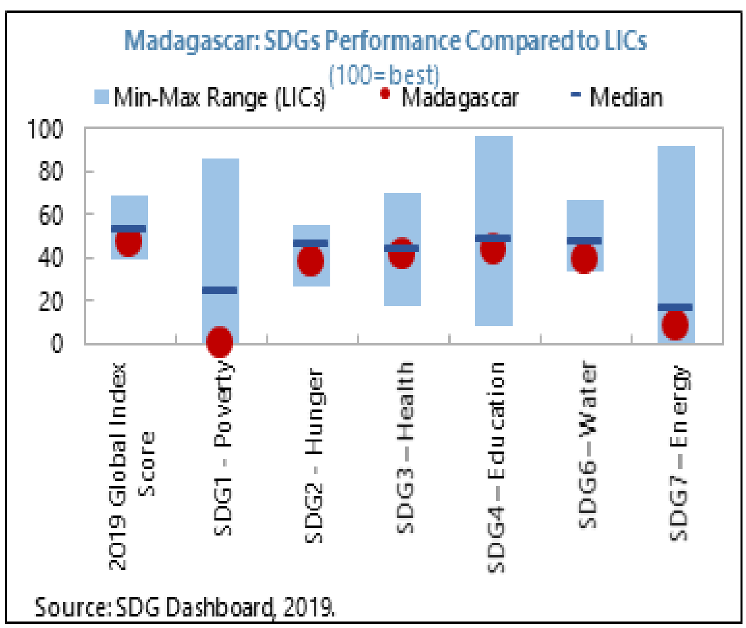
POLICY DISCUSSIONS: REFORMS FOR STABILITY AND INCLUSIVE GROWTH

The 2019 Article IV consultation held jointly with the last ECF review was an opportunity to take stock of progress in recent years and discuss remaining challenges to overcome Madagascar's fragilities. Article IV discussions focused on the key components of a medium-term strategy that would place Madagascar on the path towards more sustained and inclusive growth to improve development outcomes, guided by the government's ambitious reform plan formalized in the PEM. Policy discussions centered around four themes: (i) creating fiscal space to finance much needed investment and raise social spending; (ii) strengthening monetary and exchange rate policy effectiveness; (iii) improving financial sector development and resilience; and (iv) promoting better governance and an improved business climate.

19. Progress on the 2017-Article IV key recommendations—aligned with the ECF objectives—helped improve macroeconomic performance, advance structural reforms, and catalyze donor support (Annex II)**.** Beyond meeting protracted balance of payment needs, the ECF program began to address broader challenges facing Madagascar. It helped boost prospects for inclusive growth; create fiscal space through revenue mobilization and spending prioritization; reinforce economic governance; and strengthen central bank operations and financial supervision.

20. Continuing progress in overcoming structural fragilities that hamper human and economic development requires concerted efforts. Building on the current period of relative political stability and progress in the ECF-supported program, discussions focused on the key components of a medium-term strategy towards sustained and inclusive growth to improve development outcomes and make progress in achieving the SDGs (Annex VII), also in the context of the government's PEM.

21. Relevant technical assistance is essential to support these efforts. A revised capacity development strategy was discussed with the authorities (Annex IV). Building on recent TA that was closely aligned with the objectives of the ECF-supported program, the priorities are to strengthen on-going reforms in tax policy and administration, PFM (especially public investment management), monetary and financial sector oversight, and the implementation of the anti-corruption legal framework.



A. Fiscal Policy to Support Inclusive Growth

Efforts to create fiscal space for priority spending need to continue. Over 2014-2019, tax revenue increased by 2 percentage points of GDP, lower-priority spending (including transfers to JIRAMA) decreased, and the wage bill and transfers to the civil pension fund were contained. At the same time, public investment favored infrastructure, and spending in education and health increased. However, some of these improvements have been more modest than initially envisioned, calling for revamped efforts and more impetus for reforms.

22. The 2020-budget starts to incorporate the ambitious assumptions from the PEM. The budget, approved by ordinance on December 18, 2019 after being discussed at the National Assembly and the Senate, is based on very optimistic assumptions on tax collection (+1.4 percent of GDP compared to 2019) resulting from ongoing administrative improvements and new tax measures, notably the broadening of the VAT base and the generalization of VAT on public procurement (expected yield of at least 0.4 percent of GDP), and some increases in excise taxes (MEFP 12). The wage bill and transfers are contained, with transfers for JIRAMA temporarily set to zero pending the finalization of a medium-term plan (Box 4). There is a large increase in the budget envelope for domestic investment (+2.3 percent of GDP compared to 2019) favoring basic infrastructures, while priority social spending is set to 1 percent of GDP (from 0.7 percent in 2019). This budget shows a small domestic primary surplus and is fully financed, based on planned budget support and credible domestic financing assumptions.

23. Staff emphasized that the projected increase in revenue for 2020 is too optimistic and presented an alternative scenario. The team's scenario considers an increase in tax revenue of 0.6 percent of GDP (building on tax measures described in ¶21 and recent years' performance), limits domestic public investment to about 3 percent of GDP based on identified projects, and increases transfers by 0.3 percent of GDP compared to the budget (anticipating needed transfers to JIRAMA). Staff urged the authorities to commit to the implementation of contingency measures if the envisaged revenue increases do not materialize in the first months of 2020, including through reducing non-priority spending while protecting social spending, and to formalize these revisions in a revised budget law (MEFP, ¶13).

24. Ambitious but credible medium-term revenue mobilization plans need to be supported by a comprehensive revenue administration and revenue collection strategy. There is potential in Madagascar to significantly raise tax revenues with a sustained and sequenced strategy covering both revenue administration and tax policies (see Selected Issues Paper on Tax revenue mobilization potential). Recent FAD TA missions stressed priorities for the Domestic Tax Department (including reviving tax control operations, improving the collection of outstanding tax payments, and strengthening the reliability of taxpayer identification already initiated), and for Customs (including reducing the irregularities in customs clearance, and intensifying the control of the companies benefitting from free zone-agreements). Staff emphasized that based on evidence from recent achievements in Madagascar as well as successful revenue mobilization episodes from other SSA countries, a more conservative approach to projections on tax revenues is warranted; and that ambitious but credible annual increases of about 0.5 to 1 percentage point of GDP per year over the medium-term would already be a success.

25. Planning and monitoring of the wage bill must be strengthened, while reforms of the civil servants' pension fund are needed to contain its deficit. The government wants to contain the wage bill under 5 percent of GDP. Payroll management is improving with the generalization of the new IT tool (AUGURE). On the civil servant pension fund, reforms based on recent FAD TA are needed to contain the deficit, including by indexing pensions to prices and not wages, revising the benefit calculation rules (reducing accrual rates), and gradually eliminating some bonuses.

26. The authorities are committed to implementing a medium-term recovery plan for JIRAMA (MEFP, ¶14)**.** Short-term cost-saving measures continue to be implemented, including enforcement of public entities' bills payments, the introduction of additional smart meters, increased efforts on bill collection and the fight against fraud. Beyond these measures, the authorities committed to implementing a medium-term operational and financial recovery plan, currently finalized with the support of the World Bank, as soon as it is ready. Significant gains are expected from the renegotiations of contracts, and the plan will include an arrears' clearance strategy that will generate large savings in interest payments and avoid ad-hoc repayments (like those that occurred in 2019) (Box 4).

27. The fiscal risk associated with fuel pricing needs to be addressed (Box 5)**.** There has been no direct budget cost from fuel pricing in recent years, but a fiscal risk could materialize with unfavorable international oil price developments. The planned implementation of an automatic fuel price mechanism by September 2019 has been postponed to March 2020, waiting for the conclusion of an audit currently undertaken on the implementation of the new reference price established in June 2019 (MEFP, ¶14). Staff urged the authorities to fulfill this new commitment to prevent further liabilities, and emphasized that it is important to have mitigating measures and social safety nets in place before the planned implementation of the mechanism.

28. Further efforts are needed to ensure higher priority spending in social sectors. The authorities have taken short-term measures to favor social spending execution early in the year, including streamlined procurement procedures and regular meetings between social ministries and the Ministry of Economy and Finance dedicated to execution issues. They will also better monitor and execute social spending by non-social ministries. In addition, the expansion to additional regions of World Bank-supported safety net programs benefiting from the US$90 million grant received in March 2019, is well advanced (MEFP, ¶14).

29. The planned public investment scaling-up requires better prioritization and execution (Box 6)**.** Public investment increased from 3 to 5 percent of GDP between 2015 and 2019 but remained short of the government's target. Domestically-financed investment was often perceived as a variable of adjustment for budget savings, and externally-financed investment was so far under-executed compared to budget plans. While ongoing progress, following FAD recommendations, includes drafting a guide on public investment management and the development of a comprehensive database to improve monitoring, staff emphasized that the ambitious public investment objectives of the PEM should be further clarified, including the prioritization of projects considering implementation and absorptive capacity constraints, and proper costing.

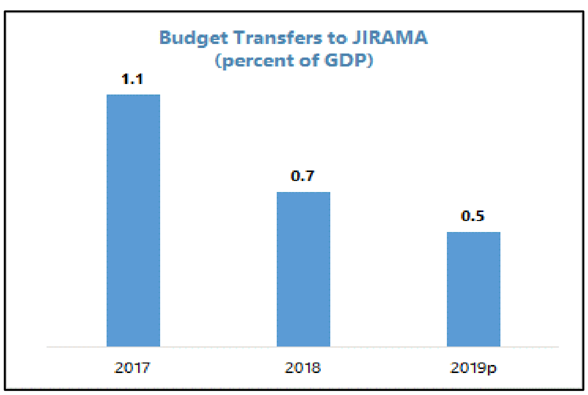
Authorities' Views

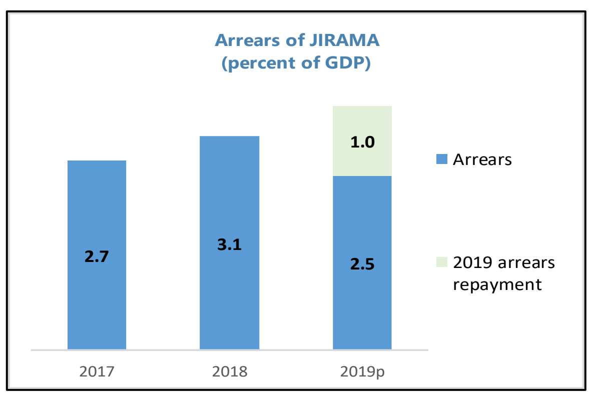
30. **The authorities broadly agreed with staff's assessment and recommendations.** They welcomed staff's analysis on revenue mobilization but reaffirmed their objective of increasing net tax revenue progressively to 15 percent of GDP by 2023. For 2020, they are confident that their revenue target can be reached through strengthened efforts on collection and control by tax administrations, and fiscal measures in the budget law. That said, the authorities are committed to implementing contingency measures—postponing lower priority spending while protecting social and investment priority spending—if their revenue assumptions do not materialize. The authorities are determined to implement a medium-term operational and financial recovery plan for JIRAMA, which is consistent with one of the government's main priorities to increase access to electricity and water. On fuel pricing, the authorities are waiting for the results of an audit on the reference price application (in use since June 2019) before implementing an automatic pricing mechanism planned by March 2020 and remain committed to avoid direct budget costs. Finally, while recognizing that additional efforts are needed to boost investment implementation capacity, they reaffirmed their ambition to increase public investment significantly, especially to finance much needed investment in basic infrastructure including energy, water and sanitation, and roads.

Box 4. JIRAMA's Medium-Term Recovery Plan

In June 2017, the Board of JIRAMA adopted an ambitious business plan that aimed to eliminate subsidies for operational losses within four years. This was part of the ECF-supported program objectives to improve quality of spending and introduce concrete measures for cost savings and enhanced revenue collection, as well as implementing monitorable monthly targets.

Budgeted transfers decreased in 2018 and 2019, but this was insufficient to compensate operational losses. As a result, JIRAMA's arrears continued to increase and were estimated to reach about 3.5 percent of GDP at end-2019. In the context of increasing water and power outages with mounting social and economic implications, a decision was taken to repay MGA 501 bn (1 percent of GDP) of arrears to JIRAMA suppliers.





Sources: Ministry of Economy and Finance, and IMF.

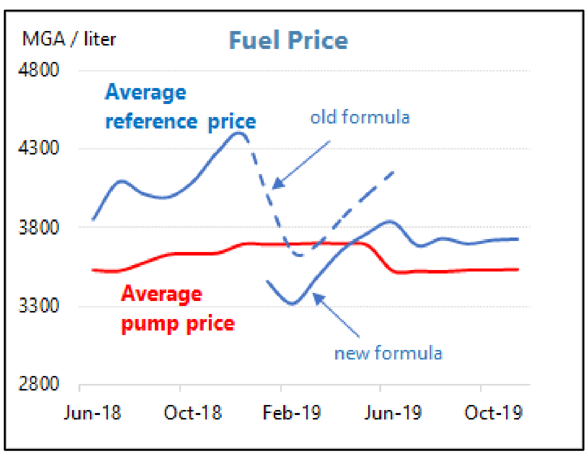
Beyond these ad hoc arrears' repayments, the authorities are committed to implement a new medium-term recovery plan. This plan should balance JIRAMA's accounts, address the issue of accumulated liabilities to avoid risks of increased public transfers and financial distress, and improve the production and distribution of electricity. A broad medium-term strategy was presented on October 12, 2019 by a consultant firm hired by the World Bank and endorsed by the company's board. It specifies measures including efficiency improvements (such as optimizing fuel supply and improving collection); a strategy for restructuring remaining arrears; the renegotiation of thermal contracts (expected to generate large savings); investments in hydro-electricity; possible adjustments in the tariff schedule; and a residual subsidy from the government to cover the cash deficit.

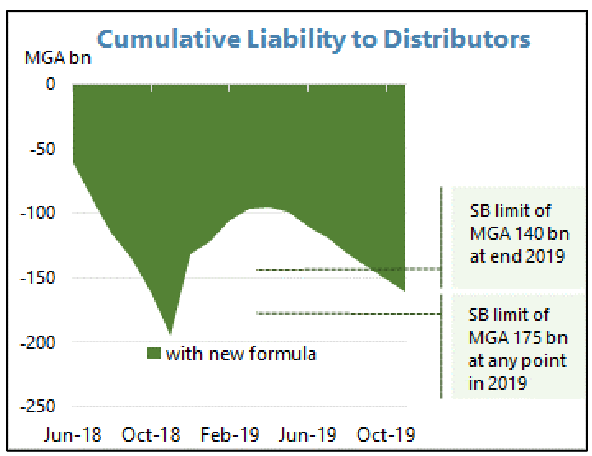
Box 5. Fuel Pricing

Madagascar initiated the process of removing fuel subsidies in the favorable context of the fall in international oil prices in 2014-15[1]. Gradual increases of pump prices took place, and the government instituted a price adjustment mechanism in February 2016 (regular price adjustments but not automatic), which worked well during 2016-2017. However, this favorable situation reversed in 2018 when, despite ad hoc adjustments in pump prices totaling 10 percent, the gap between reference and pump prices led to a cumulative liability to fuel distributors.

Important progress was achieved in 2019. In February 2019, a memorandum of understanding was signed with the fuel distributors on plans for an automatic fuel price mechanism and settlement of the existing liability. On June 19, 2019, an agreement was reached for the implementation of a new price structure, reducing the margins of the distributors by the equivalent of 12 percent. The new reference price structure, applied retroactively from January 2019, reduced the liability to distributors below MGA 110 billion (0.2 percent of GDP) at end-June 2019.

The establishment of a new pricing mechanism, which will avoid any lasting significant liability, has been postponed from September 2019 to March 2020. The objective remains to avoid budgetary impact from fuel pricing in the future by following cost recovery pricing ("vérité des prix"). The planned mechanism will combine two elements: an automatic price calculation (based on the reference price) with a smoothing formula, along with a limited discretionary adjustment, which could help manage potentially difficult social impacts. In addition to the discretionary adjustment, it is essential to put in place mitigating measures and social safety nets. Before implementing this pricing mechanism, the government would like to complete the audit of the implementation of the new reference price. Next steps would include testing the mechanism and communication to the public. In the meantime, due to a remaining small gap (less than 5 percent) between reference and pump prices, the liability has increased by 0.1 percent of GDP at end-November, which will likely result in a small breach (less than 0.05 percent of GDP) of the continuous SB limit for the year.





Sources: Malagasy authorities; and IMF staff.

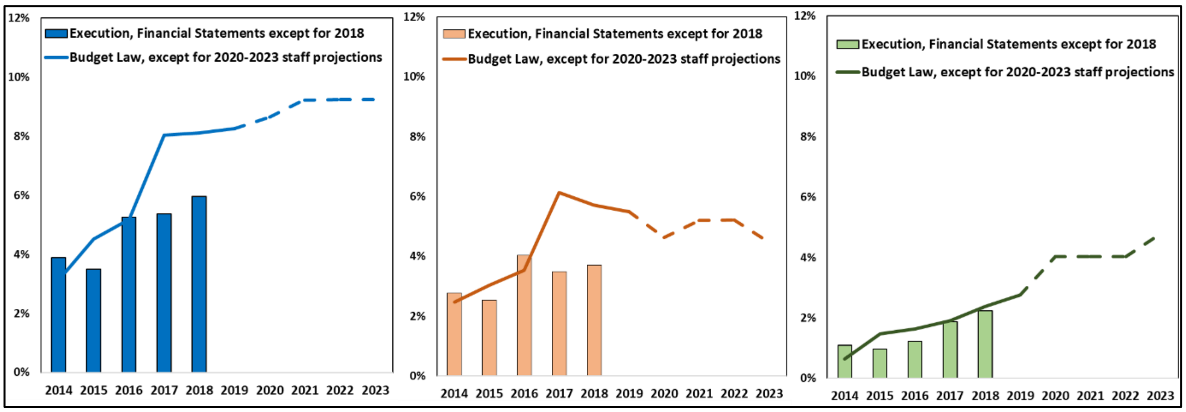
[1]For more details, www.imf.org, Annex II. Towards an Automatic Fuel Pricing Mechanism.

Box 6. Strengthening Public Investment Efficiency

The pace of scaling up set by the government appears to be very ambitious. In recent years, public investment has been under-executed compared to budget plans, especially for externally-financed investment.

Public Investment Execution

Total public investment | Externally-financed investment | Domestically-financed investment



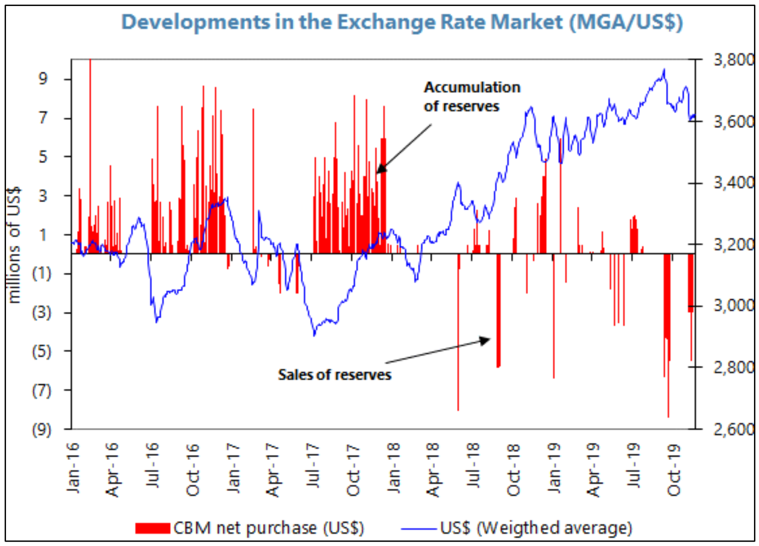
Sources: Budget Laws, Financial Statements and IMF staff estimates.

Madagascar should focus on improving public investment efficiency, in line with FAD TA recommendations, by:

- *Identifying the highest priority projects.* Funding availability would need to focus on these projects to ensure their completion.
- *Presenting financing progress against the total project cost and duration to ensure sufficient resource allocation*. For each major project, the budget documents should show the reference to specific engagement and priority in the PEM as well as specific targets in the SDGs. That way, progress in PEM and SDGs could be analyzed and effectively monitored.
- *Allowing enough time and resources to prepare projects to ensure their quality and implementation readiness*. This would help achieve the expected results and reduce inefficiency in the implementation of these projects including delays and cost overruns.
- *Proactively monitoring the implementation of the major projects*. This would identify projects experiencing delays and action can be taken to expedite them. Some countries have established high-level committees to identify and remove obstacles to implementing major projects to ensure projects are completed on schedule, within budget and deliver the expected outputs.
- *Ensuring enough funding to complete ongoing projects.* If projects already started do not receive enough funding to cover expenditures planned in the budget year, the delay will likely increase total project costs. Such costs can be avoided if budget practices give priority to funding ongoing projects before starting new projects.

B. Strengthening Monetary and Exchange Rate Policy to Contain Inflation and Promote External Stability

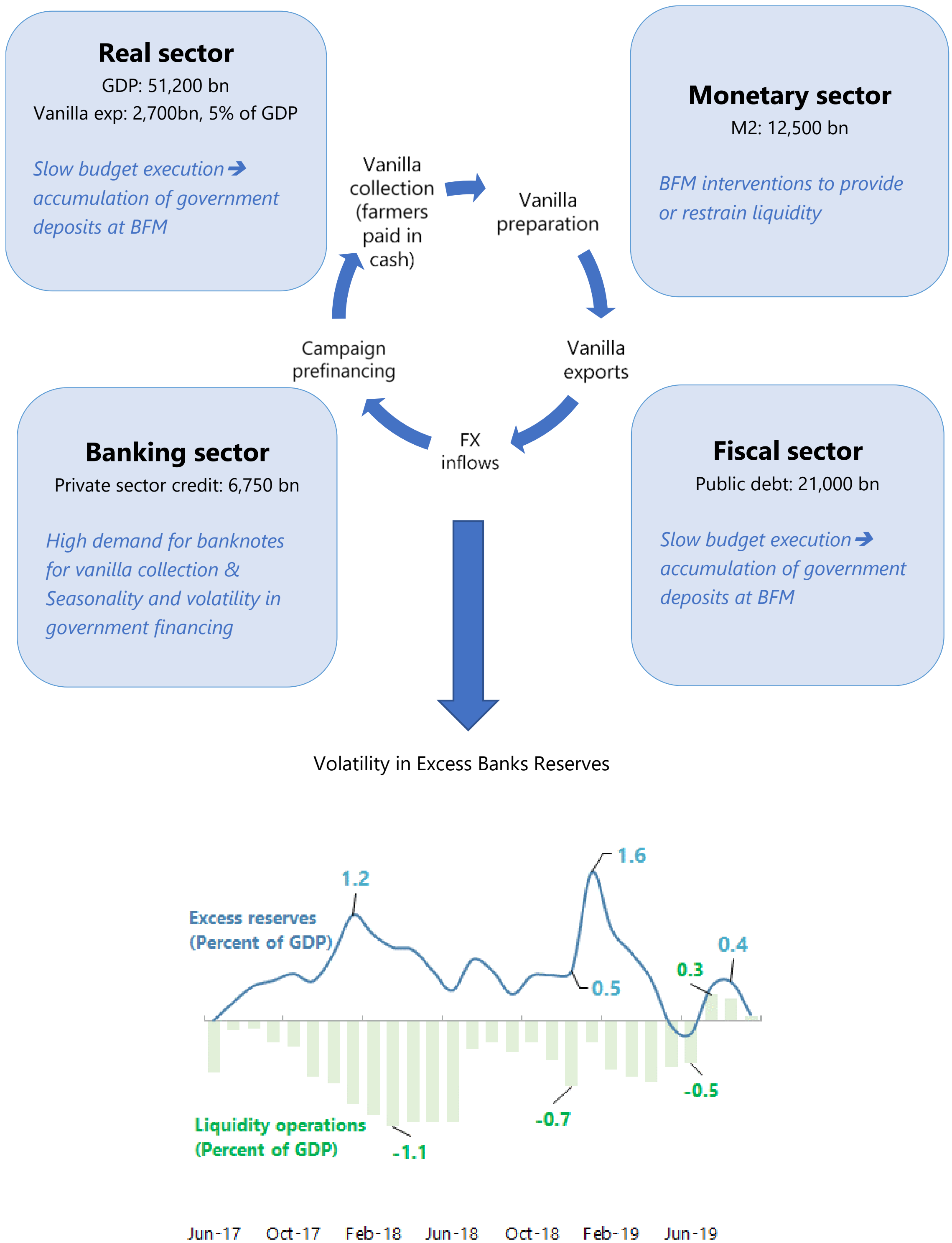
31. The BFM should continue to actively manage bank liquidity, thus supporting credit while containing inflation pressures. Within a flexible exchange rate regime with shallow money markets, a combination of active bank liquidity management relying on quantitative instruments and opportunistic FX interventions aimed at building up reserve buffers (market conditions permitting) remains an appropriate policy stance to stabilize real exchange rate developments in the face of seasonality in bank liquidity traditionally related to the vanilla cycle, and significant terms of trade volatility. In the context of exacerbated volatility, and to ensure adequate coverage of required reserves, the central bank was prompted to reverse its earlier stance of mopping-up excess liquidity and support the banks, hence bolstering credit developments. In a context of limited financial intermediation partly reflecting the ineffectiveness of the interest rate channel, staff encouraged the authorities to continue displaying flexibility in coping with unanticipated volatility, including through fixed-rate secured fine-tuning liquidity operations.



32. Progress towards improving the interest rate channel of monetary policy transmission is encouraging. Structural reforms are underway with the support of Fund TA to gradually transition from a monetary policy framework relying on reserve aggregates to interest rate targeting, starting with the development of the interbank lending (see Selected Issues Paper on Monetary policy under excess liquidity). Following the introduction in May of an interest rate corridor made up of an overnight deposit facility and an overnight standing facility, interbank market activities have started to intensify, and money market interest rates have declined from 7-8 percent in early 2019 to 3.5-4 percent in the recent months. After discontinuing the practice of announcing ceiling (floor) rates for liquidity withdrawal (injection) operations, the authorities intend to conduct volume tenders for liquidity management and better calibrate the overnight policy rate to reflect macroeconomic developments. To further incentivize market developments and the buildup of a yield curve, they also plan to introduce repurchase operations as soon as the dedicated law is adopted by Parliament.

Figure 2. Madagascar: Macro-Financial Impact of the Vanilla Cycle

(Figures in MGA, projected at end-2019)



33. Efforts are ongoing to improve foreign exchange market operations and gradually phase out the surrender requirement on export proceeds. A draft law on the foreign exchange market, prepared with IMF TA, is undergoing final revisions before being submitted to Parliament. The authorities have also prepared a plan to gradually phase out the existing surrender requirement on export proceeds, considered a capital flow management measure under the IMF's Institutional View, based on market developments.

Authorities' Views

34. The authorities concurred with staff on the need to maintain an appropriate policy stance by continuing to actively manage bank liquidity, while closely monitoring potential inflation pressures. They emphasized that continued prioritization should be given to strengthening macroeconomic forecasting capacities and its framework before phasing out quantitative instruments, including by finalizing the interest rate corridor. They welcomed staff's support on ongoing reforms through policy advice and active TA involvement, including on improving the functioning of the foreign exchange market.

C. Strengthening Financial Sector Resilience and Financial Inclusion

35. The framework for bank supervision has been strengthened but its operationalization hinges on the implementation of the new banking and financial stability laws (MEFP, ¶25)**.** Based on the 2015-FSAP recommendations, the authorities have embarked on an ambitious agenda to reinforce the independence of the central bank and address financial stability risks, notably through the implementation of risk-based supervision with the support of Fund TA. A prerequisite for the adoption of implementation instructions, the new banking law that has been submitted to Parliament in December 2019 after validation by all stakeholders and recent approval by the Council of Ministers, reinforces the independence and powers of the supervisor and introduces a bank resolution framework. The law on financial stability, under review by the Council of Government, clarifies the macroprudential architecture and sets procedures to detect system risk.

36. Efforts to improve financial inclusion have been recently stepped up, in line with the 2018-22 National Strategy for Financial Inclusion. This strategy has three main objectives: (i) financial education and consumer protection; (ii) access and use of financial services; and (iii) strengthening of the legal, regulatory, and institutional frameworks. Recent regulatory reforms include the gradual setting up of a credit bureau, expected to start its operations shortly, as well as the licensing of the public savings fund as a microfinance institution and the implementation of the first recommendations from the audit of the postal savings fund (see Selected Issues Paper on Financial sector development and access to credit). Over the last few years, microfinance institutions' activities have expanded rapidly, even though the sector only accounts for 5 percent of the total financial system assets and less than 2 percent of the country's GDP. To further address bottlenecks to financial inclusion, some government-sponsored initiatives by banks and microfinance institutions aim at enlarging access to credit to wider segments of the population, notably in rural areas, through electronic payment platforms developed with mobile phone operators (Box 7).

Authorities' Views

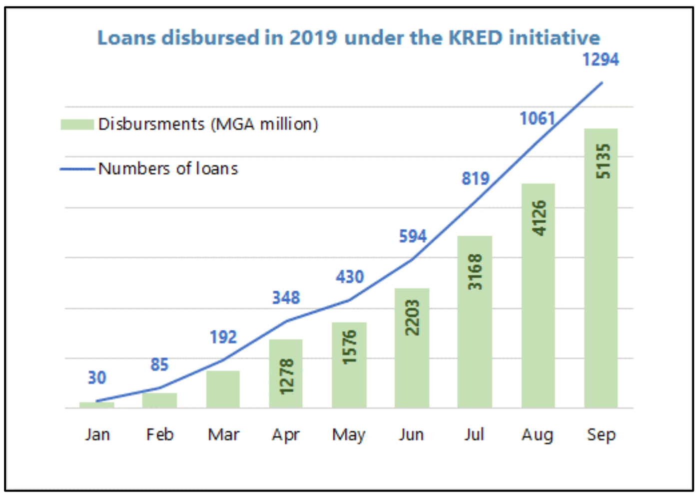
37. **The authorities concurred with staff that the banking law and the law on financial stability are essential to pave the way for enhanced bank supervision and to support financial inclusion.** They noted that providing financial services to hitherto neglected segments of the population and reducing the use of cash in everyday payments would be instrumental in reducing the share of informality in the economy, thus fostering inclusive growth.

Box 7. The KRED Initiative

In an effort to improve access to credit and financial inclusion, the largest bank in terms of assets launched in 2019 the KRED initiative—an innovative product targeting micro- and small enterprises.

The project consists of seeking to establish proximity relationships with potential customers, with sales teams permanently active in the field meeting each client to offer customized financial solutions. All transactions are carried out digitally in collaboration with the mobile phone operator TELMA, allowing for clients to apply for, receive, and repay credit remotely without ever having to go to a bank location.

This project is supported by the government, as part of its program *Fihariana*, with an agreement to provide MGA 80 bn (about US$22 million) to directly finance or guarantee loans granted under the KRED initiative. It targets economic activities in trade, services (transport, services in agriculture, IT services, restoration...), and in agriculture and fish farming. A large part of this funding goes to the informal or semi-informal sector, which contributes to the exit from informality. It also contributes to the development of agri-business activities in a sector still largely dominated by subsistence production.



First results of the initiative are encouraging, with almost 1,300 loans granted in the first three quarters of 2019, for a total amount of more than MGA 5 billion (about US$1.4 million), and an average loan of about US$1,100.

D. Promoting Better Governance and Business Climate

38. **Effective enforcement of the new anti-corruption legal framework is needed to strengthen institutions** (Annex VIII, MEFP, ¶18-19)**.** Key anticorruption laws have been enacted since 2016, including most recently the AML/CFT and the illicit asset recovery laws. Further emphasis is needed on developing and reinforcing the institutions for effective enforcement, including through the issuance of associated implementation decrees expected in early 2020. In particular, an implementing decree is necessary before the appointment of the members of the Illicit Asset Recovery Agency and to specify the way in which it will operate.

39. Further strengthening of Public Financial Management is necessary to improve the governance of public resources. Building on FAD TA, the authorities have made efforts to strengthen PFM under the 2018-2026 Strategic Plan of Modernization and the 2018-2020 Action Plan. Improvements in the institutional framework have been made in the management of national public institutions, budgeting, debt management strategy, transparency and efficiency of public procurement, cash management, implementation of the Treasury Single Account, reporting and statistics, and strengthening of internal audit and inspection bodies. These significant improvements have started to be effectively implemented. A Steering Committee of Public Finance Reforms will be established to effectively manage PFM reforms. Update of the reform actions and alignment with the objectives of the Plan Emergence Madagascar remain to be done in early 2020.

40. Improvements in the business climate are needed to strengthen the quantity and quality of investment (MEFP, ¶20)**.** Madagascar's business environment is challenging, consistently ranking very low in the Ease of Doing Business Index and below peers. Recent progress includes a better enforcement of contracts with a significant reduction in delays to resolve disputes, and better access to credit information. Further progress is needed in the regulatory framework and rule of law (investor protection, contract enforcement and property rights) to boost growth and reduce vulnerabilities to corruption.

Authorities' Views

41. The authorities agreed with staff's assessment and recommendations. They stressed that the three main priorities of the Plan Emergence Madagascar (social, economic and environmental) are articulated around improved governance and the fight against corruption. In addition to the efforts needed for the proper functioning of the institutions in charge of the fight against corruption, the authorities agreed that it is essential to improve PFM, especially the transparency of tax revenue collection and of the use of these resources by the state. They agreed that an improved business environment is essential for attracting both domestic and foreign investments and underscored the ambition to reach the top 100 ranking in Doing Business by 2023 through the efforts of the Economic Development Board of Madagascar (investment promotion agency).

STAFF APPRAISAL

42. Madagascar's economic performance has continued to improve. Despite a slowdown in the first half of the year, growth is expected to improve to 4.8 percent in 2019 after reaching 4.6 percent in 2018—the highest rate in 10 years—and inflation to be contained to 6 percent for the year. In a context of decreasing exports, the current account is expected to record a small deficit, while fiscal performance was consistent with a small primary surplus. The external position is assessed to be moderately stronger than estimates implied by fundamentals and desirable policies, while reserves are considered adequate.

43. The medium-term outlook remains broadly favorable, but subject to risks. Supported by scaling-up of public investment and stronger private sector activity, medium-term growth is expected to gradually increase to about 5.5 percent, which is more conservative than that envisaged under the authorities' PEM, while surpassing the average for sub-Saharan Africa and raising per capita income. The ongoing investment scaling-up continues to remain compatible with debt sustainability, with the updated DSA indicating that Madagascar remains at low risk of external debt distress and moderate risk of overall public debt distress. The current account is expected to gradually deteriorate. Madagascar remains highly vulnerable to terms-of-trade shocks including higher oil import bills and lower vanilla or mining export receipts and to natural disasters, while lower public investment could weigh on growth.

44. Implementation of the ECF-supported program has remained broadly satisfactory despite slowing progress on the structural agenda. All performance criteria were met for end-June 2019, the last test date under the current arrangement. There was mixed progress, however, in the structural reform agenda during the last year of the program. Several structural benchmarks were not met because of delayed actions, including the submission to Parliament of the new banking law and the law on financial stability, and the implementation of an automatic fuel pricing mechanism. Staff welcomes the commitment by the authorities to complete these important reforms.

45. Staff welcomes the authorities' determination to strengthen growth, enhance revenue collection, and foster social inclusion, but cautions against assumptions that may be too optimistic. The government has an ambitious agenda, developed in its *Plan Emergence Madagascar*, to address long-standing development issues by increasing economic growth through increased public and private investment, strengthening human capital and improving governance. Staff support these objectives but emphasize that economic growth and fiscal revenue assumptions may be too optimistic. Considering very ambitious assumptions on tax collection in the 2020 budget, staff welcome the authorities' commitment to implement contingency measures if revenue assumptions do not materialize in the first months of 2020.

46. Creating additional fiscal space for priority spending remains essential. Staff encourages the authorities to finalize and implement their new medium-term recovery plan for JIRAMA in order to make the public utility financially viable and eliminate the need for budgeted transfers at the expense of higher-priority social and investment spending. Staff also encourages the authorities to adopt the planned fuel pricing mechanism that will avoid the risk of potential budgetary impact in the future, while putting in place mitigating measures for the more vulnerable portions of the population including by the on-going scaling up of social safety net programs. This is essential to preserve and create additional fiscal space, notably for spending in the health and education sectors after budget under-execution in 2019.

47. Staff welcomes the continued progress in improving the monetary framework and strengthening the financial sector. The central bank has continued to successfully manage banks' liquidity through timely interventions and support gradual accumulation of reserves, thus contributing to macroeconomic stability. The implementation of the new banking law and the financial stability law, and the continuation of structural reforms undertaken at the central bank are instrumental to strengthen the monetary policy framework and boost financial inclusion.

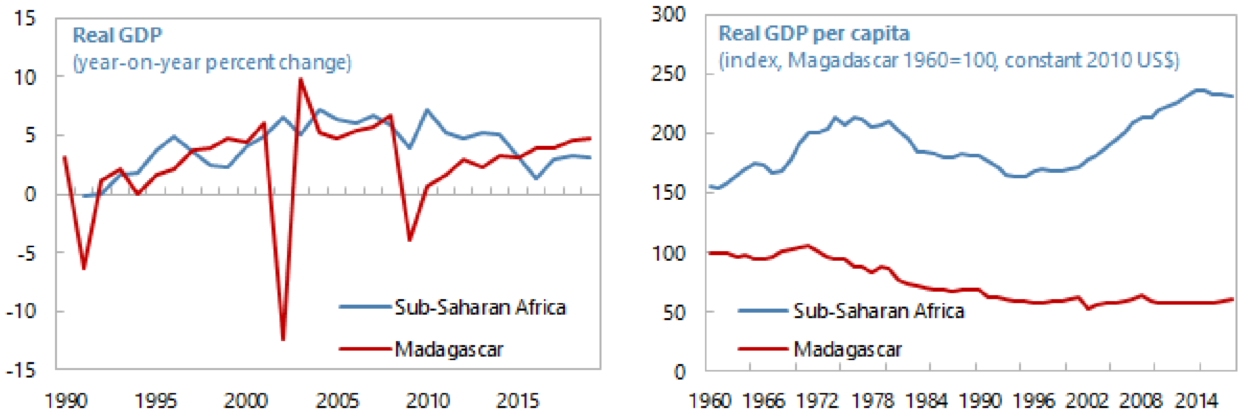
48. Staff urges the authorities to increase efforts for the implementation of the anti-corruption legal framework and continue PFM reforms. Staff encourages a firm and impartial enforcement of the legal framework that was set up in recent years, now closer to international standards. This is also crucial to strengthen the business climate and attract private investment. Continuing ongoing efforts to strengthen public financial management will enhance fiscal governance, transparency, and sound public finances.

49. Based on Madagascar's performance under the program and the authorities' commitment to outstanding reforms, staff recommends the completion of the sixth and last review under the ECF arrangement.

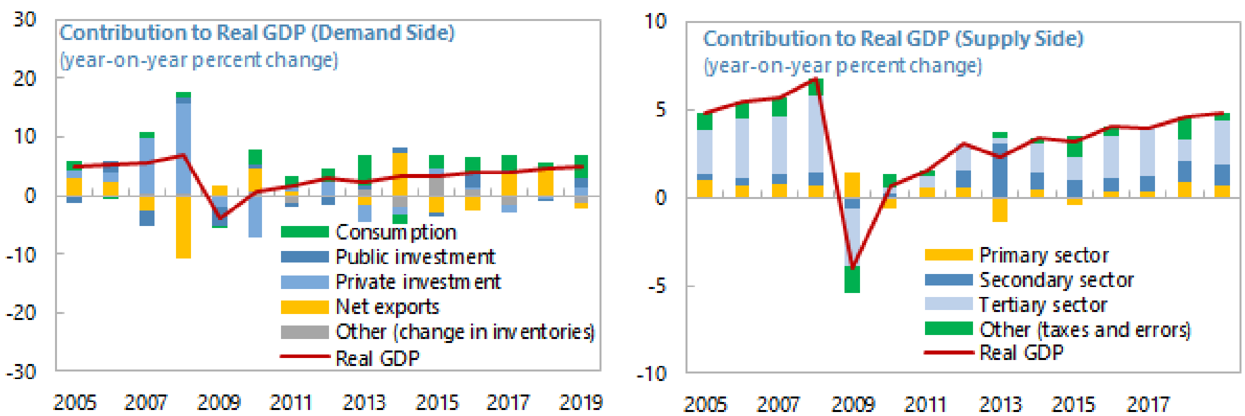
50. Staff notes the authorities' intention to start discussions on a successor arrangement. It is recommended that the next Article IV consultation take place on the standard 12-month cycle.

Figure 3. Madagascar: Real Sector Developments

Despite recent improvements, growth in Madagascar has been insufficient to offset population growth.

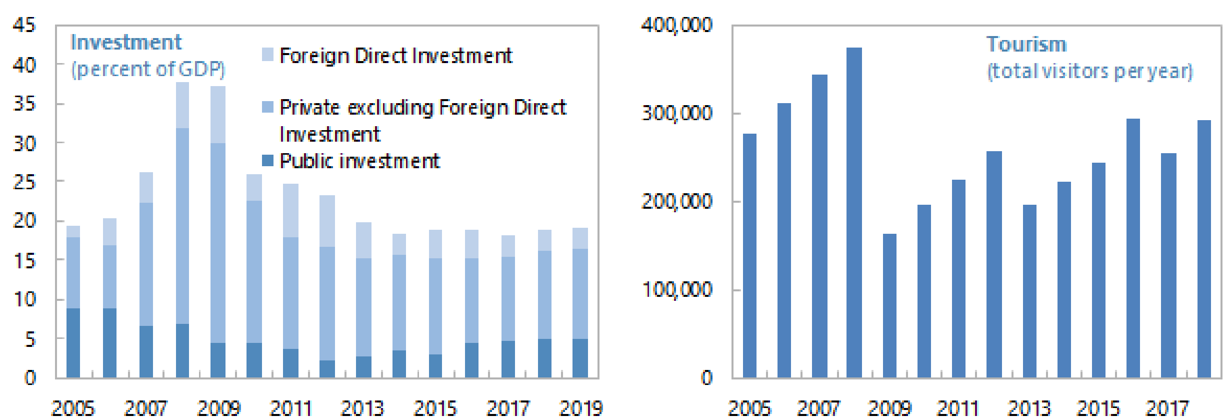


In recent years, net exports has been a key driver of growth on the demand side; on the supply side, growth is driven by the tertiary sector and a recent rebound in agriculture.



Investment is rising but is still below 2008 levels...

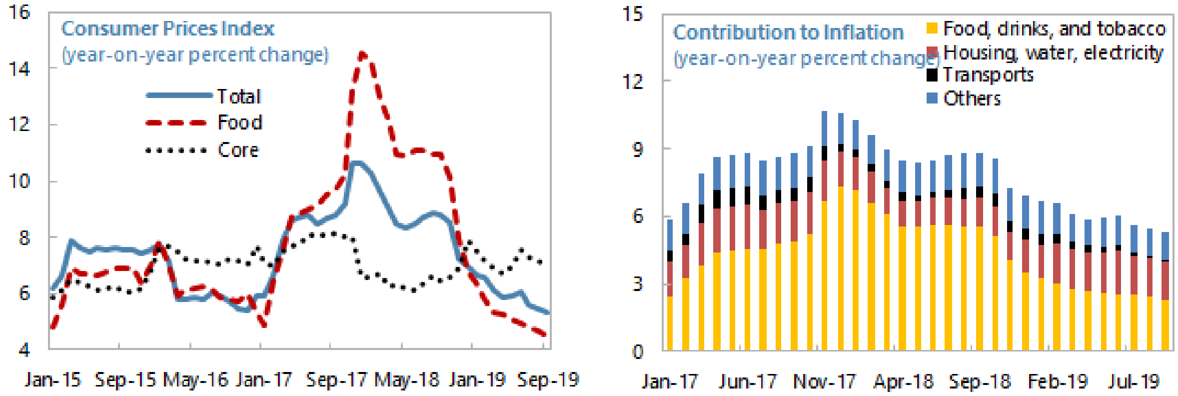
... while tourism is slowly recovering.



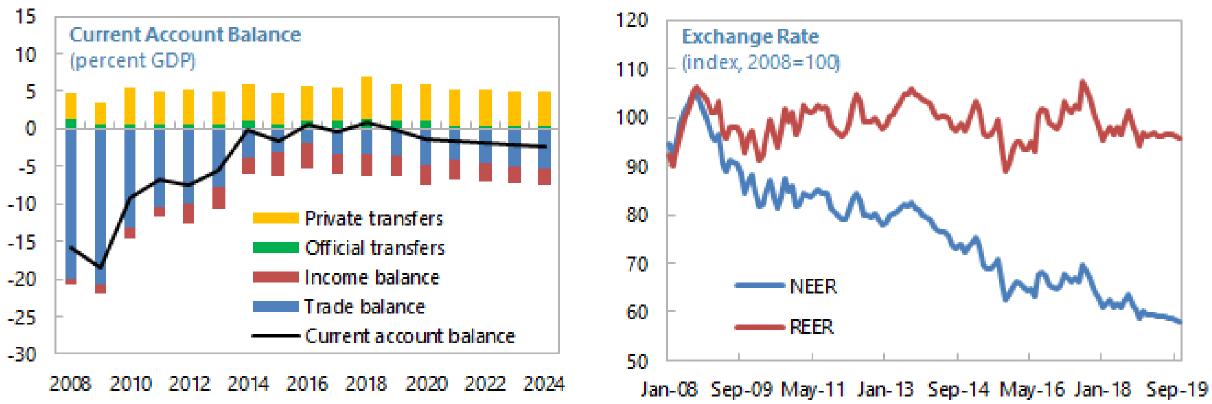
Sources: Malagasy Authorities; and IMF staff estimates.

Figure 4. Madagascar: Inflation and External Developments

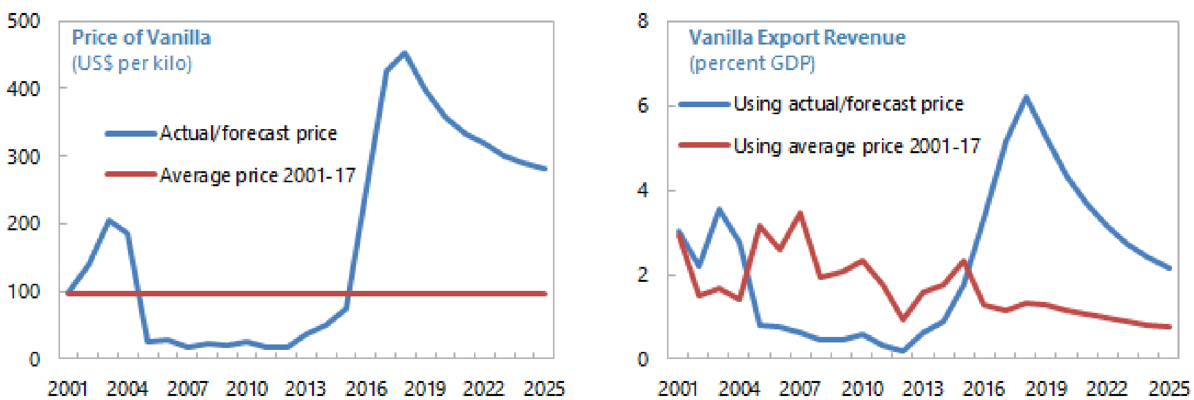
After peaking in December 2017, inflation is gradually declining.



Increasing mining and vanilla exports have improved the current account which is expected to weaken as scaled-up investment drives imports. The real effective exchange rate is relatively stable in recent years.

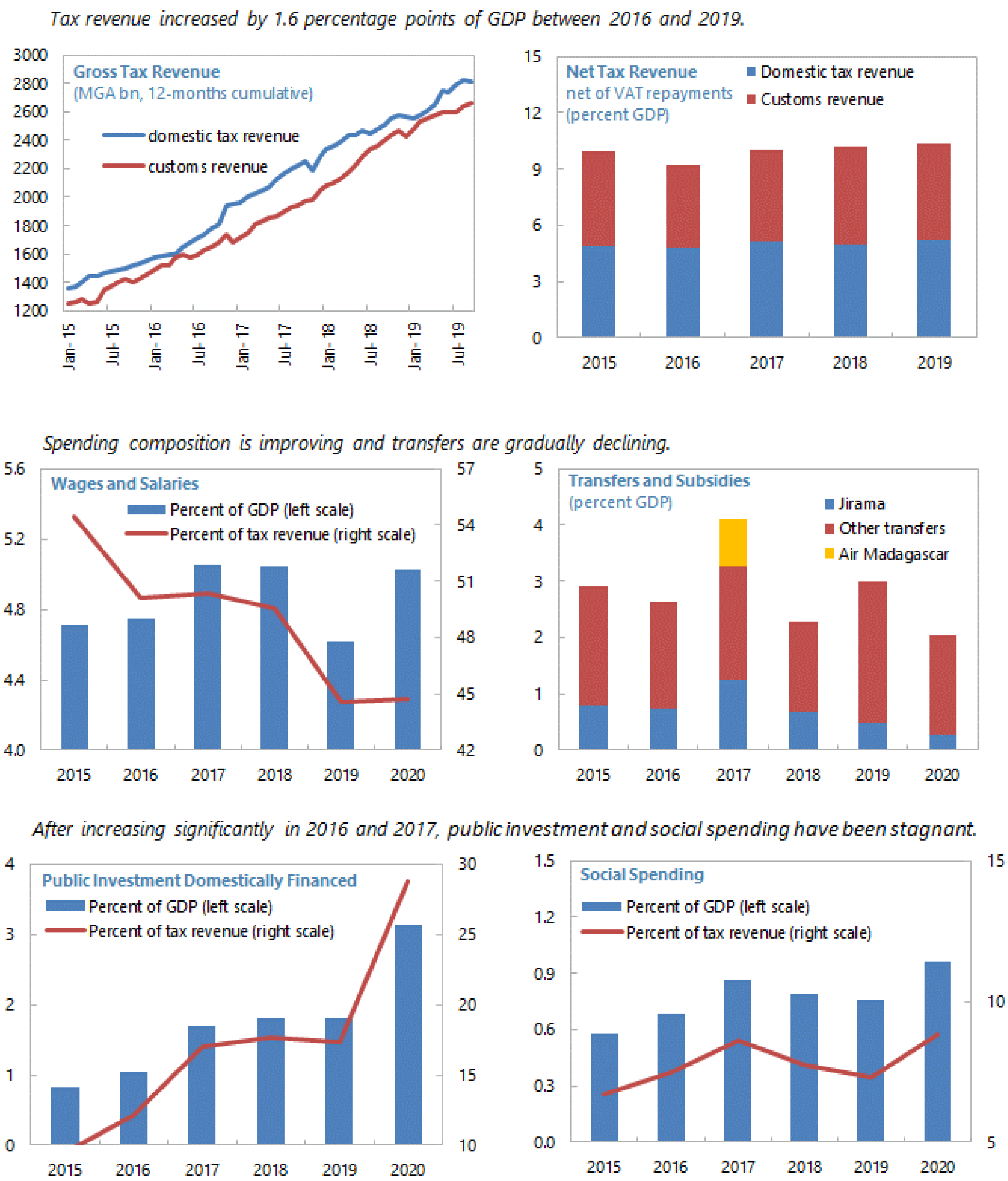


Export revenues have been boosted by high vanilla prices, which are expected to gradually unwind.



Sources: Malagasy Authorities; and IMF staff estimates.

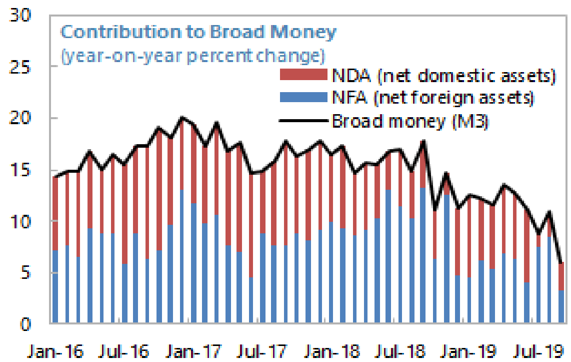
Figure 5. Madagascar: Government Revenue and Spending

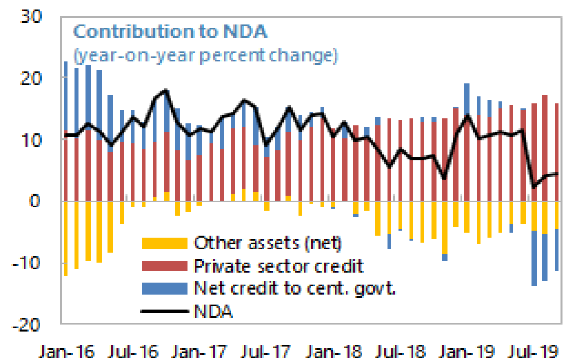


Sources: Malagasy Authorities; and IMF staff estimates.

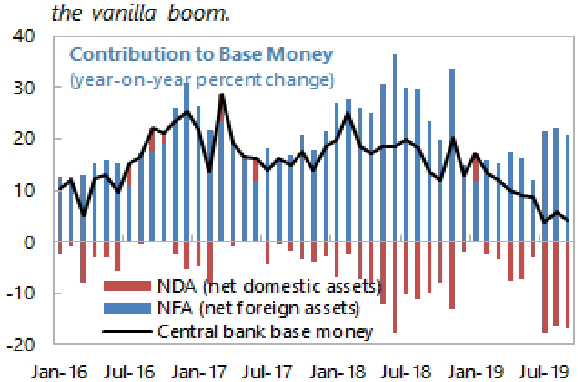
Figure 6. Madagascar: Monetary Developments

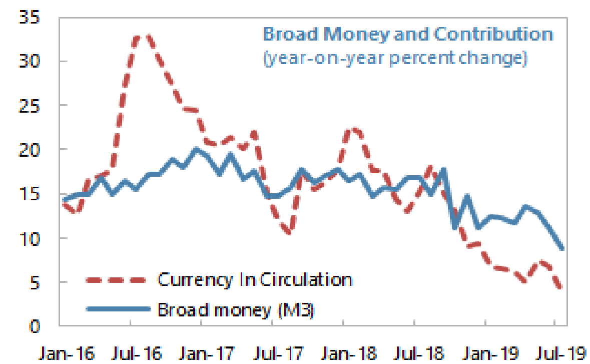
Broad money growth is driven by the accumulation of net foreign assets and credit to the private sector.



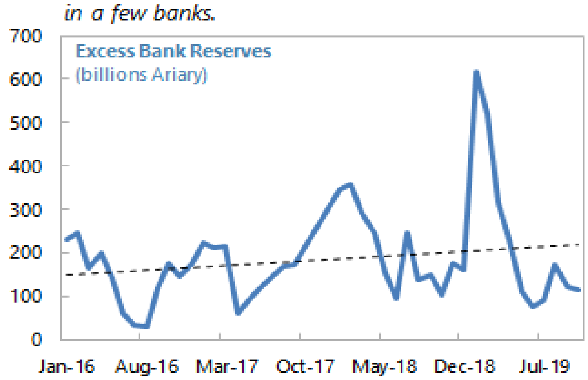


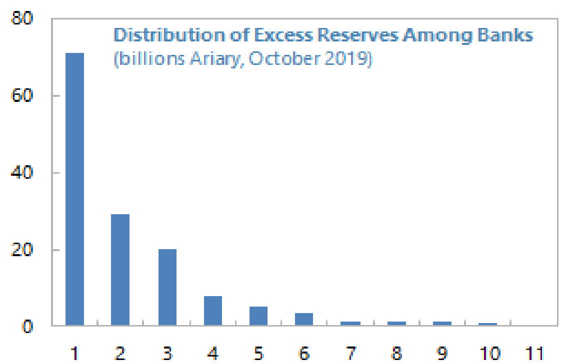
Base money growth is also driven by net foreign assets, while the demand for currency is supported by the vanilla boom.





Excess bank reserves are volatile with strong seasonal effect related to the vanilla cycle, and concentrated in a few banks.

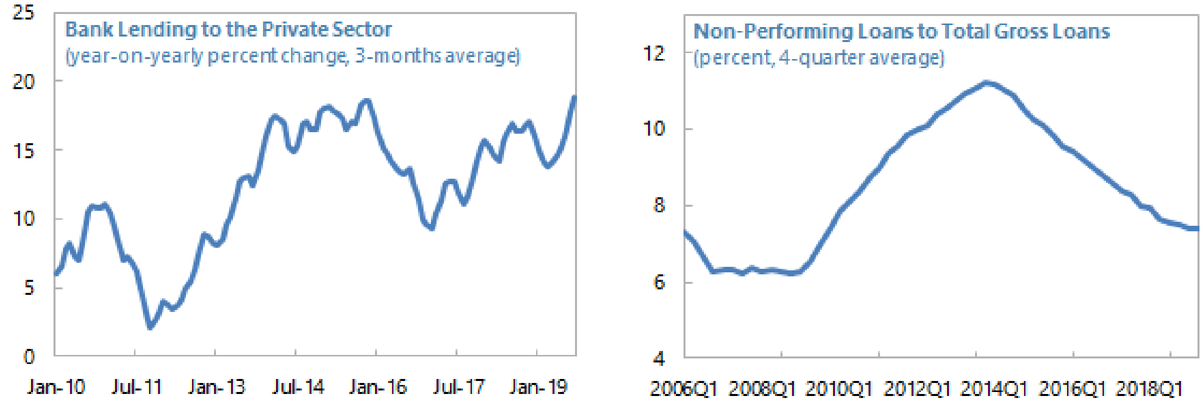




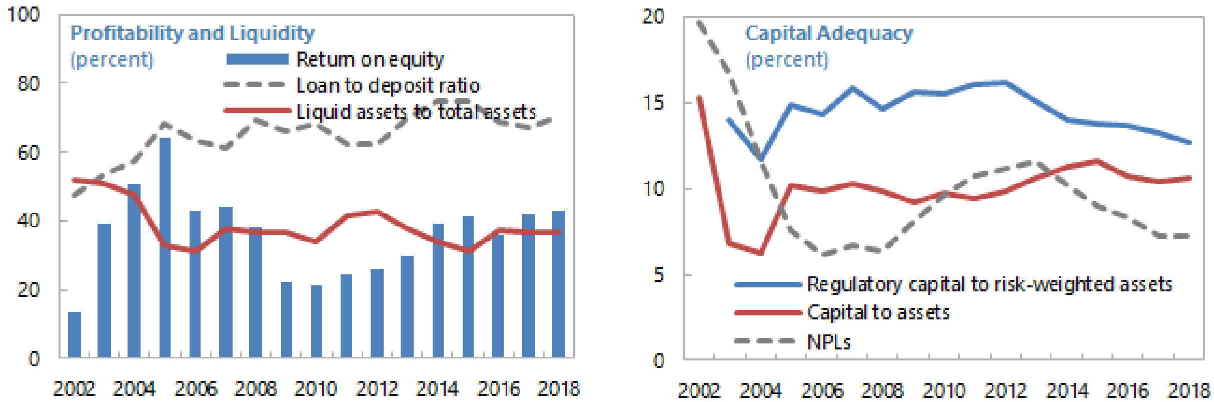
Sources: Malagasy Authorities; and IMF staff estimates.

Figure 7. Madagascar: Financial Sector Developments

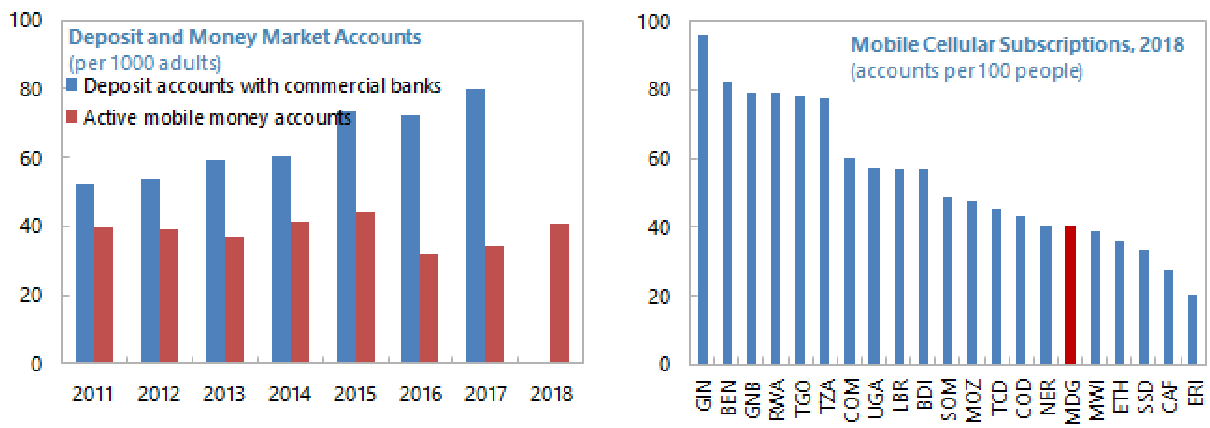
Credit is increasing at a healthy pace, and NPLs continue to decline since their peak in late 2013.



Overall, banks are well capitalized, liquid, and profitable, but significant differences exist among banks.



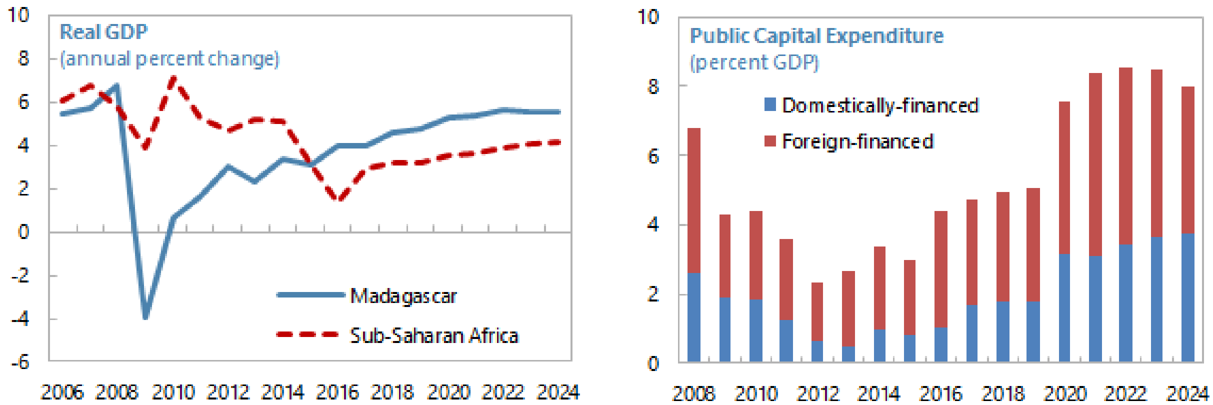
Mobile banking activities are rapidly increasing, but Madagascar lags most SSA low-income countries.



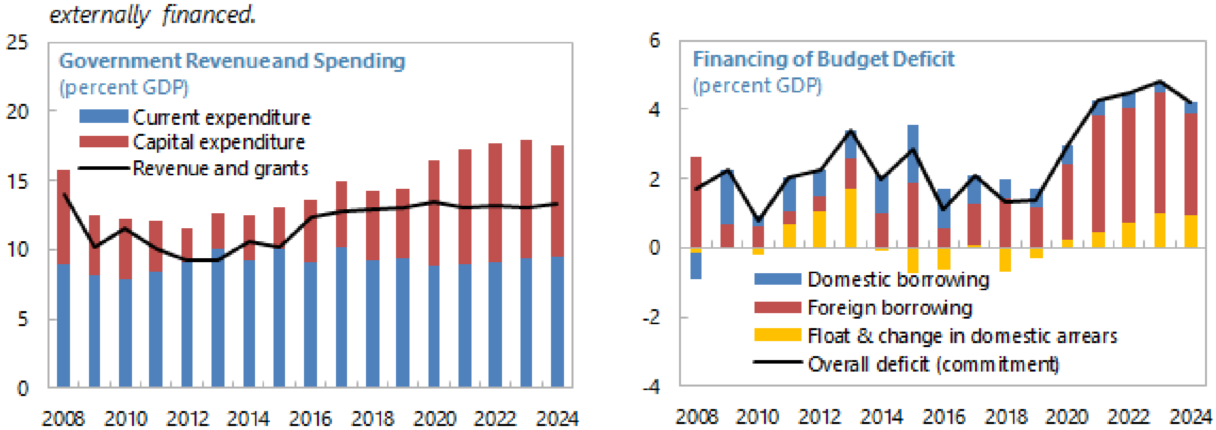
Sources: Malagasy Authorities; 2017 IMF Financial Access Survey; World Bank; and IMF staff estimates.

Figure 8. Madagascar: Medium-Term Macroeconomic Prospects

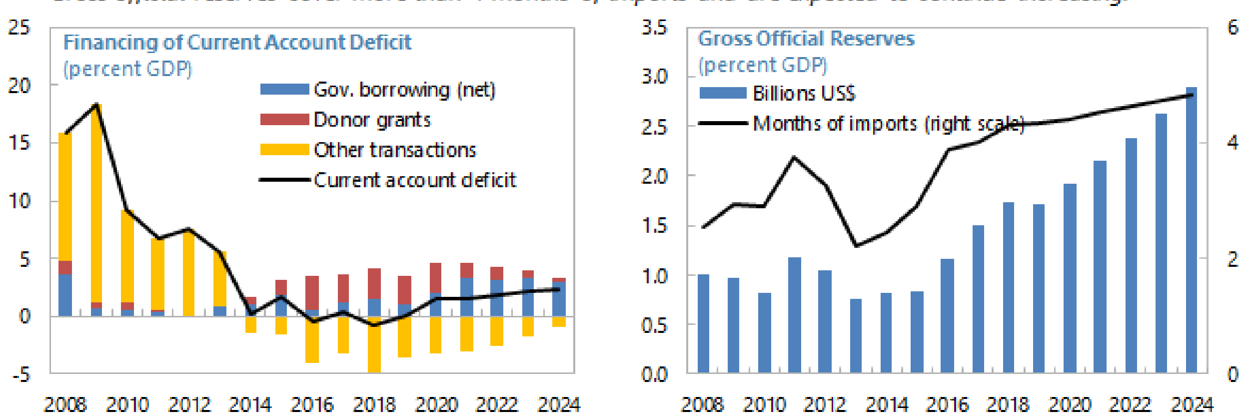
Growth is expected to remain above the Sub-Saharan average, sustained by scaled-up public investment.



Public investment scaling-up is increasing the fiscal deficit (expected to peak in 2020), which is largely externally financed.



Investment-driven increases in the current account deficit will be financed by concessional borrowing. Gross official reserves cover more than 4 months of imports and are expected to continue increasing.



Sources: Malagasy Authorities; and IMF staff estimates.

Table 1. Madagascar: Selected Economic Indicators, 2016-25

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
	Actuals	Prel. Est.	Prel. Est	Proj.	Projections					
	(Percent change; unless otherwise indicated)									
National account and prices										
GDP at constant prices	4.0	3.9	4.6	4.8	5.2	5.4	5.6	5.6	5.6	5.5
GDP deflator	6.1	8.6	8.6	5.9	7.2	6.5	5.6	5.5	5.4	5.4
Consumer prices (end of period)	6.0	10.6	6.9	6.0	6.2	5.9	5.4	5.6	5.6	5.5
Money and credit										
Reserve money	25.4	18.6	13.0	6.5	12.2	11.4	10.6	10.5	10.2	9.6
Broad money (M3)	20.1	17.8	11.2	12.3	16.2	14.9	14.6	14.7	13.4	11.9
	(Growth in percent of beginning of period money stock (M3))									
Net foreign assets	13.0	9.2	4.8	0.3	6.9	7.6	7.0	7.0	7.3	6.6
Net domestic assets	7.0	8.6	6.4	12.0	9.3	7.2	7.6	7.7	6.2	5.3
of which: Credit to the private sector	4.1	8.4	8.7	9.0	7.3	5.8	6.3	6.2	5.3	5.6
	(Percent of GDP)									
Public finance										
Total revenue (excluding grants)	9.5	10.3	10.5	10.6	11.2	11.7	12.0	12.5	13.0	13.3
of which: Tax revenue	9.2	10.0	10.2	10.4	10.9	11.3	11.7	12.2	12.7	13.0
Grants	2.9	2.5	2.5	2.4	2.5	1.4	1.2	0.6	0.4	0.3
of which: budget grants	0.6	0.7	0.9	0.8	0.7	0.0	0.0	0.0	0.0	0.0
Total expenditures	13.5	14.9	14.3	14.4	16.4	17.3	17.7	17.9	17.5	17.2
Current expenditure	9.1	10.2	9.3	9.3	8.9	8.9	9.2	9.4	9.6	9.6
Capital expenditure	4.4	4.7	5.0	5.0	7.6	8.3	8.5	8.4	8.0	7.6
Domestic financed	1.0	1.7	1.8	1.8	3.1	3.1	3.4	3.7	3.7	3.7
Foreign financed	3.4	3.0	3.2	3.2	4.4	5.2	5.1	4.8	4.3	3.8
Overall balance (commitment basis)	-1.1	-2.1	-1.3	-1.4	-2.7	-4.2	-4.5	-4.8	-4.2	-3.6
Float (variation of accounts payable, + = increase)	0.4	0.6	-0.2	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Variation of domestic arrears (+ = increase)	-1.0	-0.6	-0.5	-0.3	-0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (cash basis)	-1.7	-2.0	-2.0	-1.7	-2.7	-4.3	-4.5	-4.8	-4.2	-3.6
Domestic primary balance[1]	0.1	-0.9	0.1	0.3	0.0	0.3	0.2	0.1	0.1	0.4
Total financing	1.7	2.0	2.0	1.7	2.7	3.8	3.7	3.8	3.3	2.9
Foreign borrowing (net)	0.6	1.2	1.5	1.2	2.2	3.3	3.3	3.4	3.0	2.6
Domestic financing	1.1	0.8	0.5	0.5	0.5	0.4	0.4	0.4	0.3	0.3
Excess financing[2]	0.0	0.0	0.0	0.0	-0.2	-1.8	-2.4	-3.8	-4.7	-4.2
Of which: budget support to be programmed	0.0	0.0	0.0	0.0	0.0	-0.5	-0.8	-1.0	-0.9	-0.7
Savings and investment										
Investment	19.0	18.1	18.8	19.1	22.0	23.0	23.7	23.9	23.7	23.4
Government	4.4	4.7	5.0	5.0	7.6	8.3	8.5	8.4	8.0	7.6
Nongovernment	14.6	13.4	13.9	13.9	14.4	14.7	15.2	15.4	15.7	15.8
Gross national savings	16.8	15.4	20.3	19.0	20.5	21.5	21.9	21.8	21.3	21.0
External sector										
Exports of goods, f.o.b.	18.3	21.3	21.9	19.5	19.0	20.1	20.0	19.3	19.0	18.8
Imports of goods, c.i.f.	24.1	27.4	27.6	26.6	27.0	27.3	27.3	27.2	27.1	27.0
Current account balance (exc. grants)	-2.5	-2.9	-1.9	-2.6	-4.0	-2.9	-2.9	-2.7	-2.7	-2.8
Current account balance (inc. grants)	0.5	-0.4	0.7	-0.1	-1.5	-1.5	-1.8	-2.1	-2.4	-2.4
Public debt	40.3	40.0	39.9	40.1	39.8	40.8	42.1	43.8	45.1	45.7
External Public Debt	25.3	25.7	26.7	27.2	27.6	29.1	30.8	32.7	34.1	34.9
Domestic Public Debt	15.0	14.4	13.2	12.8	12.2	11.6	11.3	11.1	11.0	10.9
	(Units as indicated)									
Gross official reserves (millions of SDRs)	834	1086	1221	1238	1390	1552	1712	1870	2046	2226
Months of imports of goods and services	3.9	4.0	4.3	4.3	4.4	4.5	4.6	4.7	4.8	4.9
Real effective exchange rate (pa, percent change)	0.4	5.5	-2.8	...	...	...	...	...	...	...
Terms of trade (percent change, deterioration -)	84.3	14.7	5.6	-12.0	-3.5	6.3	-0.5	-0.8	-0.4	0.3
Memorandum items										
GDP per capita (U.S. dollars)	476	516	528	525	557	588	623	659	698	738
Nominal GDP at market prices (billions of ariary)	37,638	41,059	46,189	51,229	57,786	64,860	72,335	80,552	89,657	99,675

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] Primary balance excl. foreign-financed investment and grants. Commitment basis.

[2] A negative value indicates allocated financing with the disbursement schedule to be agreed.

Table 2. Madagascar: National Accounts, 2016-2025

	2016	2017	2018		2019		2020	2021	2022	2023	2024	2025
	Actuals	Prel. Est.	EBS 19/73[1]	Prel. Est.	EBS 19/73[1]	Proj.	Projections					
	(Percent change)											
Real supply side growth												
Primary sector	1.3	1.3	4.8	3.7	2.5	2.8	3.5	3.5	3.5	3.1	3.2	3.2
Agriculture	0.9	0.7	9.2	7.4	3.3	3.2	4.0	4.0	4.0	3.5	3.5	3.5
Cattle and fishing	2.5	2.4	1.9	-4.5	2.0	2.0	2.5	2.5	2.5	2.5	2.5	2.5
Forestry	1.0	2.8	-0.9	-0.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Secondary sector	4.8	5.8	5.5	8.1	7.1	7.3	7.4	7.6	7.8	8.0	8.0	7.7
Food and drink	4.4	3.5	6.4	2.4	5.9	4.6	5.3	6.1	6.4	6.4	6.4	6.1
Manufacturing	7.6	9.5		3.4		7.6	10.5	11.5	11.7	11.7	11.7	11.3
Energy	7.1	-7.2	8.4	20.0	11.5	9.6	9.7	9.8	10.4	12.8	12.8	12.5
Extractive industry	3.6	10.0	5.4	9.8	6.5	10.2	9.4	9.1	9.1	9.2	9.2	8.9
Other			4.2		4.3							
Tertiary sector	4.6	5.1	5.4	2.1	5.8	4.7	5.1	5.4	5.9	5.9	5.9	5.8
Transportation	-2.4	21.5	5.8	-1.7	7.6	4.8	4.9	4.9	7.7	7.7	7.7	7.7
Services	9.6	2.8	6.6	-0.4	5.8	2.8	3.0	3.7	3.9	3.9	3.9	3.9
Trade	3.2	-0.6	4.5	2.9	3.0	2.7	2.0	2.1	2.3	2.3	2.3	2.3
Banks, Insurance	7.6	14.6		-0.4		4.2	4.3	5.2	5.3	5.3	5.3	5.3
Public administration	-1.1	2.2	1.1	-2.1	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Indirect taxes	10.2	4.1	5.4	13.5	5.7	5.7	7.2	6.5	5.6	5.5	5.5	5.4
Real GDP at market prices	4.0	3.9	5.2	4.6	5.2	4.8	5.2	5.4	5.6	5.6	5.6	5.5
Nominal demand side composition	(Percent of GDP)											
Resource balance	-1.9	-3.3	-3.9	-3.4	-6.2	-3.6	-4.7	-4.2	-4.5	-4.9	-5.1	-5.2
Imports of goods and nonfactor services	30.2	34.2	40.0	34.9	40.9	33.5	33.9	34.4	34.4	34.1	33.9	33.7
Exports of goods and nonfactor services	28.3	30.9	36.0	31.5	34.7	29.9	29.2	30.2	29.9	29.1	28.8	28.5
Current account balance (including grants) = (S-I)	0.5	-0.4	0.8	0.7	-1.9	-0.1	-1.5	-1.5	-1.8	-2.1	-2.4	-2.4
Consumption	86.3	87.7	83.5	85.5	83.8	86.2	84.3	82.8	82.4	82.6	83.0	83.2
Government	14.8	16.1	9.8	14.3	9.4	14.4	13.7	13.8	14.1	14.5	14.7	14.8
Private	71.5	71.6	73.7	71.2	74.4	71.8	70.6	69.0	68.3	68.1	68.2	68.4
Investment (I)	19.0	18.1	20.4	18.8	22.4	19.1	22.0	23.0	23.7	23.9	23.7	23.4
Government	4.4	4.7	5.7	5.0	8.3	5.0	7.6	8.3	8.5	8.4	8.0	7.6
Private	14.6	13.4	14.8	13.9	14.2	14.0	14.4	14.7	15.2	15.4	15.7	15.8
of which: foreign direct investment	3.8	2.7	4.1	2.6	3.2	2.6	2.7	2.7	2.8	2.8	2.8	2.8
National savings (S)	16.8	15.4	21.2	20.3	20.9	19.0	20.5	21.5	21.9	21.8	21.3	21.0
Government	2.6	1.9	4.1	2.9	6.0	2.8	4.1	3.4	3.3	2.9	3.0	3.3
Private	14.3	13.4	17.1	17.5	14.9	16.2	16.4	18.1	18.6	18.9	18.3	17.7
Memoranda items:	(Billions of Ariary)											
Nominal GDP (at market prices)	37,638	41,059	40,318	46,189	45,247	51,229	57,786	64,860	72,335	80,552	89,657	99,675

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] For EBS 19/73, non rebased GDP was still in use.

Table 3. Madagascar: Fiscal Operations of the Central Government, 2017-25 (Billions of Ariary)

	2017	2018	2019		2019		2019		2020	2020	2021	2022	2023	2024	2025
			June		September		December		IMF	LFI*					
	Prel. Est.	Prel. Est.	EBS 19/73	Prel. Est.	EBS 19/73	Prel. Est.	EBS 19/73	Proj.	Projections						
Total revenue and grants	5,272	5,971	3,454	3,064	5,229	5,299	7,407	6,659	7,952	8,217	8,445	9,544	10,528	11,946	13,579
Total revenue	4,240	4,837	2,719	2,765	4,170	4,103	5,647	5,427	6,493	6,910	7,563	8,713	10,038	11,616	13,240
Tax revenue [1]	4,118	4,706	2,656	2,726	4,076	4,030	5,545	5,325	6,292	6,710	7,357	8,490	9,797	11,347	12,941
Domestic taxes	2,094	2,315	1,360	1,394	2,112	1,992	2,955	2,655	3,319	3,760	4,024	4,846	5,748	6,801	7,903
Taxes on international trade and transactions	2,024	2,391	1,296	1,332	1,964	2,038	2,590	2,670	2,973	2,950	3,334	3,644	4,049	4,546	5,038
Non-tax revenue	122	131	62	39	95	73	102	102	200	200	206	222	241	269	299
Grants	1,032	1,134	735	299	1,058	1,195	1,760	1,232	1,460	1,307	882	832	490	330	339
Current grants	298	414	352	1	352	366	751	392	430	350	0	0	0	0	0
Capital grants	733	720	383	298	706	829	1,009	841	1,030	957	882	832	490	330	339
Total expenditure and lending minus repayments	6,135	6,585	3,251	2,775	6,142	4,735	8,440	7,374	9,504	9,882	11,202	12,789	14,407	15,732	17,136
of which: Social priority spending	355	365	205	17	333	100	555	390	555	555	800	1,050	1,300	1,555	1,740
Current expenditure	4,187	4,298	2,089	1,976	3,452	3,015	4,706	4,788	5,132	4,942	5,793	6,631	7,607	8,565	9,577
Wages and salaries	2,076	2,330	1,187	1,121	1,875	1,698	2,575	2,368	2,903	2,903	3,230	3,505	3,890	4,304	4,784
Interest payments	285	353	192	166	259	232	433	433	452	452	448	529	590	682	757
Foreign	70	105	72	52	91	68	146	146	133	133	146	186	234	302	372
Domestic	215	248	120	114	168	164	287	287	319	319	302	343	356	380	385
Other	1,749	1,404	504	353	1,115	986	1,571	1,861	1,602	1,412	2,015	2,516	3,036	3,477	3,923
Goods and services	282	349	92	67	294	176	392	329	428	428	571	866	1,248	1,453	1,655
Transfers and subsidies	1,467	1,055	412	286	821	811	1,179	1,532	1,174	984	1,444	1,650	1,788	2,024	2,268
of which: Air Madagascar	303	0	0	0	0	0	0	0	0	0	0	0	0	0	0
of which: JIRAMA (operating subsidies)	447	309	128	70	191	216	255	255	150	0	150	50	0	0	0
of which: JIRAMA (arrears repayment)	...	...	...	...	...	...	...	501							
Treasury operations (net) [1]	77	211	205	336	204	99	127	127	175	175	100	82	91	101	112
Capital expenditure	1,948	2,287	1,163	799	2,691	1,720	3,734	2,586	4,372	5,041	5,409	6,158	6,800	7,168	7,559
Domestic financed	700	831	245	86	1,153	333	1,537	925	1,810	2,344	2,014	2,485	2,940	3,353	3,728
Foreign financed	1,248	1,456	918	712	1,538	1,387	2,197	1,661	2,562	2,697	3,395	3,673	3,860	3,814	3,831
Overall balance (commitment basis)	-863	-614	203	289	-914	564	-1,033	-715	-1,552	-1,665	-2,757	-3,245	-3,879	-3,786	-3,557
Float (variation of accounts payable, + = increase)	259	-80	-160	-266	144	-193	-83	-19	40	0	-30	-10	0	0	0
Variation of domestic arrears (+ = increase)	-231	-225	-106	-61	-121	-121	-145	-134	-48	-48	0	0	0	0	0
Overall balance (including grants, cash basis)	-835	-918	-64	-38	-891	249	-1,261	-868	-1,559	-1,712	-2,787	-3,255	-3,879	-3,786	-3,557
Domestic primary balance[2]	...	60	577	868	-175	988	-163	146	3	77	204	125	81	381	692
Domestic primary balance (old program definition) [3]	240	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Total financing	835	918	64	38	891	-249	1,260	868	1,559	1,712	2,456	2,707	3,064	2,941	2,846
Foreign borrowing (residency principle)	502	675	432	312	688	395	961	593	1,259	1,365	2,168	2,389	2,771	2,662	2,577
External borrowing, Gross	751	911	535	414	855	558	1,211	844	1,554	1,660	2,512	2,841	3,370	3,485	3,492
Budget support loans	236	176	0	0	23	0	23	24	21	21	0	0	0	0	0
of which: Air Madagascar	0	133	0	0	0	0	0	0	0	0	0	0	0	0	0
Project loans	515	735	535	414	832	558	1,188	820	1,533	1,639	2,512	2,841	3,370	3,485	3,492
Amortization on a due basis (-)	-248	-236	-103	-102	-167	-163	-250	-251	-295	-295	-344	-452	-599	-822	-915
Domestic borrowing (residency principle)	332	243	-368	-274	203	-645	299	275	300	347	287	318	292	279	269
Monetary sector	151	220	-294	-51	239	-482	347	348	300	347	209	217	212	189	219
Non-monetary sector	273	-67	-75	-60	-36	-11	-48	-73	0	0	78	101	81	90	50
Treasury correspondent accounts (net)	-97	77	0	-172	0	-146	0	0	0	0	0	0	0	0	0
Excess financing [4]	0	0	0	0	0	0	0	-1	-97	-175	-1,155	-1,769	-3,092	-4,199	-4,140
of which: budget support to be programmed	0	0	0	0	0	0	0	0	0	0	-331	-548	-816	-845	-712

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] Domestic taxes include MGA 72 bn (0.2 percent of GDP) in 2017 corresponding to tax arrears of Air Madagascar used for its recapitalization, offset in the line Treasury operations (net).

[2] Primary balance excl. foreign-financed investment and grants. Commitment basis.

[3] Up to June 2018, primary balance excl. foreign-financed investment (but grants included).

[4] A negative value indicates allocated financing with the disbursement schedule to be agreed.

* Loi de Finances Initiale (Initial Budget Law), differs from IMF staff projection.

Table 4. Madagascar: Fiscal Operations of the Central Government, 2016-25

(Percent of GDP)

	2016	2017	2018		2019		2020	2021	2022	2023	2024	2025
	Dec	Dec	Dec		December		Dec	Dec	Dec	Dec	Dec	Dec
	Actuals	Prel. Est.	EBS 19/73[5]	Prel. Est.	EBS 19/73[5]	Proj.	Projections					
Total revenue and grants	12.4	12.8	14.8	12.9	16.4	13.0	13.8	13.0	13.2	13.1	13.3	13.6
Total revenue	9.5	10.3	12.0	10.5	12.5	10.6	11.2	11.7	12.0	12.5	13.0	13.3
Tax revenue [1]	9.2	10.0	11.7	10.2	12.3	10.4	10.9	11.3	11.7	12.2	12.7	13.0
Domestic taxes	4.8	5.1	5.7	5.0	6.5	5.2	5.7	6.2	6.7	7.1	7.6	7.9
Taxes on international trade and transactions	4.4	4.9	5.9	5.2	5.7	5.2	5.1	5.1	5.0	5.0	5.1	5.1
Non-tax revenue	0.3	0.3	0.3	0.3	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3
Grants	2.9	2.5	2.8	2.5	3.9	2.4	2.5	1.4	1.2	0.6	0.4	0.3
Current grants	0.6	0.7	1.0	0.9	1.7	0.8	0.7	0.0	0.0	0.0	0.0	0.0
Capital grants	2.3	1.8	1.8	1.6	2.2	1.6	1.8	1.4	1.2	0.6	0.4	0.3
Total expenditure and lending minus repayments	13.5	14.9	16.3	14.3	18.7	14.4	16.4	17.3	17.7	17.9	17.5	17.2
of which: Social priority spending	0.7	0.9	0.9	0.8	1.2	0.8	1.0	1.2	1.5	1.6	1.7	1.7
Current expenditure	9.1	10.2	10.7	9.3	10.4	9.3	8.9	8.9	9.2	9.4	9.6	9.6
Wages and salaries	4.8	5.1	5.8	5.0	5.7	4.6	5.0	5.0	4.8	4.8	4.8	4.8
Interest payments	0.7	0.7	0.9	0.8	1.0	0.8	0.8	0.7	0.7	0.7	0.8	0.8
Foreign	0.2	0.2	0.3	0.2	0.3	0.3	0.2	0.2	0.3	0.3	0.3	0.4
Domestic	0.6	0.5	0.6	0.5	0.6	0.6	0.6	0.5	0.5	0.4	0.4	0.4
Other	3.1	4.3	3.5	3.0	3.5	3.6	2.8	3.1	3.5	3.8	3.9	3.9
Goods and services	0.5	0.7	0.9	0.8	0.9	0.6	0.7	0.9	1.2	1.5	1.6	1.7
Transfers and subsidies	2.6	3.6	2.6	2.3	2.6	3.0	2.0	2.2	2.3	2.2	2.3	2.3
of which: Air Madagascar	0.0	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
of which: JIRAMA (operating subsidies)	0.7	1.1	0.8	0.7	0.6	0.5	0.3	0.2	0.1	0.0	0.0	0.0
of which: JIRAMA (arrears repayment)						1.0						
Treasury operations (net) [1]	0.5	0.2	0.5	0.5	0.3	0.2	0.3	0.2	0.1	0.1	0.1	0.1
Capital expenditure	4.4	4.7	5.7	5.0	8.3	5.0	7.6	8.3	8.5	8.4	8.0	7.6
Domestic financed	1.0	1.7	2.1	1.8	3.4	1.8	3.1	3.1	3.4	3.7	3.7	3.7
Foreign financed	3.4	3.0	3.6	3.2	4.9	3.2	4.4	5.2	5.1	4.8	4.3	3.8
Overall balance (commitment basis)	-1.1	-2.1	-1.5	-1.3	-2.3	-1.4	-2.7	-4.2	-4.5	-4.8	-4.2	-3.6
Float (variation of accounts payable, + = increase)	0.4	0.6	-0.2	-0.2	-0.2	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Variation of domestic arrears (+ = increase)	-1.0	-0.6	-0.6	-0.5	-0.3	-0.3	-0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (including grants, cash basis)	-1.7	-2.0	-2.3	-2.0	-2.8	-1.7	-2.7	-4.3	-4.5	-4.8	-4.2	-3.6
Domestic primary balance[2]	0.1	-0.9	0.1	0.1	-0.4	0.3	0.0	0.3	0.2	0.1	0.4	0.7
Domestic primary balance (old program definition) [3]	0.7	0.6	...	...	...	...	...	...	...	...	...	...
Total financing	1.7	2.0	2.3	2.0	2.8	1.7	2.7	3.8	3.7	3.8	3.3	2.9
Foreign borrowing (residency principle)	0.6	1.2	1.7	1.5	2.1	1.2	2.2	3.3	3.3	3.4	3.0	2.6
External borrowing, Gross	1.2	1.8	2.3	2.0	2.7	1.6	2.7	3.9	3.9	4.2	3.9	3.5
Budget support loans	0.1	0.6	0.4	0.4	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
of which: Air Madagascar	0.0	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	1.0	1.3	1.8	1.6	2.6	1.6	2.7	3.9	3.9	4.2	3.9	3.5
Amortization on a due basis (-)	-0.6	-0.6	-0.6	-0.5	-0.6	-0.5	-0.5	-0.5	-0.6	-0.7	-0.9	-0.9
Domestic borrowing (residency principle)	1.1	0.8	0.6	0.5	0.7	0.5	0.5	0.4	0.4	0.4	0.3	0.3
Monetary sector	0.6	0.4	0.5	0.5	0.8	0.7	0.5	0.3	0.3	0.3	0.2	0.2
Non-monetary sector	0.7	0.7	-0.2	-0.1	-0.1	-0.1	0.0	0.1	0.1	0.1	0.1	0.0
Treasury correspondent accounts (net)	-0.2	-0.2	0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Excess financing [4]	0.0	0.0	0.0	0.0	0.0	0.0	-0.2	-1.8	-2.4	-3.8	-4.7	-4.2
of which: budget support to be programmed	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.5	-0.8	-1.0	-0.9	-0.7

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] Domestic taxes include 0.2 percent of GDP in 2017 corresponding to tax arrears of Air Madagascar used for its recapitalization, offset in the line Treasury operations (net).

[2] Primary balance excl. foreign-financed investment and grants. Commitment basis.

[3] Up to June 2018, primary balance excl. foreign-financed investment (but grants included).

[4] A negative value indicates allocated financing with the disbursement schedule to be agreed.

[5] For EBS 19/73, non rebased GDP was still in use.

Table 5. Madagascar: Balance of Payments, 2017-25

	2017	2018		2019		2020	2021	2022	2023	2024	2025
	Prel. Est.	EBS 19/73[3]	Prel. Est.	EBS 19/73[3]	Proj.	Projections					
					(Millions of SDRs)						
Current account	-40.1	68.9	69.6	-172.3	-10.1	-163.9	-184.6	-231.2	-295.5	-356.4	-395.6
Goods and services	-316.5	-335.5	-335.5	-560.5	-368.1	-521.5	-499.1	-583.8	-689.2	-772.7	-842.7
Trade balance of goods	-322.3	-324.2	-324.2	-523.1	-466.2	-605.9	-552.2	-620.7	-736.6	-838.3	-929.2
Exports, f.o.b.	2,020.9	2,143.3	2,143.3	2,111.4	1,995.7	2,118.3	2,417.3	2,583.2	2,699.7	2,852.1	3,051.8
of which: Mining	510.3	593.7	593.7	637.7	569.9	695.6	731.6	786.4	817.0	842.6	881.9
of which: Vanilla	488.9	605.0	605.0	460.5	535.8	481.0	439.2	409.4	378.4	360.8	350.0
Imports, f.o.b.	-2,343.2	-2,467.4	-2,467.4	-2,634.6	-2,461.9	-2,724.2	-2,969.6	-3,203.9	-3,436.3	-3,690.4	-3,981.0
of which: Petroleum products	-343.5	-387.1	-387.1	-413.1	-423.5	-431.6	-463.6	-488.6	-517.9	-552.3	-582.5
of which: Food	-398.8	-373.3	-373.3	-325.4	-340.8	-363.4	-375.5	-386.6	-398.2	-383.6	-401.9
of which: Intermediate goods and capital	-924.2	-997.5	-997.5	-1,131.6	-963.8	-1,183.2	-1,193.4	-1,284.5	-1,388.5	-1,546.7	-1,688.6
Services (net)	5.8	-11.3	-11.3	-37.4	98.1	84.3	53.1	36.9	47.4	65.7	86.6
Receipts	917.2	935.0	935.0	1,026.4	1,059.5	1,134.4	1,205.2	1,280.5	1,364.3	1,468.1	1,590.4
Payments	-911.4	-946.3	-946.3	-1,063.8	-961.4	-1,050.1	-1,152.1	-1,243.7	-1,316.9	-1,402.4	-1,503.9
Income (net)	-255.3	-281.5	-280.8	-220.6	-260.8	-301.1	-302.8	-308.6	-314.5	-334.7	-363.2
Receipts	27.3	39.1	39.8	43.8	41.4	47.9	55.0	63.3	72.8	82.5	85.0
Payments	-282.7	-320.5	-320.5	-264.4	-302.3	-348.9	-357.8	-371.8	-387.2	-417.2	-448.1
of which: interest on public debt	-16.1	-22.3	-22.3	-29.0	-29.3	-25.7	-27.1	-33.3	-40.5	-50.7	-60.7
Current transfers (net)	531.6	685.8	685.8	640.8	618.8	658.6	617.2	661.1	708.2	755.0	810.3
Official transfers	105.7	125.7	125.7	197.0	118.5	123.0	43.4	46.3	49.4	53.2	57.6
of which: Budget aid [1]	65.5	85.2	85.2	154.1	82.8	82.8	0.0	0.0	0.0	0.0	0.0
of which: Other (net)	40.2	40.4	40.4	42.9	35.8	40.2	43.4	46.3	49.4	53.2	57.6
Private transfers	425.9	560.2	560.2	443.8	500.3	535.6	573.9	614.9	658.7	701.8	752.7
Capital and financial account	208.8	41.5	40.8	230.8	-33.2	291.0	298.0	311.6	348.6	431.5	509.6
Capital account[1]	168.4	170.6	170.6	201.4	167.7	198.5	163.2	148.8	84.9	55.2	55.3
of which: Project grant [1]	168.4	170.6	170.6	201.4	167.7	198.5	163.2	148.8	84.9	55.2	55.3
Financial account	42.6	-65.1	-111.3	29.5	-200.9	92.6	134.8	162.8	263.7	376.3	454.3
Foreign direct and portfolio investment	258.1	350.7	253.0	285.5	268.3	298.5	326.4	357.2	393.8	423.8	459.1
Other investment	-215.5	-415.9	-364.3	-256.0	-469.3	-205.9	-191.6	-194.4	-130.0	-47.5	-4.8
Government	116.7	154.4	154.4	192.1	113.3	232.5	390.2	415.7	458.0	446.0	420.6
Drawing	174.1	204.5	204.5	242.0	163.6	295.4	464.7	508.1	584.0	583.7	570.0
Project drawings [1]	118.9	167.4	167.4	237.1	163.6	295.4	464.7	508.1	584.0	583.7	570.0
Budgetary support [1]	55.2	37.1	37.1	4.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	-57.4	-50.1	-50.1	-49.8	-50.3	-62.9	-74.5	-92.3	-126.0	-137.7	-149.4
Private sector	-98.1	-131.6	-155.6	-172.2	-239.2	-238.6	-242.6	-247.6	-252.1	-254.6	-257.1
Banks	1.8	38.4	38.4	2.6	-29.8	0.0	0.0	0.0	0.0	0.0	0.0
Other (inc. unrepatriated export revenues)	-235.9	-483.0	-407.5	-273.4	-373.2	-199.7	-339.3	-362.6	-336.0	-238.8	-168.3
Errors and omissions	-2.2	-63.9	-18.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	168.7	110.5	110.5	58.5	-43.3	127.1	113.3	80.4	53.1	75.1	114.1
Financing	-168.7	-110.5	-110.5	-90.5	43.3	-127.1	-174.5	-178.3	-194.5	-220.7	-230.3
Central bank (net; increase = –)	-168.7	-110.5	-110.5	-90.5	43.3	-127.1	-174.5	-178.3	-194.5	-220.7	-230.3
Use of IMF credit (net)	83.5	24.4	24.4	59.9	59.9	25.3	-12.2	-18.5	-37.2	-44.6	-49.9
Other assets, net (increase = –) [2]	-252.3	-134.9	-134.9	-150.4	-16.6	-152.4	-162.3	-159.8	-157.3	-176.1	-180.3
Debt relief and cancellation	0.0	0.0	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	32.0	0.0	0.0	61.2	97.9	141.3	145.5	116.2
Financing gap	0.0	0.0	0.0	32.0	0.0	0.0	61.2	97.9	141.3	145.5	116.2
					(Percent of GDP; unless otherwise indicated)						
Memorandum items:											
Grants	2.5	3.0	2.6	3.9	2.5	2.5	1.4	1.2	0.6	0.4	0.3
Loans	1.8	2.4	2.1	2.7	1.6	2.7	3.9	3.9	4.2	3.9	3.5
Direct investment	2.7	4.1	2.6	3.2	2.6	2.7	2.7	2.8	2.8	2.8	2.8
Current account											
Excluding net official transfers	-2.9	-2.2	-1.9	-5.8	-2.6	-4.0	-2.9	-2.9	-2.7	-2.7	-2.8
Including net official transfers	-0.4	0.8	0.7	-1.9	-0.1	-1.5	-1.5	-1.8	-2.1	-2.4	-2.4
Debt service (percent of exports of goods)	2.7	7.9	1.7	20.2	4.1	3.7	3.4	3.3	3.3	3.1	2.8
Export of goods volume (percent change)	-4.2	-4.9	-4.8	16.1	8.3	8.6	8.4	8.0	5.6	6.2	6.4
Import of goods volume (percent change)	13.6	-0.2	-0.2	6.3	2.2	9.3	10.1	8.5	7.5	7.5	7.6
Gross official reserves (millions of SDR)	1,086	1,221	1,221	1,372	1,238	1,390	1,552	1,712	1,870	2,046	2,226
Months of imports of goods and nonfactor services	4.0	4.3	4.3	4.5	4.3	4.4	4.5	4.6	4.7	4.8	4.9
Terms of trade (percent change, deterioration -)	14.7	5.7	5.6	-15.5	-12.0	-3.5	6.3	-0.5	-0.8	-0.4	0.3
Exchange rate (ariary/US$, period average)	3,116	3,335	3,335	3,603	3,632	...	...	...	...	...	...
Nominal GDP	13,176		13,851		14,106	15,365	16,639	18,045	19,575	21,221	22,989

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] Includes official external financial support only with a disbursement schedule.

[2] Includes reserve accumulation.

[3] For EBS 19/73, non rebased GDP was still in use.

Table 6. Madagascar: Monetary Accounts, 2017-25[1]

(Billions of Ariary; unless otherwise indicated)

	2017	2018		2019		2020	2021	2022	2023	2024	2025
	Dec	December		December		Dec	Dec	Dec	Dec	Dec	Dec
	Actuals	EBS 19/73	Prel. Estim.	EBS 19/73	Proj.	Projections					
Net foreign assets	4,417	4,927	4,927	5,654	4,964	5,882	7,055	8,292	9,721	11,407	13,149
Net foreign assets (BCM)	3,527	4,207	4,207	4,895	4,207	5,088	6,232	7,443	8,843	10,500	12,218
Net foreign assets (deposit money banks)	890	720	720	759	757	794	823	849	877	908	931
Net domestic assets	6,191	6,871	6,871	7,999	8,288	9,518	10,633	11,981	13,537	14,971	16,360
Domestic credit	7,001	7,935	7,935	9,500	9,697	11,000	12,018	13,167	14,534	15,949	17,648
Net credit to government	2,093	2,099	2,099	2,795	2,795	3,133	3,265	3,315	3,438	3,582	3,811
BCM	886	947	947	1,041	1,037	1,051	1,051	989	949	911	868
DMBs	938	1,096	1,096	1,350	1,355	1,667	1,786	1,885	2,036	2,204	2,462
Gross credits (mainly BTAs)	1,327	1,617	1,617	1,902	1,904	2,221	2,374	2,506	2,693	2,898	3,195
Deposits	-389	-521	-521	-552	-549	-554	-588	-622	-657	-694	-733
Other credits	269	55	55	404	403	416	429	441	453	468	481
Credit to the economy	4,907	5,836	5,836	6,705	6,903	7,867	8,752	9,853	11,095	12,367	13,837
Credit to public enterprises	42	40	40	40	40	40	40	40	40	41	42
Credit to private sector	4,846	5,765	5,765	6,635	6,832	7,797	8,693	9,803	11,056	12,300	13,767
Other credits	19	31	31	31	31	31	20	10	0	26	27
Other items (net)	-810	-1,064	-1,064	-1,351	-1,310	-1,382	-1,384	-1,186	-996	-978	-1,288
BCM	406	269	269	223	263	228	253	253	253	253	257
Other	-1,216	-1,332	-1,332	-1,574	-1,572	-1,610	-1,637	-1,439	-1,249	-1,230	-1,545
Money and quasi-money (M3)	10,608	11,798	11,798	13,653	13,252	15,400	17,689	20,273	23,258	26,378	29,509
Foreign currency deposits	1,006	1,202	1,202	1,241	1,038	1,075	1,104	1,077	1,106	1,254	1,403
Short term obligations of commercial banks	51	60	60	51	51	51	51	51	51	51	51
Broad money (M2)	9,551	10,536	10,536	12,362	12,163	14,274	16,534	19,145	22,102	25,074	28,055
Currency in circulation	3,101	3,391	3,391	3,848	3,659	3,970	4,475	5,065	5,654	6,281	6,878
Demand deposits in local currency	3,506	3,687	3,687	4,549	4,539	5,441	6,399	7,504	8,799	10,083	11,387
Quasi-money including time deposits	2,943	3,458	3,458	3,965	3,965	4,863	5,660	6,576	7,648	8,710	9,790
Reserve money	4,559	5,153	5,153	6,042	5,489	6,158	6,857	7,581	8,379	9,236	10,124
	(Percentage change relative to broad money at beginning of the year)										
Net foreign assets	10.4	5.3	5.3	6.9	0.4	7.5	8.2	7.5	7.5	7.6	6.9
Net foreign assets (BCM)	10.2	7.1	7.1	6.5	0.0	7.2	8.0	7.3	7.3	7.5	6.9
Net foreign assets (deposit money banks)	0.1	-1.8	-1.8	0.4	0.4	0.3	0.2	0.2	0.1	0.1	0.1
Net domestic assets	9.6	7.1	7.1	10.7	13.4	10.1	7.8	8.2	8.1	6.5	5.5
Domestic credit	10.3	9.8	9.8	14.9	16.7	10.7	7.1	7.0	7.1	6.4	6.8
Net credit to government	1.3	0.1	0.1	6.6	6.6	2.8	0.9	0.3	0.6	0.6	0.9
BCM	-1.8	0.6	0.6	0.9	0.8	0.1	0.0	-0.4	-0.2	-0.2	-0.2
DMBs	3.7	1.7	1.7	2.4	2.5	2.6	0.8	0.6	0.8	0.8	1.0
Other credits	-0.6	-2.2	-2.2	3.3	3.3	0.1	0.1	0.1	0.1	0.1	0.1
Credit to the economy	9.1	9.7	9.7	8.3	10.1	7.9	6.2	6.7	6.5	5.8	5.9
Credit to public enterprises	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Credit to private sector	9.4	9.6	9.6	8.3	10.1	7.9	6.3	6.7	6.5	5.6	5.9
Other credits	0.0	0.1	0.1	0.0	0.0	0.0	-0.1	-0.1	-0.1	0.1	0.0
Other items (net; asset = +)	-0.7	-2.7	-2.7	-2.7	-2.3	-0.6	0.0	1.2	1.0	0.1	-1.2
	(Percentage change year-on-year)										
Broad money (M2)	19.3	10.3	10.3	17.3	15.4	17.4	15.8	15.8	15.4	13.4	11.9
Currency in circulation	17.8	9.4	9.4	13.5	7.9	8.5	12.7	13.2	11.6	11.1	9.5
Demand deposits in local currency	23.2	5.2	5.2	23.4	23.1	19.9	17.6	17.3	17.3	14.6	12.9
Quasi-money in local currency	16.4	17.5	17.5	14.7	14.7	22.6	16.4	16.2	16.3	13.9	12.4
Credit to the private sector (in nominal terms)	18.4	19.0	19.0	15.1	18.5	14.1	11.5	12.8	12.8	11.3	11.9
Credit to the private sector (in real terms)	7.8	12.9	12.0	8.7	12.5	7.9	5.6	7.4	7.2	5.7	6.4
Memorandum items:											
Credit to private sector (percent of GDP)	11.8	...	12.5	...	13.3	13.5	13.4	13.6	13.7	13.7	13.8
Money multiplier (M3/reserve money)	2.3	2.3	2.3	2.3	2.4	2.5	2.6	2.7	2.8	2.9	2.9
Velocity of money (GDP/end-of-period M3)	3.9	3.4	3.9	3.3	3.9	3.8	3.7	3.6	3.5	3.4	3.4

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] End of period.

Table 7. Madagascar: Balance Sheet of the Central Bank, 2017-19[1]

(Billions of Ariary; unless otherwise indicated)

	2017	2018					2019					
	Dec	March	June	Sep	December		March		June		December	
	Actuals	Actuals	Actuals	Actuals	EBS 19/73	Actuals	EBS 19/73	Prel. Est.	EBS 19/73	Proj.	EBS 19/73	Proj.
Net foreign assets	3,527	3,544	3,577	3,583	4,207	4,207	4,222	4,222	4,580	4,103	4,895	4,207
Gross foreign assets	4,985	5,039	5,063	5,253	5,876	5,876	5,958	5,958	6,501	6,011	6,959	6,266
Gross foreign liabilities	-1,458	-1,495	-1,487	-1,670	-1,669	-1,669	-1,736	-1,736	-1,920	-1,909	-2,063	-2,059
Net domestic assets	1,032	913	794	1,118	945	945	765	765	192	655	1,146	1,281
Credit to government (net)	886	885	845	949	947	947	732	732	253	606	1,041	1,037
Claims on central government	1,275	1,134	1,132	1,223	1,269	1,269	1,037	1,037	1,089	1,030	1,390	1,464
Statutory advances	174	84	84	98	212	212	0	0	0	0	255	255
Securitized debt (T-bonds and bills)	786	776	765	754	744	744	733	733	722	722	701	701
Discounted bills of exchange	39	0	0	78	17	17	0	0	0	0	0	50
On-lending of funds	n.a.	n.a.	n.a.	292	295	295	303	303	301	306	311	316
Other credits	n.a.	n.a.	n.a.	1	1	1	1	1	66	1	123	143
Government deposits	-389	-250	-287	-274	-321	-321	-305	-305	-837	-423	-349	-428
Claims on other sectors	15	17	17	17	16	16	18	18	21	20	20	20
Claims on banks: Liquidity operations (+ = injection)	-276	-465	-445	-133	-287	-287	-245	-245	-380	-185	-137	-38
Other items (net; asset +)	406	477	377	285	269	269	260	260	298	214	223	263
Reserve money	4,559	4,458	4,371	4,700	5,098	5,153	4,988	4,988	4,772	4,758	6,042	5,489
Currency in circulation	3,101	2,969	3,041	3,358	3,337	3,391	3,150	3,150	3,411	3,244	3,848	3,659
Bank reserves	1,457	1,488	1,329	1,342	1,507	1,507	1,575	1,575	1,104	1,263	1,927	1,776
Currency in banks	236	217	234	218	281	281	226	226	226	264	226	254
Deposits	1,221	1,271	1,095	1,124	1,226	1,226	1,349	1,349	878	999	1,701	1,522
Resident deposits	1	1	1	1	255	255	255	263	257	251	267	52
	(Cumulative annual flows, unless otherwise stated)											
Memorandum items:												
Net foreign assets	818	17	50	56	681	681	15	15	373	-105	688	0
Net foreign assets (Millions of SDRs)	165	-12	0	-24	106	106	-23	-23	35	-55	91	-43
Net domestic assets	-104	-118	-238	86	-87	-87	-180	-180	-753	-290	201	336
Credit to government (net)	-142	-1	-41	63	62	62	-215	-215	-695	-341	93	89
Reserve money	714	-101	-188	142	594	594	-165	-165	-380	-395	889	336
Exchange Rate (MDG/SDR, end of period)	4,589	4,686	4,657	4,811	4,812	4,812	...	4,961	...	5,010	...	5,062
Net foreign assets (Millions of SDRs)	769	756	768	745	874	874	851	851	910	819	965	831

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] End of period.

Table 8. Madagascar: Financial Soundness Indicators, 2009-19[1]

(Ratios, percent)

	2009 Dec	2010 Dec	2011 Dec	2012 Dec	2013 Dec	2014 Dec	2015 Dec	2016 Dec	2017 Dec	2018 Mar	2018 June	2018 Sep	2018 Dec	2019 Mar	2019 June
Capital Adequacy															
Regulatory capital to risk-weighted assets	15.6	15.5	16.0	16.2	15.1	14.0	13.8	13.6	13.2				12.7		
Capital to assets	9.2	9.8	9.4	9.8	10.6	11.2	11.6	10.7	10.4	10.7	9.4	9.7	10.6	10.9	9.4
Regulatory Tier 1 capital to risk-weighted assets	16.2	16.1	17.0	16.9	16.0	14.6	14.8	14.1	0.0				12.6		
Tier 1 to assets	7.8	8.2	7.9	8.1	8.6	8.5	8.7	8.0	7.5				7.2		
Non-performing loans net of provisions to capital	25.0	25.3	26.0	22.0	25.6	20.9	19.5	16.5	15.5	16.9	16.6	17.5	15.8	15.5	18.0
Net open position in equities to capital	5.2	4.8	5.2	4.4	4.8	5.2	5.4	5.1	4.6	4.3	5.0	4.8	4.1	4.0	4.6
Asset Quality															
Non-performing loans to total gross loans	8.1	9.6	10.7	11.1	11.6	10.1	9.0	8.4	7.3	7.9	7.2	7.8	7.2	7.6	7.2
Earnings and Profitability															
Return on assets	2.2	2.1	2.4	2.6	3.0	4.2	4.6	3.9	4.4	4.5	4.6	4.4	4.4	3.8	3.9
Return on equity	22.5	21.2	24.5	26.2	30.0	38.9	41.5	35.9	41.9	43.2	45.2	43.4	43.1	36.9	39.3
Interest margin to gross income	58.1	59.3	59.2	60.5	60.9	56.5	55.0	60.5	62.0	63.6	62.5	61.9	61.1	62.1	62.0
Non-interest expenses to gross income	59.5	60.5	61.5	65.1	62.2	55.2	55.0	58.4	55.5	53.6	54.2	54.3	54.5	57.1	55.6
Trading income to total income	7.9	7.8	5.7	4.9	3.8	8.2	8.1	4.9	3.8	4.0	3.9	4.2	4.9	5.1	5.4
Personnel expenses to non-interest expenses	29.9	31.0	30.1	31.4	32.8	34.2	33.1	32.9	33.0	34.1	32.5	32.0	31.5	32.2	32.9
Liquidity															
Liquid assets to total assets (liquid asset ratio)	36.8	33.8	41.6	42.9	37.8	34.1	31.3	37.3	36.8	40.2	38.5	38.6	36.8	39.4	35.9
Liquid assets to short-term liabilities	56.0	50.7	60.4	64.0	56.4	51.5	46.9	54.6	53.4	59.7	55.6	58.8	54.8	58.3	51.5
Customer deposits to total (non-interbank) loans	163.8	164.5	164.9	177.7	150.4	144.7	137.4	145.6	146.3	144.6	144.2	151.6	139.6	147.9	141.4
Sensitivity to Market Risk															
Net open position in foreign exchange to capital	18.2	18.4	13.7	9.6	12.8	10.9	11.7	8.6	9.0	6.7	3.4	3.2	5.7	4.3	4.1
Spread between reference lending and deposit rates (basis point)	1,065	1,120	1,167	1,186	1,245	1,202	1,162	1,180	1,187	1,146	1,143	1,144	1,149	1,079	1,082
Foreign currency-denominated loans to total loans	20.8	23.6	20.5	20.7	16.1	15.6	15.8	12.8	15.0	12.2	11.9	11.8	12.1	13.1	12.9
Foreign currency-denominated liabilities to total liabilities	17.8	19.3	18.3	17.5	16.3	17.5	16.6	15.7	15.0	14.6	14.4	18.1	13.9	12.9	13.5

Source: Malagasy authorities.
[1] Ratios only concern banking sector.

Table 9. Madagascar: External Financing Requirements and Sources, 2016-19

(Millions of U.S. Dollars)

	2016	2017	2018	2019
		Prel. Est.		Proj.
Total financing requirements	911	960	934	915
Current account deficit	-57	56	-99	14
Net repayment of private sector debt	205	136	220	330
Repayment of government debt	70	80	71	69
Gross reserves accumulation (+ = increase) [1]	325	350	191	23
IMF repayments	15	12	10	4
Other (inc. unrepatriated export revenues)	353	327	540	474
Available financing	911	960	934	915
Foreign direct and portfolio investment	452	358	358	371
Budget support loans	17	77	52	0
Project support	398	398	479	458
Project grants	278	233	242	232
Project drawings	121	165	237	226
IMF: RCF disbursement and ECF arrangement	44	128	44	87
Budget support to be programmed	0	0	0	0
Memorandum items:				
Gross official reserves [1]	1,159	1,506	1,729	1,710

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1] The change in gross official reserves can deviate from the gross reserves accumulation because of exchange rate movements.

Table 10. Madagascar: Projected External Borrowing, 2019

Public and publicly-guaranteed external debt contracted	Volume of new debt		PV of new debt (program purposes)	
	USD million	Percent	USD million	Percent
By sources of debt financing	**575**	**100**	**309**	**100**
Concessional debt, of which	***565***	***98***	***302***	***98***
Multilateral debt	398	69	199	64
Bilateral debt	167	29	103	33
Other	0	0	0	0
Non-concessional debt, of which	***10***	***2***	***7***	***2***
Grant element between 0 and 35 percent	10	2	7	2
Commercial terms	0	0	0	0
By Creditor Type	**575**	**100**	**309**	**100**
Multilateral	408	71	207	67
Bilateral - Paris Club	11	2	6	2
Bilateral - Non-Paris Club	156	27	96	31
Other	0	0	0	0
Uses of debt financing	**575**	**100**	**309**	**100**
Infrastructure	476	83	252	82
Budget Financing	61	11	30	10
Social Spending	0	0	0	0
Other[1]	38	7	27	9

Sources: Malagasy authorities; and IMF staff estimates and projections.

[1]Includes Agriculture and Financial Sector Development.

Table 11. Madagascar: Proposed Schedule of Disbursements of ECF Arrangement

Availability Date	Disbursement (In percent of quota)	Disbursement (In SDRs)	Conditions for Disbursement
July 27, 2016	12.9	31,428,000	Board approval of the arrangement
June 28, 2017	25.4	61,978,000	Board completion of first review based on observance of performance criteria for end-
November 20, 2017	12.9	31,428,000	Board completion of second review based on observance of performance criteria for end-June 2017
May 20, 2018	12.9	31,428,000	Board completion of third review based on observance of performance criteria for end-December 2017
November 20, 2018	12.9	31,428,000	Board completion of fourth review based on observance of performance criteria for end-June 2018
May 20, 2019	12.9	31,428,000	Board completion of fifth review based on observance of performance criteria for end-December 2018
November 20, 2019	12.9	31,432,000	Board completion of sixth review based on observance of performance criteria for end-June 2019
Total	102.5	250,550,000	

Source: IMF.

Table 12. Madagascar: Quantitative Performance Criteria and Indicative Targets

	End-June 2019			
	Performance Criteria	Adjusted	Estimate	Status
Fiscal				
Floor on primary balance excl. foreign-financed investment and grants (commitment basis) [1]	-22		868	Met
External				
Ceiling on accumulation of new external payment arrears (US$ millions) [2]	0		0	Met
Ceiling on new external debt contracted or guaranteed by the central government or BFM, in present value terms (US$ millions) [4]	900		478	Met
Central bank				
Floor on net foreign assets (NFA) of BFM (millions of SDRs) [5]	833	812	816	Met
Ceilings on net domestic assets (NDA) of BFM [5]	1,521		1,134	Met
Indicative targets				
Floor on social priority spending [1]	198		17	Not met
Floor on gross tax revenue [1]	2,800		2,806	Met
Ceiling on new nonconcessional external debt with original maturity of more than one year, contracted or guaranteed by the central government or BFM (US$ millions) [3]				
Grant element of less than 35 percent	383		283	Met
Grant element of less than 20 percent	100		95	Met
Ceiling on new nonconcessional external debt with original maturity of up to and including one year, contracted or guaranteed by the central government or BFM (US$ millions) [2]	0		0	Met

Sources: Madagascar authorities; and IMF staff projections.

[1] Cumulative figures from the beginning of each calendar year.

[2] Cumulative ceilings that will be monitored on a continuous basis starting from end-May, 2016.

[3] Cumulative ceilings that will be monitored on a continuous basis starting from January 1, 2016.

[4] Cumulative ceilings that will be monitored on a continuous basis starting from January 1, 2018.

[5] The total stock of NFA and NDA measured at the program exchange rates.

Table 13. Madagascar: Structural Benchmarks

Action	Dates	Rationale	Status
<u>Mobilizing fiscal revenue</u>			
Adopt a strategy for the control of high-risk sectors, such as free trade zones and new special economic and industrial zones.	End-July 2019	Safeguard revenue	Met.
Employ the new Tax Identification Number (TIN) throughout all ministries.	End-Dec. 2018	Strengthen fiscal controls	Not met. Action completed in the major ministries.
<u>Improving the composition and quality of fiscal spending</u>			
Implement an automatic fuel price formula with a smoothing mechanism no later than end-September 2019, while avoiding budget costs from fuel pricing in the interim.	Continuous benchmark	Critical to contain transfers	Not met. Budget costs have been avoided so far, but the implementation of automatic pricing is still pending.
<u>Enhancing economic governance</u>			
The terms and conditions of all PPP contracts will be published within one month of the date of signature on the web site of the Ministry of Economy and Finance.	Continuous benchmark	Critical to enhance transparency and accountability	Met.
Notify World Bank and IMF staff in advance of any single source procurement contracts for JIRAMA's purchases of fuel and electricity and purchases and rentals of generators.	Continuous benchmark	Critical to enhance transparency and accountability	Not met. JIRAMA signed one single source contract for fuel supply without notifying Fund and World Bank staff.
Establish a public registry of companies that have violated the procurement regulations and are prohibited from participating in future bids.	End-Aug. 2019	Transparency and value for money	Met.
<u>Strengthening financial sector development</u>			
Submit to Parliament a law on financial stability, in line with international standards and FSAP recommendations, establishing the structure in charge of analyzing, identifying, and preventing systemic risks as well as managing and addressing financial crises.	End-June 2019	Financial stability	Not Met. Reviewed by the Council of Government.
Submit to Parliament a new banking law that will: (i) improve the bank recovery and resolution framework in line with FSSA recommendations; (ii) reinforce the framework for corrective bank supervisory measures (with the specific triggers, responsibilities, and time limits for an effective response to bank violations and vulnerabilities to be determined by the law or regulation); and (iii) enhance the powers and independence of the financial supervisor (CSBF), including legal protection for its staff and Board members.	End-Dec. 2018	Contain systemic financial risk	Not Met. Action achieved in December 2019, when the law has been submitted to Parliament after its adoption by the Council of Ministers on December 11, 2019.

Table 14. Madagascar: Indicators of Capacity to Repay the Fund, 2019-32

(As at December 5, 2019)

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
							(Millions of SDRs)							
Fund obligations based on existing credit														
Principal	3.1	6.1	12.2	18.5	37.2	43.6	49.9	43.8	37.5	18.9	9.4	0.0	0.0	0.0
Charges and interest	0.3	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Fund obligations based on existing and prospective credit														
Principal	3.1	6.1	12.2	18.5	37.2	43.6	53.1	50.1	43.8	25.1	15.7	3.1	0.0	0.0
Charges and interest	0.3	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Total obligations based on existing and prospective credit														
Millions of SDRs	3.3	7.1	13.2	19.5	38.1	44.5	54.0	51.1	44.8	26.1	16.6	4.1	0.9	0.9
Billions of Ariary	16.6	36.6	71.1	108.8	220.1	265.7	330.9	320.8	288.4	172.2	112.5	28.2	6.7	6.8
Percent of exports of goods and services	0.1	0.2	0.4	0.5	0.9	1.0	1.2	1.0	0.8	0.4	0.3	0.1	0.0	0.0
Percent of debt service	2.4	4.9	9.0	11.1	18.5	17.7	19.8	17.4	13.7	7.5	4.3	0.9	0.2	0.2
Percent of GDP	0.0	0.1	0.1	0.2	0.3	0.3	0.3	0.3	0.2	0.1	0.1	0.0	0.0	0.0
Percent of government revenue	0.3	0.6	0.9	1.2	2.2	2.3	2.5	2.2	1.7	0.9	0.5	0.1	0.0	0.0
Percent of quota	1.4	2.9	5.4	8.0	15.6	18.2	22.1	20.9	18.3	10.7	6.8	1.7	0.4	0.4
Outstanding IMF credit based on existing and prospective drawings														
Millions of SDRs	277.2	302.5	290.3	271.7	234.6	191.0	137.9	87.8	44.0	18.8	3.1	0.0	0.0	0.0
Billions of Ariary	1,389.1	1,569.4	1,569.3	1,519.4	1,353.8	1,140.2	844.9	551.8	283.4	124.4	21.2	0.0	0.0	0.0
Percent of exports of goods and services	9.1	9.3	8.0	7.0	5.8	4.4	3.0	1.8	0.8	0.3	0.1	0.0	0.0	0.0
Percent of debt service	203.2	210.0	198.1	154.9	113.9	75.8	50.5	30.0	13.5	5.4	0.8	0.0	0.0	0.0
Percent of GDP	2.7	2.7	2.4	2.1	1.7	1.3	0.8	0.5	0.2	0.1	0.0	0.0	0.0	0.0
Percent of government revenue	25.6	24.2	20.7	17.4	13.5	9.8	6.4	3.7	1.7	0.7	0.1	0.0	0.0	0.0
Percent of quota	113.4	123.8	118.8	111.2	96.0	78.1	56.4	35.9	18.0	7.7	1.3	0.0	0.0	0.0
Net use of IMF credit (millions of SDRs)	59.8	25.3	-12.2	-18.5	-37.2	-43.6	-53.1	-50.1	-43.8	-25.1	-15.7	-3.1	0.0	0.0
Disbursements	62.9	31.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	3.1	6.1	12.2	18.5	37.2	43.6	53.1	50.1	43.8	25.1	15.7	3.1	0.0	0.0
Memorandum items:							(Billions of Ariary, unless otherwise indicated)							
Exports of goods and services (millions of SDRs)	3,055	3,253	3,623	3,864	4,064	4,320	4,642	5,002	5,389	5,807	6,257	6,742	7,265	7,828
Debt service	683.6	747.2	792.0	980.8	1,188.6	1,504.8	1,672.3	1,841.7	2,100.1	2,290.3	2,622.4	3,011.6	3,425.8	3,912.2
Nominal GDP (at market prices)	51,229	57,786	64,860	72,335	80,552	89,657	99,675	110,699	122,814	136,113	150,697	166,670	184,145	203,241
Government revenue	5,427	6,493	7,563	8,713	10,038	11,616	13,240	14,915	16,759	18,795	21,055	23,510	26,223	29,216
Quota (millions of SDRs)	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4	244.4

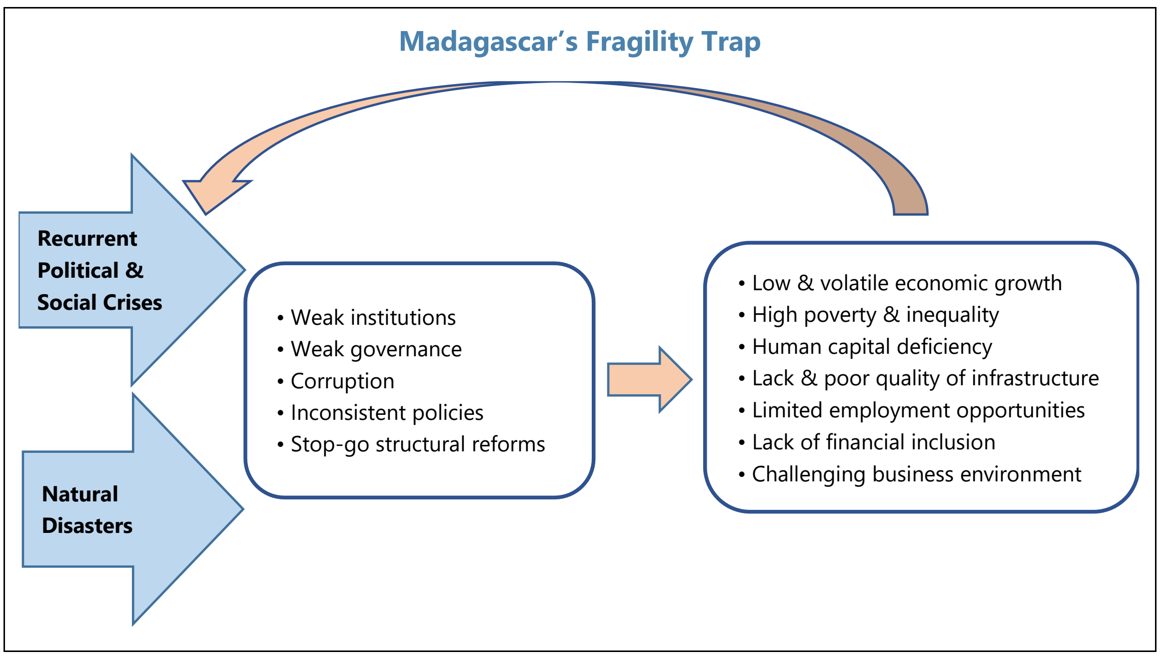
Source: IMF

Annex I. Country Engagement Strategy—Summary

A. Sources and Consequences of Fragility

1. Despite recent progress Madagascar appears to be stuck in a "fragility trap".[1] Over the long term, political instability, the poor quality of institutions and governance, and bad and inconsistent economic policies have impaired economic performance and the delivery of basic social services. As a result, challenges are numerous and difficult: widespread and persistent poverty, high income inequality, human capital indicators among the worst worldwide, lack and poor quality of basic infrastructures, lack of financial inclusion, systemic corruption, lack of sources of employment and income, and a challenging business environment.

2. Madagascar's many dimensions of fragility present challenges for sustaining inclusive growth and improving social indicators.[2] Like other fragile countries, Madagascar's dimensions of fragility are related to political, social, economic, infrastructure and governance deficiencies. These include:



[1] The 2018 Report on Escaping the Fragility Trap by the LSE-Oxford Commission on State Fragility, Growth and Development focuses on what makes countries suffer from fragility and how to escape their "fragility trap".

[2] Madagascar was classified as "fragile" in the World Bank's "Harmonized list of Fragile Situations" following the 2009-2012 crisis. As of FY2018, Madagascar is no longer part of this list primarily because of improvements in its Country Policy and Institutional Assessment score. Madagascar is listed as "high warning" based on the Peace 2019 Fragile States Index which ranks all countries, and "fragile" in the OECD's 2018 States of Fragility report. As discussed in Thier (2019), whether one country is fragile or not it is not a binary question: it is a multidimensional condition that "exists in gradations and with significant variation". Madagascar remains a fragile country with high vulnerability to significant domestic and exogenous shocks.

- **Widespread and persistent poverty**. In 2018, Madagascar was ranked among the poorest countries in the world with approximately 75 percent of the population living on less than US$1.90 a day at purchasing power parity—a marginal improvement over 78 percent recorded in 2012 at the end of the last social and economic crisis.

- **Large disparities between urban and rural areas.** Close to 80 percent of the population live in rural areas, where absolute poverty is almost twice as high compared to urban areas; as a result, almost 9 out of 10 poor people live in rural areas. Other development indicators are also less favorable in rural areas: infant mortality is higher, life expectancy is shorter, literacy is lower, malnutrition is more widespread, school attendance is lower, and only a very small minority of the rural population has access to electricity and safe drinking water.

- **Poor human capital indicators.** Madagascar ranks 139th among 157 countries in the World Bank's 2018 Human Capital Index—one of the lowest worldwide—a decline from 2012. These indicators paint a worrisome picture: the worst scores in the index include stunting, malnutrition and learning outcomes. About one in two children under five suffer from stunting; chronic malnutrition rates are the fourth highest in the world; and Madagascar has the fifth highest number of children dropping out of primary school in 2012 in the world. Not only is human capital declining but total expenditures on education and health are among the lowest in the world. The outbreak of epidemics such as measles (in 2019) and the plague (in 2018) underscore weaknesses in the overall health system.

- **An infrastructure deficit that constrains private sector investment and growth.** Supporting infrastructures including access to electricity and transport, as well as port infrastructure are often costly and/or inadequate. This often reflects low levels of domestic financing for public investments (due to lack of fiscal space), or the start-and-stop nature of scaling-up financed by development partners interrupted by political turbulence.

- **Low financial inclusion.** While improving in recent years, notably through mobile money operations that have expanded rapidly since their inception in 2010, financial inclusion remains low compared to peers.

- **Slow progress in implementing governance and anti-corruption frameworks.** In recent years, there has been progress in strengthening the anticorruption legal framework (Figure 1, panel 5), with several laws adopted since 2016 helping to bring Madagascar's legal framework towards international standards. Institutions necessary for effective enforcement of this new legal framework are not established, and progress to strengthen public financial management and enhance good governance, transparency, and sound public finances is slow.

- **Challenging business environment.** The country ranked 161st among 190 countries in the World Bank's 2019 Doing Business, behind most comparator countries and below the SSA average in all but one categories of the Doing Business index (Figure 1, panel 6).

3. This fragility has created immense challenges, summed up by poor performance towards making progress in achieving of the SDGs. Madagascar faces significant challenges in reaching the SDGs. Latest reports from the 2019 Africa SDG Index suggest that Madagascar ranks

44 out of 52 countries in Africa and has a global rank of 158 out of 162 countries according to the 2019 SDG Report. Madagascar faces major or significant challenges in 15 out of the 17 goals in the 2019 SDG report, which include goals relating to poverty, access to electricity, access to clean water and sanitation, education, and health and well-being.

4. Substantial resources will be needed to mitigate these fragilities and make significant progress in achieving meaningful SDGs outcomes. Recent costing exercises estimate additional expenditure needs of around 20 percent of GDP by 2030 for Benin and Rwanda—Madagascar's needs are expected to be substantially higher since Madagascar has made less progress towards achieving the SDGs than these two countries. Financing this effort will be very challenging and will likely require increases in domestic public resources, private investment, and official development assistance (ODA). On the latter, and despite progress since Madagascar's reengagement with the international community in 2014, net ODA received by Madagascar remains low: about US$530 million per year on average between 2010 and 2017, which represents only about 1 percent of total ODA received by African countries over this period.

B. Future Fund Engagement

5. The Fund reengaged with Madagascar in 2014. After two disbursements under the Rapid Credit Facility (RCF) and satisfactory implementation of a six-month Staff-Monitored Program, the Executive Board approved a 40-month ECF arrangement on July 27, 2016. In response to further BOP needs caused by the March-2017 cyclone (the most severe in 13 years), additional access of 12.5 percent of quota was approved by the Executive Board on June 28, 2017, bringing Madagascar's access to SDR250.55 million at that time. The disbursement associated with this augmentation was on-lent to the Treasury as indirect budget support for additional spending related to reconstruction efforts. Part of the first ECF-disbursement in July 2016 was also indirect budget support through on-lending to the Treasury.

Based on the experience from the ECF, some lessons for future engagement:

- A **close engagement**, through the Resident Representative office and frequent country team missions, is important to ensure the pursuit of policies and reforms; help the authorities focus on program implementation; and contribute to enhancing inter-ministerial coordination.

- **Realism** about what can be achieved and the time it takes to implement specific reforms. The slowing pace of reforms towards the end of the current ECF—although primarily due to the electoral calendar—underscores the importance of focusing on well-targeted reforms at the beginning of the program and identifying "quick-wins" to maintain the momentum for reforms and ensure support by the population.

- Need to **build buffers into the design of a potential successor program** and respond flexibly to new developments given Madagascar's exposure to external and internal shocks. Such flexibility (including on allowing more time for the implementation of a fuel pricing mechanism) was key for completing the 2016-19 ECF reviews.

- Given the government's ambitious objectives in terms of increasing domestic revenue and improving spending composition towards investments and social spending, it will be important to **maintain a strong focus on fiscal management** and to support fiscal reforms with targeted TA to achieve results (including by closely monitoring the actual implementation of past reforms).

- Beyond recent reforms to strengthen **the anti-corruption legal framework**, a strong focus on fair and effective implementation of this framework, and more broadly improving the **business climate** would yield a significant dividend.

6. **Fund engagement can continue to help address fragilities that hamper sustainable and inclusive growth and improvements in development outcomes in Madagascar.** The authorities indicated their willingness to start discussions on a potential successor arrangement after the completion of the 6th and last review of the current ECF-arrangement. Fund engagement will also take the form of continued CD and policy advice.

7. **The Fund could continue to support the authorities' policy priorities by** (i) helping with continuity, building on the good track record of the current ECF and support the strengthening and the acceleration of reforms; (ii) serving as a catalyst to help unlock other financing, as the program can serve as a signal that the country has adopted sound policies, reinforcing policy credibility, and increasing investors' and donors' confidence (including for budget support); and (iii) supporting the implementation of the authorities' PEM development plan and its efforts to raise growth, reducing poverty, and making progress in attaining the SDGs in a credible medium-term macroeconomic framework.

8. **The Fund could help the authorities to maintain macroeconomic stability and achieve sustained and inclusive growth, by:**

- **Creating additional fiscal space, by:**
  - ✓ *Further improving revenue mobilization,* helping to define ambitious but credible objectives for tax revenue mobilization, building on Fund experience in similar countries, tailored advice, and associated TA to improve both tax administration and tax policies.
  - ✓ *Containing lower-priority spending.* This includes the transfers to JIRAMA, consistent with the medium-term operational and financial recovery plan under finalization.
  - ✓ *Identifying and quantifying fiscal risks and proposing solutions to mitigate them.* This includes solutions to avoid direct budget impact of the government liability to fuel distributors, maintain the deficit of the civil servant fund at a sustainable level, and manage potential risks with the planned development of PPPs.
  - ✓ *Catalyzing additional budget support.*

- **Ensuring that this fiscal space is used for higher priority spending in social sectors and infrastructure, by:**
  - ✓ *Helping the authorities embrace all macro-criticality dimensions of social spending* (fiscal sustainability, spending efficiency and spending adequacy).

- ✓ *Improving the planning and monitoring of priority spending*, through quantitative targets and structural benchmarks.
- ✓ *Providing additional TA on public investment management.*

- **Further improving governance and the fight against corruption, and strengthening the business climate,** by encouraging the implementation of the anticorruption legal framework now in place and supporting reforms to alleviate impediments to private sector development (including costly regulatory requirements, a weak legal and judicial business law environment).

- **Continuing improvements in the effectiveness of the monetary policy framework** and supporting the ambitious central bank reform agenda.

- **Further strengthening financial sector resilience and promoting financial inclusion.**

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Annex II. Risk Assessment Matrix

Risks	Relative Likelihood	Potential Impact	Policy Response
Domestic Risks			
Weak investment implementation capacity.	**High**	**Medium**: Slower economic growth.	Monitor available domestic capacity and prioritize investments with highest returns.
Larger than anticipated transfers to SOEs (e.g., JIRAMA).	**Medium**	**Medium**: Transfers to SOEs reduce other priority expenditures. Potential economic disruption if SOEs' operations are affected.	Identify options to protect key public services. Encourage authorities and development partners to protect social priority spending. Strengthen governance structures, including government oversight of key SOEs. Consider private management of specific units or operations.
Stall in governance reforms, especially for SOEs.	**High**	**High:** A lack of transparency and even-handedness may compromise additional concessional support, hinder private investment (incl. PPPs), and harm negotiations with fuel suppliers.	Undertake promised reforms and renew commitment to operating SOEs (e.g., JIRAMA) in a transparent and equitable manner.
Failure to tackle corruption.	**High**	**Medium:** Reduced inflow of FDI and donor support.	Step-up anti-corruption and AML/CFT efforts.
External Risks			
Weaker-than-expected global growth.	**Medium** (U.S.); **High** (Europe, China)	**Medium**: Slower growth in tourism (especially Europe) and lower commodity prices (especially due to lower Chinese demand) weaken the balance of payments.	Maintain exchange rate flexibility as a shock absorber. Diversify sources of tourism.
Rising protectionism and retreat from multilateralism.	**High**	**Medium**: Reduced inflows from FDI and donor support. Lower access to foreign markets.	Maintain exchange rate flexibility and reallocate fiscal spending from investment to key public services and support of the most vulnerable. Energize donor support by emphasizing the merits of the medium-term development plan.
Large swings in energy prices.	**Medium**	**Medium**: Higher energy prices weaken the balance of payments, raise inflation, and make ongoing energy reforms more difficult.	Continue reform of JIRAMA and implement agreement with fuel distributors on an automatic fuel pricing formula going forward, while using social transfers and fuel type differentiation to protect the most vulnerable.
Higher frequency and severity of natural disasters.	**Medium**	**Medium**: Loss of real and human capital and lower growth.	Reallocate fiscal spending to finance recovery work and appeal to donors for post-disaster financing.

Annex III. Status of Key Recommendations of the 2017 Article IV/Program Objectives

1. Key recommendations of the 2017 Article IV consultation were aligned with the objectives supported by the ECF, most of which have been achieved or have shown significant progress:

- The macroeconomic objectives have shown significant progress. Real GDP growth gradually improved, reaching 4.6 percent in 2018, with contained inflation, fairly good fiscal performance (with tax revenue mobilization in line with initial targets), and a solid external position.
- Progress was also achieved in the reform agenda, notably in the financial sector, and in the reinforcement of the anti-corruption legal framework. Other reforms aimed at promoting inclusive growth, through the shifting of public spending in favor of priority spending have also showed progress, but with results sometimes more modest or slower than expected; capital and social spending increased but remain short of initial objectives, and the transfers to compensate the loses of JIRAMA or the civil pension fund also declined less quickly than expected.

2. Going forward and to maintain macroeconomic stability and achieve sustained and inclusive growth, the Fund can support the authorities in:

- Creating additional fiscal space, by:
  - ✓ Further improving revenue mobilization, helping to define objectives for tax revenue mobilization, building on Fund experience in similar countries, tailored advice, and associated TA to improve both tax administration and tax policies.
  - ✓ Containing lower-priority spending. This includes the transfers to JIRAMA, consistent with the medium-term operational and financial recovery plan under finalization.
  - ✓ Identifying and quantifying fiscal risks and proposing solutions to mitigate them. This includes solutions to avoid direct budget impact of the government liability to fuel distributors, maintain the deficit of the civil servant fund at a sustainable level, and manage potential risks with the planned development of PPPs.
  - ✓ Catalyzing additional budget support.
- Ensuring that this fiscal space is used for higher priority spending (social and infrastructure), by:
  - ✓ Helping the authorities embrace all macro-criticality dimensions of social spending (fiscal sustainability, spending efficiency and spending adequacy).
  - ✓ Improving the planning and monitoring of priority spending, through quantitative targets and structural benchmarks.
  - ✓ Providing additional TA on pubic investment management.
- Further improving governance and the fight against corruption, and strengthening the business climate, by encouraging the implementation of the anticorruption legal framework now in place and supporting reforms to alleviate impediments to private sector development (including costly regulatory requirements, a weak legal and judicial business law environment).
- Continuing improvements in the effectiveness of the monetary policy framework and further strengthening financial sector resilience and promoting financial inclusion.

Macroeconomic Objectives for Stronger Stability and Sustainability	**Assessment**	
Accelerate economic growth to 5 percent a year	🟡	Real GDP gradually improved, reached a 10 year-highest with 4.6 percent in 2018 and is projected at 4.8 percent in 2019.
Maintain inflation in single digits with a downward trend toward 5-6 percent	🟡	Inflation is contained to single digits, but the downward trend is still uneven, even if inflation is projected at 6 percent at end-2019.
Improve international reserves coverage gradually to at least 3½ months of imports	🟢	Helped by the positive vanilla shock and appropriate FX management by the central bank, this objective is more than achieved, with a coverage projected to 4.3 months of imports at end 2019.
Raise net tax revenue gradually to 12 percent of GDP (equivalent to 10.6 percent of new GDP)[1]	🟡	The objective is almost achieved, with tax revenue anticipated at about 10.4 percent of GDP in 2019.
Boost public capital expenditure substantially to 8 percent of GDP (equivalent to 7 percent of new GDP)[1]	🟡	Capital spending gradually increased from 3 to a projected 5 percent of GDP between 2015 and 2019 but will remains short of initial objective due to implementation capacities.
Achieve a modest surplus in the domestic primary balance (excluding foreign-financed investment)	🟢	The domestic primary balance is expected to be slightly positive in 2019, like in 2018.

[1]These two objectives were set before the national accounts rebasing.

Structural Reform Objectives for Sustainable and Inclusive Growth	**Assessment**	
Promote inclusive growth, inter alia by shifting public spending significantly in favor of infrastructure investment, education, and health and improving the business climate.	🟡	Public investment scaling up has favored infrastructure. Spending in education and health has also increased, even if delays and shortfall in externally financed investments also impacted social sectors.
Create fiscal space, inter alia by mobilizing domestic revenue and sharply reducing the need for transfers to SOEs and pension fund.	🟡	Revenue mobilization was in line with initial targets. Transfers to SOEs are downward, but more slowly than anticipated. The pension fund deficit remains significant at 0.6 percent of GDP, and further reforms are needed.
Enhance economic governance and fight corruption, by limiting the use of restricted tenders in procurement, devoting more resources to anti-corruption agencies and reinforcing the legal framework.	🟢	Key laws relevant to the fight against corruption have been enacted, including a new AML/CFT law in December 2018, and the law on illicit asset recovery. An anti-corruption court has been opened.
Strengthen stability and financial sector development, inter alia through enhanced central bank independence, reinforced financial sector supervision, and better liquidity management.	🟢	The adoption of the Central Bank Act in 2016 was followed by an impressive reform agenda. Further progress is expected with the new banking law, and a law on financial stability still pending parliament vote.

🟢 Objective achieved

🟡 Objective partially achieved

Annex IV. External Sector Assessment

Staff assesses the 2019 external position of Madagascar is moderately stronger than estimates implied by fundamentals and desirable policy settings. Within the near to medium-term, the external position is expected to converge towards its norm as vanilla prices continue to normalize and capital infrastructure spending increases, and, with it, import demand. The reserve adequacy assessment for credit-constrained economies suggests that 2019 international reserves are adequate; however, in the absence of an IMF program, 2019 reserves would fall below the lower bound.

A. Current Account and the REER Approach

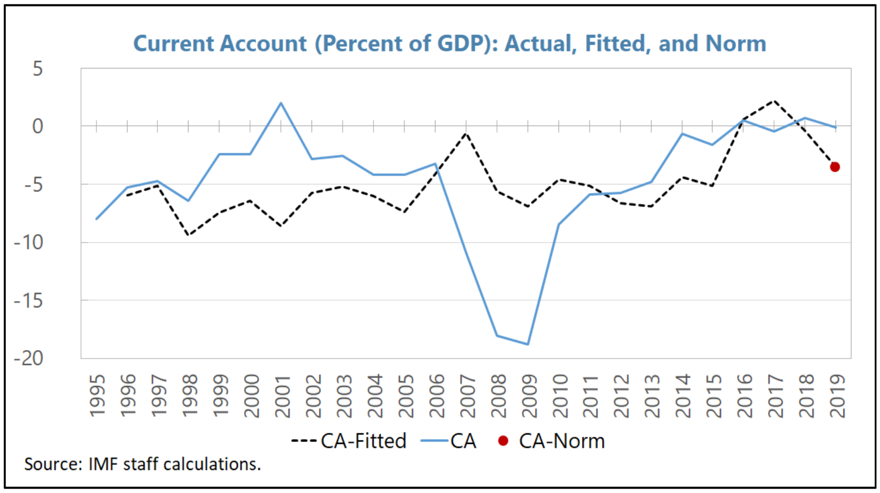
EBA-Lite Methods

1. The EBA-lite methodology uses estimates of current account gap and real effective exchange rate norms and gaps. Norms are the estimated levels of the current account based on underlying fundamentals, while gaps are the deviations of observed values from the norms. To predict the equilibrium of the current account consistent with structural and policy factors, EBA-Lite uses regression analysis for a large sample of countries

2. The 2019 current account is projected to be a deficit of -0.1 percent of GDP. In 2019, the current account balance fell to -0.1 percent of GDP, down from a surplus of 0.7 percent of GDP in 2018. Amongst goods exports, the price of vanilla fell from its peak by almost 10 percent, cobalt prices dropped by half, and clove export volumes fell by nearly two-thirds due to cyclical production factors. Net service exports reached a surplus of 1 percent of GDP in 2019 due to stronger-than-expected tourism arrivals, up from -0.1 percent of GDP at end 2018, while goods imports were also lower-than-anticipated due to under-execution in public investment.

3. The decline in key commodity prices reflects a normalization of Madagascar's terms-of-trade and is adjusted for in the context of the model. At projected vanilla prices (set at an average over the 2020-2025 period, which assumes a gradual decline), exports would be lower by the equivalent of 1.1 percent of GDP in 2019, which together with a -.1 percent adjustment for cobalt prices (using the same approach) and the model-implied cyclical adjustments, suggests an adjusted current account deficit of 1.9 percent of GDP.

4. The adjusted current account in 2019 is 1.7 percent of GDP higher than the cyclically adjusted norm, suggesting it is moderately stronger than estimates implied by fundamentals and desirable policies. Table 1 summarizes the adjusted current account (-1.9 percent of GDP) and the EBA-lite current account model estimates for Madagascar. The current account norm is -3.6 percent of GDP, of which 0.14 percent of GDP is driven by policy gaps (deviations from desirable policies). The high deficit for the current account norm reflects the long-term development needs of the country. Relative to the 2017 assessment, which found the external position to be stronger than estimates implied by fundamentals, vanilla and metals prices have fallen from their recent peaks and imports are starting to scale up behind needed capital investments, despite still being lower than anticipated.



5. The current account approach suggests a REER undervaluation of 6.1 percent. Using an elasticity of -0.27 estimated on historical data, in combination with a current account gap of 1.7 percent of GDP suggests a REER undervaluation of -6.1 percent, which is moderately stronger than fundamentals and desirable policy settings.

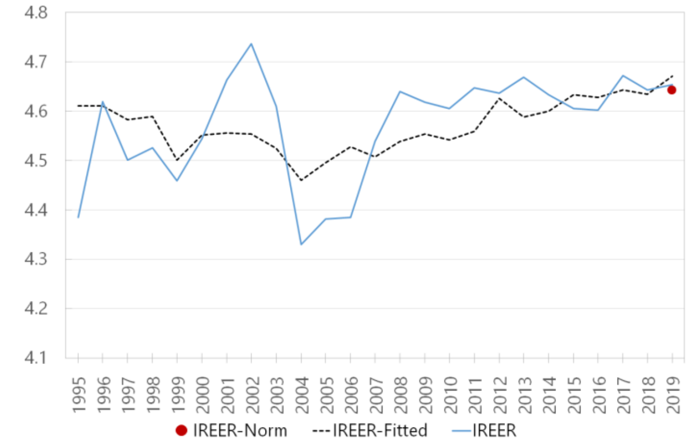
Table 1. IMF Assessed Current Account and REER Gaps

(percent of GDP, unless otherwise indicated)

Actual current account (A)	-0.1
Temporary factors (model implied + commodity price effects) (B)	1.8
Adjusted current account (C=A-B)	-1.9
Fitted current account (D)	-3.5
Policy gap (E)	0.14
Natural Disasters & Conflicts	-0.2
Current account norm (F=D-E - Natural Disasters)	-3.4
Multilaterally Consistent Cyclically adjusted CA Norm (G=F-model implied cyclical factors)	-3.6
Current account gap (H=C-G)	**1.7**
Elasticity	-0.27
REER gap (percent)	**-6.1**

6. The REER approach suggests that Madagascar's REER is broadly consistent with fundamentals. The REER model is a reduced form model that estimates a fitted value for the real effective exchange rate in terms of a set of economic variables that cause persistent deviations from long-run purchasing power parity, such as terms of trade, productivity, aid, and remittances. There is an estimated slight overvaluation of 1.2 percent—reflecting a policy gap of 3 percent due largely to capital controls, some of which the authorities are currently addressing. Based on this approach, the REER is broadly consistent with fundamentals.

IREER: Actual, Fitted, and Norm



Source: IMF staff calculations.

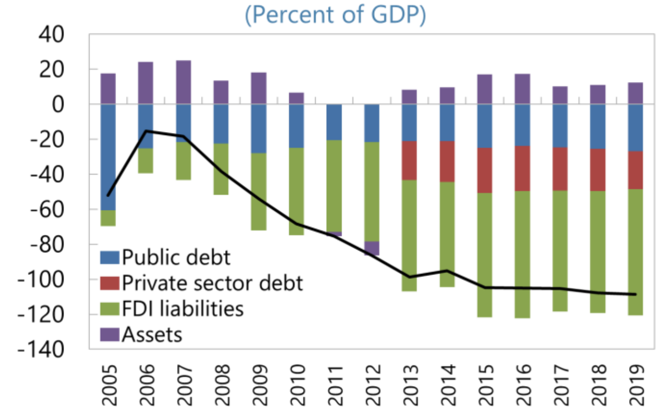
Table 2. Madagascar: EBA-lite Exchange Rate Assessment
(percent)

	Norm	Underlying	Implied REER deviation
CA Approach (CAB/GDP)	-3.6	-1.9	-6.1
IREER (log REER)	4.64	4.65	1.2

7. The current account balance is projected to adjust to its norm as the terms-of-trade returns to historical levels and as public investment scales up as we approach the medium term. The vanilla price boom is expected to continue gradually subsiding, with 2019 prices already falling 10 percent relative to their peak. In addition, Madagascar's investment needs will remain significant given its current level of development. As capital investments scale up, imports are expected to rise as a percent of GDP between 2019-2021.

8. The net international investment position (NIIP) remains negative but does not represent a critical vulnerability. From 2006 to 2019, the NIIP decreased from -15 to -108 percent of GDP, mainly linked to private-sector liabilities in the mining sector. Since 2015, the NIIP has been broadly stable. Based on ongoing and discussed plans for scaling and upgrading production, the risk related to these liabilities is contained.

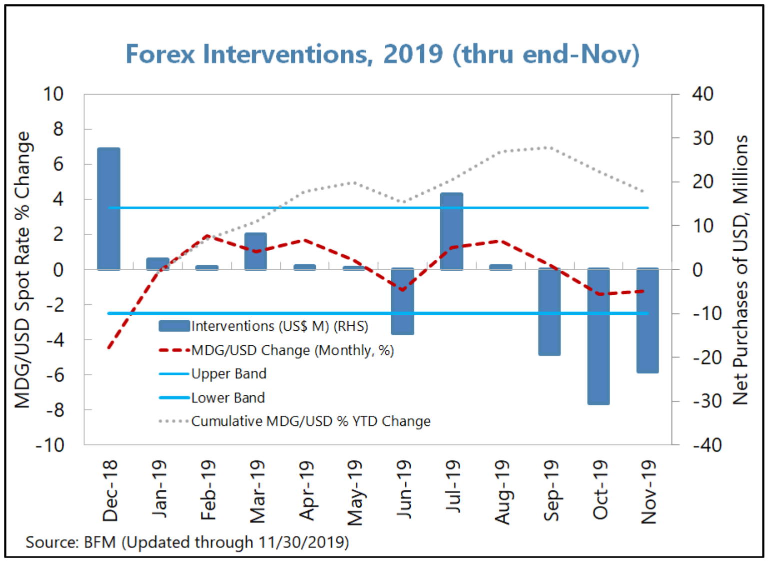
Net International Investment Position (NIIP)
(Percent of GDP)



Sources: Malagasy authorities and IMF staff calculations

B. Exchange Rate Regime

9. Madagascar has a floating exchange rate regime and intervenes to smooth volatility and build reserves. The central bank (BFM) follows an algorithm, developed with technical assistance from the Fund, for intervening in the interbank market to smooth exchange rate fluctuations and meet foreign reserve targets.[1] In 2019, a gradual depreciation in the first half of the year was accompanied by persistent, but moderate reserve accumulation. By May 2019, cumulative depreciation had reached 5.3 percent (greater than the +3.5 percent intervention rule upper bound) and the authorities intervened, executing net sales of $14.6 million USD in June 2019. According to the algorithm, they could have intervened as early as end-April. The authorities intervened between September and November with $73.2 million USD in net sales after another breach of the upper band, leading to a subsequent appreciation in the nominal exchange rate of 2 percent.



10. Efforts are ongoing to improve foreign exchange market operations and gradually phase out a surrender requirement. A draft law on the foreign exchange market, prepared in consultation with IMF TA, is being revised following recent feedback from stakeholders and will be finalized in 2020. The authorities have also prepared a plan to gradually phase out the existing surrender requirement on export proceeds, considered a capital flow management measure (CFM) under the IMF's Institutional View on the Liberalization and Management of Capital Flows (the IV), based on market developments. Finally, staff discussed a provision in a regulation that requires MEF approval for free zone enterprises to purchase foreign exchange for their operations. Such a provision typically has jurisdictional implications as approval could be denied for bona fide current international transactions. Staff recommended that this provision be amended or clarified. The authorities addressed this by issuing a circular on December 20th, 2019.[2]

[1] The maximum allowance of either a weakening or strengthening in the spot rate is 5 percent, with intermediate margins that allow for a relatively larger depreciation of the exchange rate before triggering an intervention. When the exchange rate is within its designated fluctuation bands, the BFM accumulates reserves.

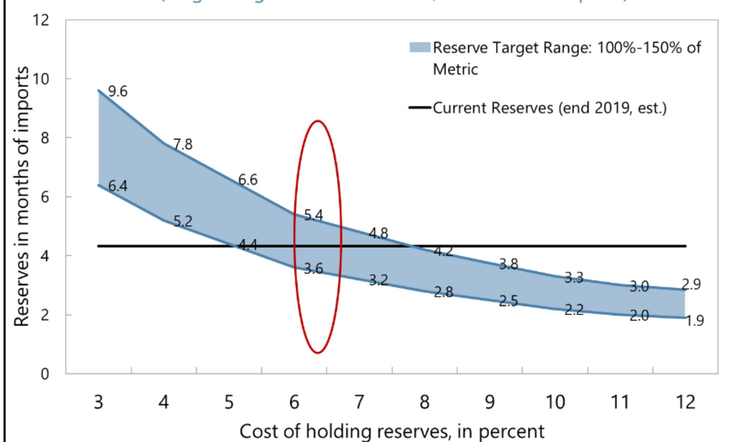
[2] In consultation with the legal department, staff had recommended that the provision be addressed in one of three ways: amendment of the decree to remove the authorization requirement; amendment of the decree to require free zone enterprises to exhaust their own foreign exchange resources before purchasing foreign exchange; or issuing a circular stating that all bona fide requests for foreign exchange (related to current international transactions) by free zone enterprises will be approved.

C. Reserve Adequacy

11. International reserves are broadly adequate. Reserves coverage stands at 4.3 months of current imports at the end of 2019 based on preliminary estimates, almost 1 percent higher than end-2018. The projected level of reserves exceeds the traditional three-month rule, as well as the lower bound from an ARA model for credit-constrained economies that compares the marginal costs of holding reserves against marginal benefits. The ARA model approach allows for consideration of the costs associated with terms of trade shocks, natural disasters, as well as the benefits associated with having a flexible exchange rate and an IMF program. The figure shows the range of optimal reserves. Preliminary estimates of 2019 reserves at 4.3 months coverage are centered within the band of adequacy for the average cost of 6.2 percent, where the upper bound is 5.4 and the lower bound is 3.6.[3] As imports rise in line with the projected increase in capital investment, import coverage of reserves is likely to fall in within the medium term. Finally, Madagascar remains vulnerable to external shocks, particularly to terms-of-trade fluctuations. Reserve accumulation is projected to continue at a gradual pace over the medium-term.

MDG Optimal Reserves

(Target range and current levels, in months of imports)



Source: IMF staff calculations.

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[3] The average cost estimate of 6.2 percent is based on empirical analysis estimating the cost of reserves using marginal productivity of capital (i.e., the opportunity cost to the economy of devoting investible resources into holdings of liquid foreign financial assets.

Annex V. Capacity Development Strategy (November 2019)

1. Madagascar has been an intensive user of IMF technical assistance (TA) and training since the normalization of its relations with the Fund in 2014, notably in the context of the ECF-arrangement launched in July 2016. Priorities closely aligned with the objectives of the program included reforms at the central bank (BFM), tax policy and administration, Public Financial Management (PFM), financial sector, and the anti-corruption legal framework. Fund TA evolved with the progress in the reform agenda, from general assessment early in the program towards more specific recommendations. Fund TA departments and the country team have maintained close interaction with the Malagasy authorities and leveraged the proximity of AFRITAC South (AFS) to ensure that TA needs and activities are always aligned, and capacity development (CD) is more relevant, effective and efficient.

A. Assessment of Recent Fund Technical Assistance

2. FAD reengagement with Madagascar on tax and custom administrations and PFM in 2015 has been followed by specific TA missions to improve government resources management. Since then, headquarters (HQ) support and AFRITAC South capacity development (CD) have been intense with a positive impact. Recommendations in tax and customs administration have been effective and helped reverse the decline in revenue collections. PFM reforms have also advanced with progress on medium term budgeting, public investment management and fiscal risk management. The implementation of a Strategic Plan of Modernization of PFM is underway and has contributed to improved transparency and more robust institutions for public investment

3. LEG assistance in the drafting of anti-corruption legislation has contributed to the significant progress in strengthening the anti-corruption framework, with several important laws adopted since 2016 (anti-corruption law; law on anti-corruption courts; law on international cooperation, AML/CFT law, and law on illicit asset recovery), bringing Madagascar closer to international standards.

4. Based on the 2015 FSAP recommendations, MCM and AFRITAC South assistance has been instrumental for reforms to: (i) strengthen BFM's independence; (ii) modernize the monetary policy operational framework, including by improving liquidity management and forecasting; (iii) develop foreign exchange markets; (iv) strengthen banking supervision; and (v) improve central bank internal audit functions and bring them to international standards.

5. MCM and LEG helped BFM on safeguards and transition to IFRS. BFM has continued to implement the recommendations of the July 2018 safeguards monitoring report, and work is progressing on the transition to IFRS in line with commitment to fully adopt the standards for the 2020 accounts.

6. STA (including AFRITAC South) has provided intensive TA, instrumental for National Accounts rebasing, reweighted CPI, external statistics with a broadened scope to include the dissemination of International Investment Position, monetary and financial statistics (MFS) and financial soundness indicators (FSIs), and government finance statistics to expand data coverage beyond budgetary central government. The authorities have also strengthened their participation in the enhanced General Data Dissemination System (e-GDDS), with a web-based National Summary Data Page launched in May 2019.

B. Key Overall CD Priorities Going Forward

7. Going forward, IMF TA support will continue to focus on deepening reforms that have yielded results in recent years and strengthening skills in the ministry of finance, the BFM, and the statistical agency; and expand to address new high-priority policy objectives. Key priorities include: (i) continuing the modernization of the customs and tax revenue administrations to improve compliance and reduce tax evasion; (ii) designing and implementing tax policies to converge towards a level of taxation more consistent with the country's tax potential; (iii) strengthening PFM through tougher internal controls, better control of fiscal risks (pensions, PPPs, and SOEs), improved management of public investment and the wage bill, and enhanced forecasting and budgeting; (iv) continuing the ongoing multiyear-reform plan to improve monetary policy, with the objective of gradually transition from monetary aggregate controlling to policies based on market interest rates; (v) further strengthening financial sector stability and development through better supervision and a resolution framework; and (vi) improving governance by effectively enforcing the legal framework.

Key Overall CD Priorities for the Next Three Years

Priorities	**Objectives**
Domestic tax and customs administration	Increase tax and custom revenue through further reforming and modernizing tax administrations, including effective control and enforcement, and business facilitation for compliant taxpayers.
Tax revenue policy	Help the dedicated Tax Policy Unit to make tax policy recommendations, including through limiting exemptions, based on recent evaluation of tax exemptions annexed to the budget law.
Monetary Policy Implementation & Operations	Help BFM to progressively migrate from the current framework (strict monetary targeting) to an interest rate targeting based framework.
PFM: Budget Execution and Control	Strengthen public investment management; streamline salary expenditure by improving payroll management and control; continue to improve the macro-fiscal and budget framework and fiscal risks management.

C. Authorities' Views

8. The authorities welcome the TA received from the Fund in recent years and find that priorities have been closely aligned with the program objectives, including in the areas of public financial management, revenue mobilization, and financial sector development (following the Financial Sector Assessment Program in 2015-16).

9. The authorities appreciate the opportunity to discuss their capacity development needs and priorities in meetings with FAD, MCM, LEG held during the Annual and Spring Meetings, as well as with the country team. They understand that resource constraints may limit the availability and staffing of IMF TA, which underscores the importance of prioritizing needs, defining clear terms of reference for the proposed missions, and identifying complementarities with missions from other TA providers.

10. The authorities welcome the collaboration between IMF HQ technical departments and AFRITAC South and find missions well-sequenced and complementary. They suggest that the frequency between TA missions could be adapted to ensure that the advice can be internalized and absorbed and suggest that sufficient time is allowed between the investigation/analysis mission and the review mission to allow the proper implementation of the recommendations provided. The authorities also appreciate the training opportunities given to officials of the Ministry of Economy and Finance and of the central bank.

11. Overall, the authorities find that the Capacity Development strategy is appropriate for Madagascar. They emphasize that TA provision has been instrumental for the success of the reform program and request that this effort is sustained in the coming years to continue progress on ongoing reforms and address new needs and challenges arising from the implementation of the new economic reform agenda under the Plan Emergence Madagascar. The authorities also reiterate their interest in long-term experts in specific areas, notably in revenue administration and tax policy, and medium-term budget framework.

Annex VI. Progress in Meeting the Sustainable Development Goals

Madagascar faces significant challenges in reaching the Sustainable Development Goals (SDGs). Latest reports suggest that based on progress on all 17 goals, Madagascar ranks 44 out of 52 countries in Africa (2019 Africa SDG Index) and has a global rank of 158 out of 162 countries (2019 SDG Report). Given this, substantial resources would be needed to make significant progress in achieving meaningful outcomes on the SDGs by 2030, which presents a significant challenge.

A. Background

1. Like most sub-Saharan African countries, Madagascar faces several challenges in meeting the SDGs. At the commencement of the SDG campaign, Madagascar started with a history of poor development outcomes, a large informal economy, frequent changes of government, and an overall GDP per capita that is lower than it was several decades ago. Progress in meeting the SDGs has been very slow; the 2019 SDG report assigns Madagascar an overall score of 46.7 out of 100 (ranking 158 of 162 countries).[1]

2. Madagascar faces significant challenges in 15 out of the 17 SDG goals. A comparison of Madagascar's latest SDG scores in the 2019 SDG report with Low Income Countries in Sub-Saharan Africa (SSA LICs) demonstrates the significant challenges. Most visible are challenges relating to (i) SDG1-No Poverty with a score of zero reflecting the fact that Madagascar has one of the highest poverty rates world-wide with 92 percent of the population estimated to live on less than $3.2 a day, and 55 percent of the population in extreme poverty; (ii) SDG7 where access to electricity is particularly low (three out of four households have no access to electricity—one of the lowest rates in the world); (iii) SDG6 since only half of the population has access to clean water, and less than 10 percent benefit from access to sanitation; (iv) SDG4 access to quality education with various indicators that measure the quality of the education system signaling weaknesses; and (v) SDG3 good health and well-being. Only one goal, SDG 12-Responsible Consumption and Production is on track to be achieved, and another goal, SDG13-Climate Action, faces less challenges partly because of Madagascar's economic underdevelopment and low greenhouse emissions (due to low industrial production).

B. Progress in Achieving the SDGs

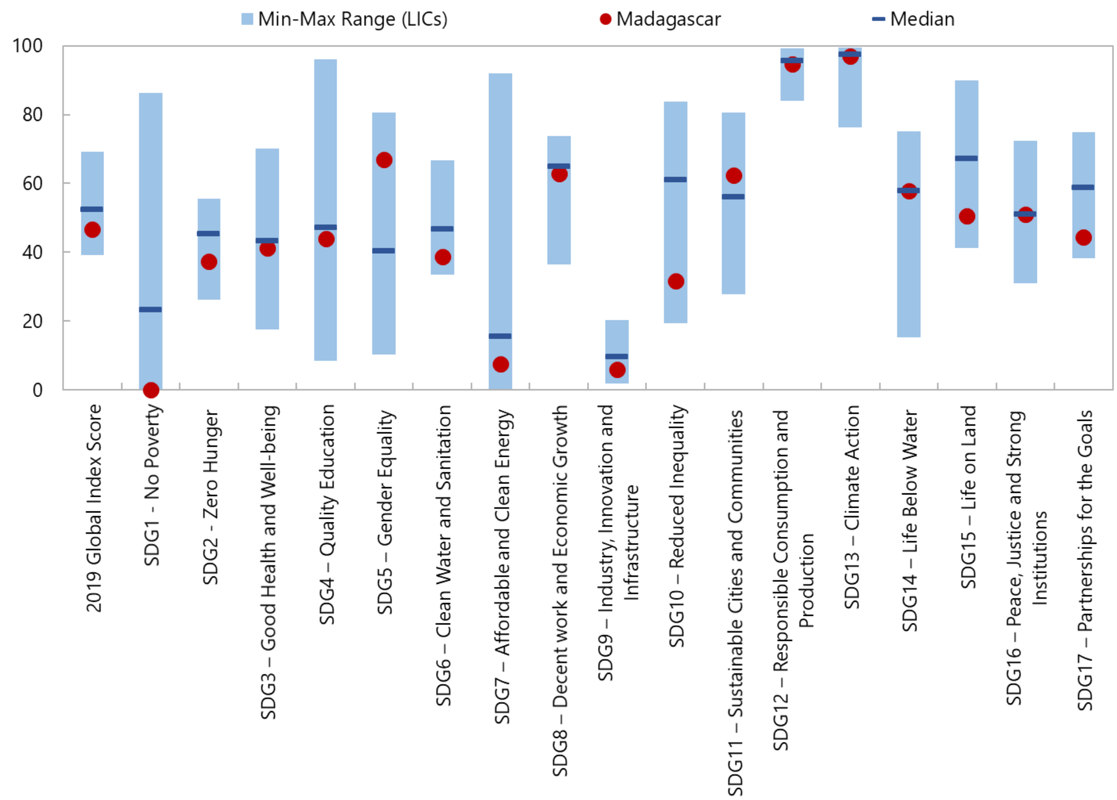
3. The authorities' PEM priorities are aligned with making substantial progress in attaining the SDGs. In the context of a broader and durable development strategy, the PEM makes explicit references to aligning the development strategy's priorities with the international engagements to attain the SDG goals by 2030. Key strategies discussed in the PEM are linked directly to the relevant SDG goals, including scaling-up the infrastructure, doubling electricity production, increasing access to water, expanding agricultural land, and preserving the ecosystem. The PEM in its present form does not discuss financing needs to meet the SDGs, and so far, there

[1] According to the 2019 SDG report, no country is on track to achieve all 17 goals, and even the best performing countries face some performance gaps.

has been no detailed sectoral analysis to produce sectoral strategies and preliminary estimates of achieving the SDGs.

4. Despite the high-level commitments to the SDGs, challenges remain. A combination of limited financial and human resources, poor basic data collection, and the dispersion of the population across a large area slow progress in the SDGs. The political commitment may also be undermined by the lack of a specific implementation framework to translate efforts into concrete actions.

Figure 1. Madagascar Compared to SSA LIDCs: SDG Goals



Source: SDG Dashboard, 2019.

C. Assessing Spending Needs to Achieve the SDGs

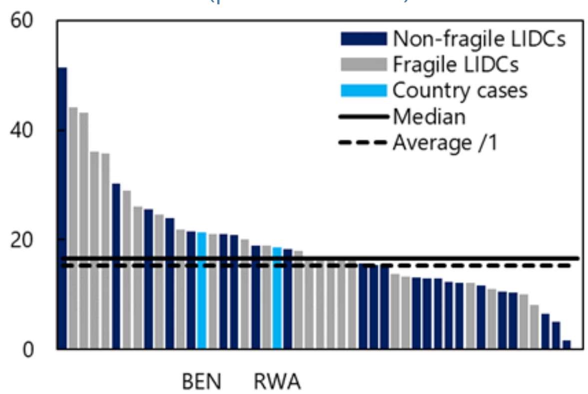
5. The IMF developed a cross-country methodology to estimate the additional annual spending required for meaningful progress on the SDGs.[2] The estimates refer to additional spending in 2030, relative to a baseline of current spending to GDP in five key sectors—education, health, roads, electricity, and water and sanitation. The methodology was applied to a sample of 155 countries: 49 low-income developing countries, 72 emerging market economies, and 34 advanced economies. The analysis was refined with five country studies: Benin, Guatemala, Indonesia, Rwanda, and Vietnam.

6. The estimated additional spending to attain the SDGs in 2030 is US$0.5 trillion for low-income developing countries. The IMF Staff Discussion Note SDN/19/03 finds that delivering

[2] See IMF Staff Discussion Note SDN/19/03.

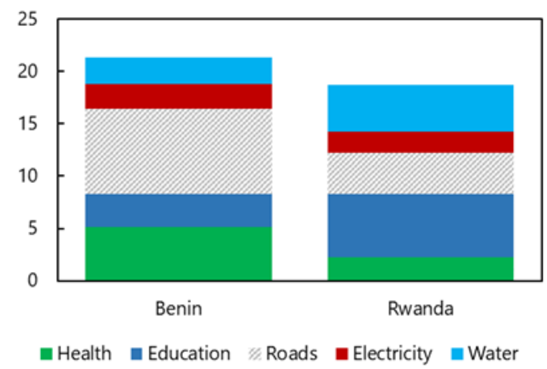
on the SDG agenda will require additional spending in 2030 of US$0.5 trillion for low-income developing countries, equivalent to 15 percent of GDP. Improving spending efficiency can help contain additional spending needs. Spending needs also vary among low-income countries, ranging between 5 and 50 percent (Figure 2). Spending needs for each sector are very different from one country to another: for example, Benin needs more spending on health and roads but less on education and water than Rwanda (Figure 3).

Figure 2. Additional Spending in 2030 to Achieve SDGs in LIDCs
(percent of GDP)



Source: IMF Staff Discussion Note SDN/19/03.

Figure 3. Additional Spending in 2030 to Achieve SDGs in Benin and Rwanda
(percent of GDP)



Source: IMF Staff Discussion Note SDN/19/03.

7. Substantial additional resources would be needed to achieve the SDGs in Madagascar and financing this effort will be challenging. The recent costing exercise estimates additional expenditure needs of around 20 percent of GDP by 2030 for Benin and Rwanda (SDN/19/03 and Rwanda IMF Country Report No. 19/211). Since Madagascar has made less progress towards achieving the SDGs than Rwanda and Benin, costing estimates for Madagascar would likely exceed those of Rwanda and Benin.[3] Financing this effort will be challenging and will require increases in domestic public resources, private investment, and official development assistance (ODA). On the latter, and despite progress since Madagascar's reengagement with the international community in 2014, net ODA received by Madagascar remains low: about US$530 mil-lion per year on average between 2010 and 2017 (about 4.5 percent of GDP), which represents only about 1 percent of total ODA received by African countries over this period.

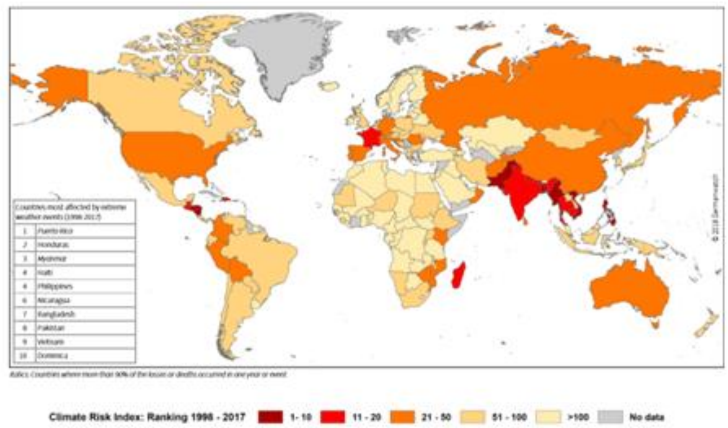
[3] An in-depth country assessment in consultation with the government and development partners would help estimate spending gaps in health, education and selected areas of infrastructure. It would also inform the crucial process of mapping long-term development goals to medium-term budgeting, with priority spending programs and identified sources of financing.

Annex VII. Exposure to Climate Shocks

Due to its location, topography, and socioeconomic conditions, Madagascar is one of the world's most exposed and vulnerable countries to climate change and extreme weather events, with cyclones, flooding, and drought posing the greatest risks. Damages and losses from disasters have a high economic and fiscal impact inhibiting the economy's ability to grow and improve social conditions. Enhancing resilience and response capacity to natural disasters is central to sustained inclusive growth.

1. Madagascar remains one of the most vulnerable countries to natural disasters and climate-related shocks in the world due to its geographical location and topography. Weak socio-economic infrastructure, poverty and heavy reliance on rainfed subsistence agriculture, in a context of limited access to insurance, amplifies the impact of adverse weather conditions on vulnerable households. Limited preparedness and lack of adequate resources further inhibit the country's crisis adaptation and response capacity. In 2019, Madagascar was ranked 17th out of 171 countries in Climate Risk Index (CRI), thus being among the 20 most vulnerable countries in the world (Figure 1).[1]

Figure 1. World Map of the Global Climate Risk Index 1998–2017



Sources: Germanwatch; and Munich Re NatCatSERVICE.

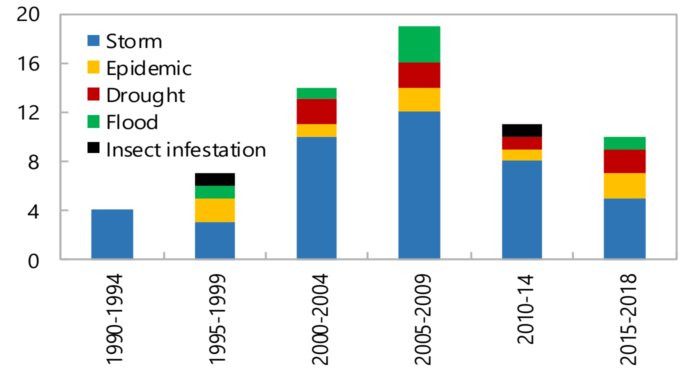
2. Madagascar has the highest risk from tropical cyclones in Africa. Cyclones account for the largest share of the disasters, and these events are becoming increasingly frequent and intense.[2] Since 1990, Madagascar has been struck by 42 cyclones, 8 floods and 7 periods of severe droughts (a three-fold increase over the previous 20 years), causing $1 billion in damages and affecting food security, drinking water supply and irrigation, public health systems, environmental management and quality of life (EM-DAT database) (Figures 2-4). Cyclone Enawo hit Madagascar in March 2017 with winds of up to 290km/h and major floods and landslides; it is estimated at that 433,000 people were affected, out of which almost 250,000 were displaced, and 81 died. More than 83,000 houses were damaged and critical infrastructure was destroyed and there was also extreme damage to food reserves.

[1] The Global Climate Risk Index (CRI) developed by Germanwatch analyses quantified impacts of extreme weather events both in terms of fatalities as well as economic losses that occurred. The countries ranking highest are the ones most impacted.

[2] In the past 60 years, Madagascar has experienced significant increases in daily temperatures across all seasons and pronounced increases in daily maximum temperatures during the dry season; increased variability in the relative distribution of temperature and rainfall, with higher temperatures and decreased rainfall in the northern areas and increased rainfall in the southern areas; reduction in the length of the dry season and longer periods of drought in the central and western parts of the country; and increased intensity of rainfall during cyclones.

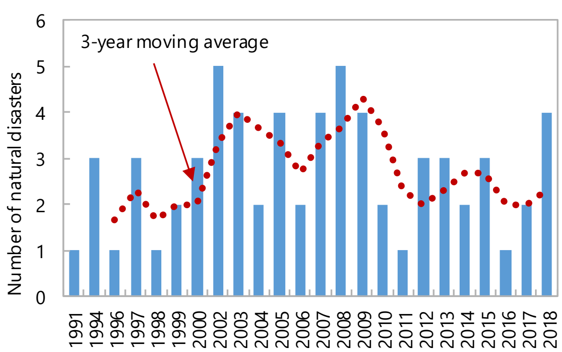
3. Madagascar's high levels of poverty, food insecurity, lack of access to social safety nets and dependence on rain-fed agriculture presents challenges for resilience to natural disasters. With a large and rising proportion of the population living in absolute poverty, food security is a major concern—25 percent of the rural population is classified as food insecure. Disasters disproportionately affect the most vulnerable and therefore pose an important obstacle to poverty reduction if adequate measures are not taken. Relative to sub-Saharan Africa, almost half of the Malagasy population was affected by natural disasters during 2000-19 (Figure 5). Climate change is likely to compound the existing problems of the country's agriculture sector, which include limited productivity, low yields, lack of technical capacity and limited extension services. Rainfall variability and higher temperatures have consequences for the production of staple rainfed crops such as rice, cassava and maize. Extreme weather events lead to loss of real and human capital, as well as threaten agricultural productivity. Madagascar's exceptional biodiversity is also affected by climate conditions. According to the World Wildlife Fund 2018 report, 25 percent of Madagascar's species are threatened by rising temperatures.[3]

Figure 2. Frequency of Natural Disasters



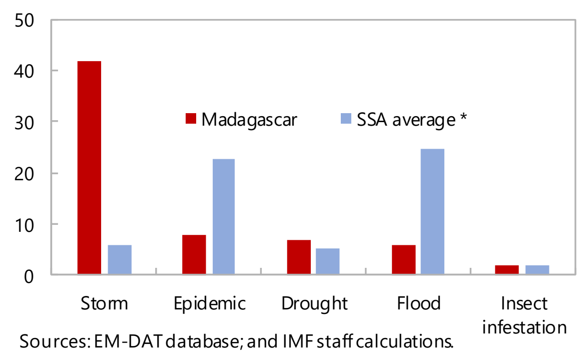
Sources: EM-DAT database; and IMF staff calculations.

Figure 3. Calamity Strikes



Sources: EM-DAT database; and IMF staff claculations.

Figure 4. Natural Disasters by Number and Type, 1990-2019



Sources: EM-DAT database; and IMF staff calculations.
* Average frequency of natural disaters per year from 1990 till 2019.

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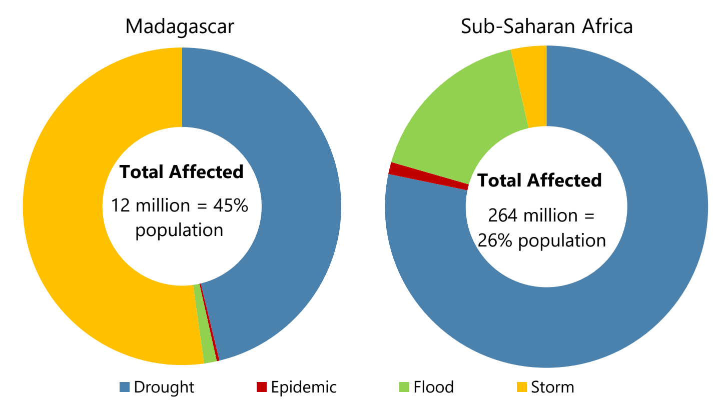
[3] See WWF (2018), "Wildlife in a warming world: The effects of climate change on biodiversity in WWF's Priority Places."

4. The growing frequency and intensity of the climate change shocks has placed immense pressure on the ability to tackle development challenges and improve social conditions. Climate-related disasters are estimated to cost on average, 1 percent of GDP per year.[4] However the annual average masks the severity of major disasters, such as cyclone Enawo, that resulted in damages equivalent to 4 percent of GDP.[5] Reducing these risks could involve strengthening early intervention in case of disasters, improving mitigating measures, as well as reforming social safety nets so that they are further expanded and can be used more flexibly in times of emergency.

5. Integrating climate change within the country's broader developmental agenda is essential. Enhancing resilience and response capacity to natural disasters is also central to sustained and inclusive growth. Madagascar has started to shift its focus from post-disaster relief operations to proactive disaster risk management (DRM) by adopting laws and policies aligned with relevant international frameworks. The authorities' PEM also sets a key priority to strengthen resilience through enhanced access to disaster risk information and identified several specific objectives, including improving the production and dissemination of weather and climate data and strengthening early warning systems; ensuring effective integration of DRM in the national development policy and sector development policies; and enhancing DRM governance. Given the impact that climate related shocks have on physical infrastructure, mitigating measures could include regular maintenance of infrastructure. Creating fiscal space to better prepare and deal with the consequences of future natural disasters will also be crucial. Support from development partners for post-disaster financing remains essential to restore infrastructure and bring the economy on a recovery footing. In particular, the World Bank has been assisting the authorities' efforts at national, regional and local levels, through both analytical work and lending operations, to integrate climate change resilience within their broader development agenda.

Figure 5. Population Affected by Type of Natural Disaster, 2000-19



Sources: EM-DAT database; and IMF staff claculations.

[4] See World Bank (October 2019) "Madagascar Country Economic Memorandum: Scaling Success—Building a Resilient Economy."

[5] See World Bank (2017), "Madagascar Economic Update: Copping with disasters."

Annex VIII. Further Improving Governance and Controlling Corruption

Madagascar's economy is at a turning point, and efforts to address governance, corruption, and to strengthen the business climate can have a lasting positive impact.

A. Background

1. Despite Madagascar's recent improvements, governance challenges remain as reflected in low scores on a range of cross-country indicators. Madagascar's score is particularly low on measures/proxies of corruption, rule of law, and government effectiveness. According to the Worldwide Governance Indicators,[1] Madagascar has regressed over the last 13 years. Performance has improved on measures of freedom of the press, political stability, and absence of violence and terrorism.

B. Recent Developments

2. The new anti-corruption legal framework is a key step to bring Madagascar closer to international standards. The National Anti-Corruption Strategy, adopted in September 2015, aims to complete the legal framework and build necessary institutions. Several important laws passed under this initiative include:

- The *Anti-Corruption Law* (2015), which is essential for the prevention and detection of the laundering of the proceeds of corruption;
- The *Law on Anti-Corruption Centers* (2016), which is needed to establish specialized and independent tribunals;
- The *Law on International Cooperation* (2017), which ensures that anti-corruption agencies can effectively participate in international cooperation;
- The *Law on Anti-Monetary Laundering/Combating the Financing of Terrorism* (December 2018), which requires that financial and non-financial institutions carry out customer due diligence and report suspicious activity; and
- The *Law on Asset Recovery* (June 2019), which ensures that judicial authorities can seize and confiscate illegally acquired assets.

Other recent developments include:

- The first anti-corruption court in Antananarivo was opened in June 2018.
- The Global Competitiveness Report for 2019 ranks Madagascar 125th out of 141 countries in judicial independence (a low score, but a slight improvement since 2016).

[1] The Worldwide Governance Indicators (WGI) report on six broad dimensions of governance for over 215 countries and territories over the period 1996-2018: (I) Voice and Accountability; (II) Political Stability and Absence of Violence; (III) Government Effectiveness; (IV) Regulatory Quality; (V) Rule of Law; and (VI) Control of Corruption. See: https://datacatalog.worldbank.org/dataset/worldwide-governance-indicators.

- On November 4, 2019, the first quarterly meeting of the anti-corruption committee, steered by Comité pour la Sauvegarde de l'Intégrité (CSI), took place. The committee is expected to finalize six implementation decrees with the view to issuing them in early 2020.

3. **Since July 2019, legal reforms have stalled, and further emphasis is needed on developing and reinforcing governance-related institutions for effective enforcement.** The issuance of several implementation decrees (on the anti-corruption centers, on asset declarations, on the reorganization of SAMIFIN and BIANCO, and on the creation of an asset recovery Agency) needs to be accelerated. The government committed to do in early 2020. Failure to issue the decrees will increase the risk of Madagascar being non-compliant with international laws, with potentially significant economic and financial costs. Anti-corruption institutions would benefit from a clear framework as decisions are delayed by inter-agency coordination problems (including insufficient exchange of information), unclear deadlines, and uncertainty regarding when laws and the associated implementation decrees will be passed. Funding increases to these agencies in recent years was reversed when the government announced budget cuts, leaving them underfunded and facing future uncertainty. Several entities are attached to the Presidency, which leads to a perceived lack of independence. A second anti-corruption court is envisioned for Mahajanga, but its establishment and operationalization have been delayed by the slow recruitment of judges.

4. **Madagascar has made noteworthy progress in terms of transparency**. Quarterly statistics on corruption cases based on investigations made by the anticorruption office (BIANCO) and the financial intelligence unit (SAMIFIN) have been regularly published since April 2018. The online platform to publish all final court decisions by the anti-corruption courts provide searchable internet access, using the criteria of topics and presiding judges, and has been operational since early December 2018. All reports and decisions of the Court of Accounts since February 2019 are available. As of September 2019, the number of complaints received more than doubled since 2017, while the number of people prosecuted and arrested almost tripled since 2018 (Table 1). Cases related to abuse of function and misappropriation of public funds reported and investigated also increased significantly. However, no indictments in cases of high-profile individuals have yet been issued by the Haute Court of Justice since they need first to be decided by the Parliament.

Table 1. BIANCO: Selective statistics[1]

	2017	2018	2019
Number of received complaints	1896	2689	4197
of which, investigable	1509	851	1162
Grievances sent to the courts after investigations		179	245
Grievances joined to another grievance		123	156
Number of prosecuted people		415	1111
Number of arrested persons		147	421
Number of persons detained		39	78
Cases related to			
Corruption		63	86
Abuse of function		95	148
Misappropriation of public funds		23	84

Source: BIANCO.

[1] Data for 2019 refer to data from January 1 to September 30, 2019.

C. Going Forward

5. **Governance will remain a key area of focus for the Malagasy authorities**. The Plan Emergence Madagascar (PEM) has set better governance and the fight against corruption as high priorities but, so far, does not provide concrete steps on how to improve governance and control of corruption. Concrete results in fighting corruption can take time and will require sustained efforts on

many levels to improve the quality and trust in the public institutions and ensure a fair and effective implementation of existing laws and regulations.

6. In 2020 Madagascar will be hosting several international events related to governance and will be subject to several international reviews. Madagascar has put in place many of the necessary institutions and laws that are the foundation for good governance, however it lags peers on the effective implementation of this framework, as evidenced by perception surveys of the population and users. An improved implementation of the new governance framework is needed. Further implementation delays could harm confidence and squander the benefits of the progress made.

Appendix I. Letter of Intent

Antananarivo, Madagascar

December 18, 2019

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C. 20431 USA

Dear Madam Managing Director:

1. On July 27, 2016 the Executive Board of the International Monetary Fund (IMF) approved a 40-month Extended Credit Facility (ECF) arrangement with the government of the Republic of Madagascar to help reinforce macroeconomic stability and boost sustainable and inclusive growth. The arrangement was augmented in the context of the first review, and five reviews have been completed, the last one on July 26, 2019. On November 4, 2019 the Executive Board approved a three-month extension of the ECF arrangement to allow time for the conclusion of the sixth and final review, after delays associated with the electoral cycle.

2. The government has made significant progress towards the ECF-supported program objectives to strengthen macroeconomic stability, promote inclusive and sustainable growth, and reduce poverty. Economic growth is expected to be close to 5 percent in 2019, and inflation remains under control. After the smooth electoral period and transfer of power, the government has laid the foundation for the implementation of an ambitious reform agenda to further strengthen macro-economic prospects, including by accelerating economic growth driven by increasing private sector activity and the ongoing scaling up of public investment. The government also attaches the utmost importance to security, the social situation, and the fight against poverty. Our external sustainability remains sound and, based on an updated debt sustainability assessment, the risk of overall public debt distress remains moderate.

3. Notwithstanding this momentum, Madagascar faces persistent and significant challenges as it puts in place the foundation of economic emergence. As a low-income fragile country, Madagascar remains highly vulnerable to external and internal shocks. We aim to make further headway in raising living standards and reducing poverty by promoting inclusive growth. The key fiscal priorities are increasing spending on public investment and social needs, containing the level of lower priority spending, and enhancing revenue mobilization. In addition, reforms are continuing to build a sound and inclusive financial sector, as well as continuing progress in economic governance, especially the fight against corruption.

4. As documented in the attached MEFP, we have met all the performance criteria for end-June 2019 (last test date of the current arrangement), including the one on domestic primary balance. Due to the late adoption of the 2019 revised budget and the reorganization of the ministries the end-June 2019 indicative target on increasing social spending—one of the highest priorities of the government—was out of reach, but social spending has picked up significantly since then. Our structural reform agenda is advancing despite some delays in achieving a few of the structural benchmarks. The structural benchmark on fuel pricing has not been achieved, as the planned implementation of an automatic pricing mechanism by end-September 2019 is now scheduled for March 2020. However, significant progress has been made with the implementation of a revised fuel price structure in June 2019, and the main objective—avoiding direct budget costs of fuel pricing—has been respected so far. The government remains committed to avoid budget costs of fuel pricing, while mitigating potential impacts on the poorest. Due to an emergency, one single source contract for fuel supply has been signed in August 2019 without prior notification to Fund and Bank staff, thereby failing to observe the related continuous benchmark. The two structural benchmarks, on the submission of the financial stability law and banking laws to Parliament are progressing: the banking law has been submitted to Parliament in December 2019, while the financial stability law has been adopted by the Council of the Government and submitted to the Council of Ministers, last step before submission to Parliament. There is also progress for the use of the tax identification number.

5. The attached MEFP describes government policies for the rest of 2019, for 2020 in the context of the budget law, and for the medium term in line with the economic reform agenda described in the Plan Emergence Madagascar (PEM). This ambitious plan which remains consistent with the main objectives of the ECF-supported program prioritizes strategies for (i) higher and sustained economic growth, based on the mobilization of tax revenues and the prioritization of spending, particularly towards investment; (ii) more inclusion, supported by strengthened social policies and spending, with the objective of reducing poverty and a better access to education, health, and housing; and (iii) better governance and institutions.

6. In light of the performance on end-June 2019 targets and continuing progress in implementing the program, we request the IMF Executive Board to approve the completion of the sixth and last review under the ECF arrangement and the disbursement of the final tranche in the amount of SDR 31.432 million.

7. Beyond the conclusion of the last review under the current arrangement, the government of the Republic of Madagascar is convinced that continued financial and technical support from the IMF remains essential, including to help catalyze financial support of donors. In a letter sent on November 6, 2019 to DMD Furusawa, we expressed our desire to start discussions on a successor arrangement consistent with the objectives of the PEM, after the completion of the last review of the current arrangement.

8. The Malagasy authorities agree to the publication of this Letter of Intent (LOI) and the attached MEFP and Technical Memorandum of Understanding (TMU), as well as the IMF staff report related to the arrangement under the ECF, after approval by the Executive Board.

Sincerely yours,

/s/
Mr. Richard Randriamandrato
Minister of Economy and Finance
Madagascar

/s/
Mr. Henri Rabarijohn
Governor
Central Bank of Madagascar

Attachments:
- Memorandum of Economic and Financial Policies
- Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

This Memorandum of Economic and Financial Policies (MEFP) updates the one outlined for the completion of the fifth review approved by the IMF Executive Board on July 26, 2019. It describes recent economic developments, implementation of the ECF-supported program, the economic outlook and risks, and macroeconomic policies.

RECENT ECONOMIC DEVELOPMENTS

1. **Despite a slight slowdown in the first half of the year, economic growth is expected to remain close to 5 percent in 2019.** After reaching an estimated 4.6 percent in 2018—the best performance in the last ten years—economic activity lost some momentum in early-2019 due to weakening external demand, a wait-and-see attitude by the private sector during the election period, and slow budget execution. Recent developments are encouraging including results from recent surveys showing increasing confidence in the private sector (with a significant increase in orders and sales and plans to increase investment and hiring), resumption of budget execution, pickup of tourism, textiles, and the mining sector, and increasing demand for private credit.

2. **At the same time, inflation has remained under control**. Consumer price inflation gradually declined to 6.9 percent year-on-year (y-o-y) in December 2018 after peaking to 10.7 percent y-o-y in November 2017. During the same period, core inflation (excluding rice and energy) was stable at about 6.7 percent y-o-y. Inflation continued to fall in 2019 and was contained at about 6 percent on average during the first three quarters of the year, and only 5.3 percent y-o-y in September 2019.

3. **Fiscal revenue increased in 2019 but fell short of objectives, while spending accelerated in the second part of the year after having been largely under-executed until June:**

- Net tax revenue is expected to reach about 10.5 percent of GDP at the end-2019, an increase from 10.2 percent of GDP in 2018, but lower than the target of 10.8 percent of GDP in the revised budget law. The objective for end-June was met (see ¶7), but difficulties in recovering taxes from two big companies later in the year resulted in the shortfall for the year.

- Due to the installation of the government, the reorganization in the ministries, and the late adoption of the 2019 revised budget law in June, spending was limited in the first half of the year, and directed mainly to mandatory spending (debt service, wages, and pension payments). This resulted in a large surplus of the primary domestic balance estimated at about 1.7 percent of GDP in the first half of 2019. At the same time, the financing of the budget was eased by favorable Treasury bill and bond issuances (after some difficulties in 2018) and the disbursement in June of a $100 million World Bank budget support (more than double the amount initially planned). We took advantage of this opportunity to repay the stock of Central Bank statutory advances (0.5 percent of GDP at end-2018) in the first quarter of 2019 and we did not use them by end-November We also accumulated Treasury deposits at the Central Bank, peaking at

1.9 percent of GDP at end-July 2019 before starting to decline with the gradual normalization of spending.

- Spending started to normalize in July with the implementation of the 2019 revised budget law. The budget execution increased from 25 percent in end-June to 65 percent at mid-November.

4. External developments remain positive. After reaching 0.7 percent of GDP in 2018, we expect a current account deficit of 1.1 percent of GDP in 2019, mainly driven by a decline in vanilla and metals prices, coupled with a reduction in cloves export volumes associated with cyclical production factors. We note that IMF staff expect a smaller current account deficit (about 0.1 percent of GDP), reflecting under-execution of public investment impacting imports (or commitments late in the year that will impact imports in 2020 only). External financing continues to rely on concessional borrowing and our capacity to carry debt is improving.

5. The BFM continues to reduce exchange rate volatility and support gradual accumulation of reserves. After increasing to SDR 1221 million in 2018 or 4.3 months of imports, reserves have increased slightly in 2019, standing at SDR 1238 million at end-October 2019—still above 4 months coverage of imports. In the context of the flexible exchange rate regime, the BFM has continued to follow the algorithm developed with Fund technical assistance (TA) to reduce volatility and support gradual accumulation of reserves. BFM net purchases of foreign currencies have been negative so far in 2019 (by US$25 million by end-October) after some interventions in late September and early October to support the ariary. Overall, the NEER depreciated by 4.2 percent year-on-year through end-October, and the REER depreciated by 1 percent, reflecting higher inflation in Madagascar compared to its trading partners.

6. Despite volatile conditions, the BFM has successfully managed inflation and bank liquidity. Inflation has continued its downward path, as described above. Bank reserves are usually both cyclical and volatile in Madagascar, notably impacted by the cycle of vanilla, exacerbated in recent years by historically high prices. While banks lose liquidity when they provide currency to vanilla farmers who keep much of their savings in cash, they gain liquidity when they sell foreign exchange (mainly related to vanilla exports) to the BFM. In addition to these cyclical variations, bank liquidity has been impacted in the first half of 2019 by the government underspending and the accumulation of Treasury deposits at the BFM. As a result, in June 2019 bank reserves were only 7 percent above the required reserves—the lowest in two years—and BFM carried out several liquidity injection operations between July and August to increase in banks' reserves. BFM's management of liquidity has led to developments in monetary aggregates in line with the objectives of growth and inflation. Credit to the private sector growth accelerated from 14 percent y-o-y in early 2019 to 20 percent y-o-y in September 2019 and remains consistent with macroeconomic stability and financial sector soundness.

PERFORMANCE UNDER THE ECF-SUPPORTED PROGRAM

7. Performance on the program's quantitative targets at end-June 2019 was strong, with all performance criteria (PC) met:

- The domestic primary balance target, fiscal anchor of the program, was met with a wide margin. While the target for the first six months of 2019 was slightly negative, the domestic primary balance recorded a surplus of MGA868 bn (1.7 percent of GDP) reflecting the large budget under-execution in the first part of the year but also good revenue performance. The indicative target (IT) on net tax revenue has been achieved at end-June 2019, with the total of domestic tax revenue and custom revenue reaching MGA 2805 bn, equivalent to 5.5 percent of GDP, in line with the target of 10.8 percent for the entire year.
- However, the IT on domestically financed priority social spending was significantly missed, due to the late adoption of the revised budget law in June. There has been significant progress since end-June with domestically-financed priority social spending accelerating: commitments have increased by twelvefold between end-June and end-November (MGA 17 billion to MGA 203 billion, respectively). Going forward, the government is committed to further prioritizing social spending and is taking measures to avoid execution delays in 2020 (see ¶14).
- Regarding the central bank, the floor on net foreign assets has been met, as well as the ceiling on net domestic assets with a substantial margin given government spending under-execution.
- Finally, the performance criteria of zero accumulation of new external payment arrears and on the present value of external debt contracted were respected. Indicative targets for ceilings on new long-term non-concessional external debt as well as for short-term debt, were also met.

8. Despite some delays mainly related to the electoral period and the installation of the new Parliament, progress in the implementation of the structural reform agenda continued. Three of the eight remaining structural benchmarks (SBs) were observed, and there was significant progress for the others:

- We have observed the continuous SB on governance related to transparency in PPPs. Regarding JIRAMA's procurement activity, in the context of severe electricity shortages in the capital and to ensure the continuity of fuel supply to the public utility, one single source contract for fuel supply has been signed in August 2019 without prior notification to Fund and World Bank staff, thereby failing to observe a continuous benchmark. With this exception, the practice of single source contracts in use until 2016 has been eliminated.

- The end-July 2019 SB related to fiscal revenue mobilization, on the adoption of a strategy for the control of high-risk sectors, has been achieved, as well as the end-August 2019 SB on establishing a public registry of companies that have violated the procurement regulations and are prohibited from participating in future bids.

- The Tax Identification Number (TIN) is in use in all the directorates of the Ministry of Economy and Finance, at the Ministry of Trade, at CNAPS, and at INSTAT. The project of introducing a unique national identifier (PRODIGY) will allow unification of the national identification system.

- The submission to the Parliament of the banking law (SB for end-2018) and of the law on financial stability (SB for end-June 2019) have been delayed. The draft banking law and the draft law on financial stability have been finalized and validated by all stakeholders and were approved by the Council of Government on November 21 and submitted to the Council of

Ministers, the last step before submission to Parliament. The banking law has been transmitted to Parliament in early-December.

- Finally, the continuous SB on fuel pricing is not met as the objective of starting to implement the automatic fuel pricing mechanism no later than end-September 2019 was not possible due to residual uncertainties on the application of the refence price structure. The setting of a new price structure in June 2019, applied retroactively from January 2019, was a crucial first step towards the objective to set the automatic fuel pricing mechanism: it closed the gap between pump and reference prices for the first half of the year, reduced significantly the liabilities due to oil distributors, and allowed for a reduction of pump prices, in particular for kerosene (which is consumed by the most vulnerable). While a gap between pump and reference prices has appeared again in the second part of 2019, it has been limited to 4-5 percent since July. Furthermore, the final objective of this SB—avoiding direct budget cost from fuel pricing—has been respected so far.

ECONOMIC OUTLOOK AND RISKS

9. The macroeconomic outlook continues to be favorable. The Plan Emergence Madagascar (PEM) assumes a gradual increase in real GDP growth from 5.5 percent in 2020 to 7 percent in 2023. These projections, which are higher than those in the current ECF arrangement, are based on improvements in both the quality and quantity of public investment in infrastructure, despite recent under-execution, and on increasing private sector activity, especially tourism, light manufacturing (e.g., textiles), mining, and agriculture. Current projections for private investment, including foreign direct investment, could prove conservative, provided a substantial portion of announced plans materializes more rapidly than forecast. We will also focus on gradually enhancing the productivity of smallholder agriculture and developing export-oriented agribusiness to support inclusive growth. We are also confident that we can contain inflation within single digits and towards a long-term objective of about 5 percent per year.

10. Nonetheless, we are aware of the vulnerabilities faced by Madagascar, as a low-income country with an open economy and continuing weaknesses in institutions. The country remains highly vulnerable to natural disasters (cyclones and droughts), and terms of trade shocks, particularly from oil, metal and vanilla prices. In addition, growth could remain below our expectations if implementation of public infrastructure investment continues to be slower than expected. The government continues to work on the identification, monitoring and, where possible, mitigation of fiscal risks, including those related to state-owned enterprises (SOEs), especially JIRAMA, or to the deficit of the civil and military pension fund.

11. We believe that there are also upside risks, particularly for growth. We are convinced that our efforts to accelerate the scaling-up of public investment will bear fruit, consistent with our objective of a growth rate of at least 6 percent per year on average. In addition, current projections for private investment, including foreign direct investment, could prove to be conservative, provided a substantial portion of announced plans materializes more rapidly than forecast.

MACROECONOMIC AND STRUCTURAL POLICIES

A. Creating More Fiscal Space to Support Inclusive Growth

12. The 2020-budget adopted by the National Assembly on December 2, 2019 and then discussed with the Senate will be passed by the end of 2019. The budget reflects the assumptions of the PEM while remaining consistent with the ECF objectives.

- **We target a net tax revenue ratio of about 11.5 percent of GDP**, a significant increase of more than 1 percentage point compared to 2019. This objective builds on ongoing improvements in tax and customs administration, including stronger verification of declared values for imports, better collection of the VAT payments on public investment projects, enhanced collection of tax arrears, and centralized financial management of the tax receipts, as well as tax measures included in the budget law. These measures account for 0.7 percent of GDP and include: (i) the broadening of the VAT base, including the restoration of taxation of wheat and corn and the generalization of VAT on public procurement (expected yield of more than 0.4 percent of GDP); (ii) the increase in some excise duties on beer, tobacco, precious stones, semiprecious stones and mobile telephones (expected yield of almost 0.2 percent of GDP); (iii) the introduction of income tax on dividends for non-resident individuals and companies; (iv) income tax at the rate of 10 percent on education and health sector revenues; and (v) the introduction of a 2 percent installment on income tax to be collected from all export-related operations (expected yield of 0.1 percent of GDP).
- **The draft budget does not include any transfers to JIRAMA so far.** The government plans to introduce a transfer to JIRAMA (through a revised budget law) once financing needs are assessed. Cost-saving measures continue to be implemented including the renegotiation of contracts with suppliers, the clearing of outstanding bills to JIRAMA by ministries and public institutions, the acceleration of the introduction of additional smart meters, the development of hybrid solar plants and hydroelectric facilities, the fight against fraud of electricity, and increased efforts on bill collection.
- **The wage bill is close to 5 percent of GDP.** The increase compared to 2019 can be explained by the wage increase proposed by the Government, which amounts to 0.3 percent of GDP, and the change in the workforce, notably the new hires for the National Gendarmerie, the National Police, Defense, Education and Health, in line with the government's priorities on social sector and security. The wage bill also includes a temporary increase equivalent to 0.05 percent of GDP per year over 2019-2022 to integrate contractual teachers in the civil service.
- **Transfers to the civil servants and military pension fund are limited to MGA 354 bn.** This level reflects credible assumptions for the anticipated deficit for 2020 to limit the risk of additional slippages that will need to be compensated by additional spending under" Other Net Treasury Operations", as done in recent years.
- **Investment is planned to reach 8.7 percent of GDP**, from an anticipated/estimated 6.0 percent in 2019, in line with the government's priorities under the PEM. Authorities plan a domestically-financed public investment spending of an unprecedented level of 4.1 percent of GDP, more than doubling compared to 2019. Externally-financed investment is projected at

about 4.5 percent of GDP from 4 percent in 2019. These ambitious objectives will be supported by ongoing efforts to improve implementation capacity (see ¶14).

- **Priority social spending is set to slightly increase to 1 percent of GDP (MGA 555 bn).** In 2018 and 2019, priority social spending (as defined under the TMU, ¶22) fell short of initial objectives. The government is firmly committed to execute the planned spending in 2020, and measures to further prioritize and accelerate the execution of this high priority spending are described in paragraph 14. Also, this does not include externally financed social spending; social spending that is part of the budget envelope of other (non-social) ministries, of the Presidency or the Prime Minister's Office; or salaries for teachers or medical staff. Including all these categories of spending, social spending is much higher.
- **Overall, the domestic primary balance is expected to remain positive at 0.2 percent of GDP**, in line with our objective to preserve medium-term public debt sustainability. The 2020 budget is fully financed, including through budget support committed by the World Bank (Human Capacity Development Policy Operation of US$100 million) and the European Union, and with relatively conservative net domestic financing assumptions.

13. We are ready to implement contingency measures if our revenue assumptions do not materialize. We note IMF staff advice about the challenges of increasing tax revenue by more than 1 percent of GDP (more than the increase during 2016 to 2019) in one year. The alternative scenario by the IMF, consistent with a full financed budget, considers an increase in tax revenue by 0.6 percent of GDP, limiting domestic public investment to about 3 percent of GDP based on identified prioritization of projects, and increasing transfers by 0.3 percent of GDP compared to the budget. We are confident that our revenue projections will materialize, but, nevertheless, we have scheduled a prudent phasing of expenditures, reflected in cash flow, and identified a contingency plan for shortfalls in tax revenue. This contingency plan includes a set of non-priority spending that, as a last resort, could be postponed, while protecting social and investment priority spending. These revisions would be part of a revised budget law.

14. Beyond the 2020 budget, we remain committed to increasing fiscal space over the medium term for priority spending:

- We aim to contain the **wage bill** at a sustainable level, with the objective of continuing its reduction as a percentage of tax revenue. The use of our IT tool for payroll management (AUGURE) will improve the accuracy and comprehensiveness of the budget in this area. These forecasts will include the payment of teachers that are not part of the civil servants (currently budgeted under transfers), as well as all allowances, including the "*dette d'avancement*" accumulated by postponing promotions. On the latter, we will fulfill past unmet obligations for grade promotions, which requires additional one-off outlays until 2022. Building on past verifications of ministries' payroll, and on the implementation of recommendations from the recent audit funded by the EU, our efforts will continue to enhance payroll management. Our objective is also to ensure the alignment of wage bill projections and sectoral medium-term spending plans, and to adopt, in due course, an updated overall strategy of modernization of Madagascar's civil service.

- Total transfers are highly dependent on the amounts allocated to the **civil servants and military pension fund**. A Fiscal Affairs Department (FAD) technical assistance mission in April 2019 proposed measures to better assess the anticipated deficit and accommodate related government financing in the budget, as well as a set of cost saving reforms. Among our priorities, we are committed to (i) unifying the CRCM (Caisse de Retraite Civile et Militaire) and CPR (Caisse de Prévoyance Retraite) under homogeneous and revised benefit rules (lower accrual rates, discontinuing the practice of some bonuses); and (ii) improving the transparency of accounting and fiscal reporting of CRCM and CPR. We are also aware of the risks related to the sustainability of the National Social Security Fund (Caisse Nationale de Prévoyance Sociale, CNaPS) and we plan to assess the possibility of revising the benefit calculation rules, investing reserves, and commissioning a new actuarial assessment.

- As soon as a medium-term recovery plan **for JIRAMA**, currently under preparation with the support of the World Bank, is finalized, we commit to start its implementation. This plan aims to balance JIRAMA's accounts, address the issue of accumulated liabilities to avoid risks of increased public transfers and financial distress, and improve the production and distribution of electricity. To this end, a broad strategy was presented on October 12, 2019 by the consultant firm hired by the World bank and endorsed by the company's board. It specifies measures including efficiency improvements (such as optimizing fuel supply and improving collection); a strategy for restructuring arrears (estimated to about 3 percent of GDP); the renegotiation of thermal contracts; investments in hydro-electricity; possible adjustments in the tariff schedule; and a residual subsidy from the government to cover the cash deficit. While working out the details of the plan, in the context of increasing water and power outages with mounting social and economic implications, a decision was taken to repay MGA 501 bn (1 percent of GDP) arrears to JIRAMA suppliers before the end of 2019.

- We will continue to monitor the implementation of the multi-year business plan of **Air Madagascar** after its restructuring in 2017, which came with an exceptional support of the government in an amount equivalent to about 1 percent of GDP. To respect the initial objective of avoiding additional budget transfers to the company in the future, the recovery of the company remains essential. The government is therefore determined to fulfill its obligations under the partnership agreement, including commitments regarding additional landing rights for foreign airlines.

- While the fiscal risk associated with **fuel pricing** is limited (the cumulative liability towards distributors is lower than 0.3 percent of GDP), we are determined to address the issue. We still plan to implement an automatic fuel pricing mechanism by March 2020 but first we will validate the implementation details of the reference price through an ongoing independent audit, whose results are expected by end-year. The Malagasy Office for Hydrocarbons (OMH), which is responsible for calculating the average reference price and the price at the pump, will act as an autonomous body responsible for the implementation of the automatic pricing mechanism, and the transparent communication to stakeholders and the public. The liability to distributors, which could approach MGA 170 bn at the and-2019 (slightly above the limit agreed under the ECF), will be settled by end-2020, through savings from the positive differential between the pump and reference price, or by other measures.

- We are strengthening our **fiscal risk** management. Fiscal risks such as the pension fund, JIRAMA and other SOEs, fuel pricing, public-private partnerships (PPPs), and risks associated with natural disasters or term-of-trade shocks, are documented in an annex to the 2020 budget law, following a good practice established since 2018. With support of an FAD TA mission in July 2019, we have strengthened this analysis, which includes more details on appropriate measures if these risks materialize. In addition, given the expected increase in public guarantees, we will take stock of all public-sector guarantees, exploring the possibility to provision for all new guarantees in the budget. It is also important to manage the fiscal risks associated with PPPs. The institutional framework and procedures are in place to manage these risks: our staff have the technical skills to assess the financial viability of each project, and we plan to set limits on overall guarantees for PPPs. With the support of the World Bank and the African Development Bank, we are also developing standard guidelines to be used within the different Ministries. Certain aspects of the laws and the decrees under preparation could be revised to accelerate the procedures, incorporating feedback from stakeholders and in coordination with the World Bank. For transparency purposes, we remain committed to publish the terms and conditions of all PPP contracts within one month of the date of their signature on the website of the Ministry of Economy and Finance.

- Strengthening **social policies and spending** is among the highest priorities of the government, as stated in the PEM. We plan to put in place an expenditure classification to track all social spending by non-social ministries. To avoid delays in the commitment of this priority spending or its under-execution (as observed in 2018 and 2019), measures have been taken, such as supporting institutions and ministries, streamlining regulatory procedures with the establishment of one-stop shops for public procurement, and the organization of regular meetings between the Ministry of Economy and Finance and sector ministries dedicated to execution issues. These issues were discussed at the Council of Ministers to ensure better execution of the Minsters' respective budgets. We are also working to expand to three additional regions existing social safety nets, like the Human Development Cash Transfer—a conditional cash transfer program providing regular cash benefits for families with children 0-12 years—and the Madagascar's Productive Safety Net program—which provides cash for work opportunities over three years. These programs are supported by the World Bank, which recently provided a US$ 90 million grant, retroceded to the Development Intervention Fund. This record funding for safety nets in Madagascar will help the government to increase the access of extremely poor households to safety nets and lay the foundation for a social protection system.

- **Investment capacity.** Additional efforts to boost investment implementation capacity are needed, as the pace of scaling up public investment has not accelerated as much as initially targeted. Following recent FAD mission recommendations to strengthen investment capacity, the Ministry of Economy and Finance (MEF) is preparing a guide on public investment management (PIM) and the Organization for the Coordination and Monitoring of Investments and their Financing (OCSIF)—in charge of coordinating and trouble-shooting investment—is developing a database of all projects to improve their monitoring and detect implementation issues. To translate the PEM assumptions into a credible spending trajectory, aligned with the availability of funds and absorptive capacity, we are preparing a rolling three-year investment plan consisting of major projects, and we have plans to better estimate their costs and to include them in the budgetary documents. In the context of the 2020 budget, we will start the implementation of new procedures to account for and manage the "*autorisations d'engagement/credits de paiements*" (AE/CP) for selected ongoing multiyear public investment, including with new IT tools. In addition, following another recommendation from the PIMA TA mission, efforts are being made to strengthen inter-ministerial coordination to ensure better complementarity of investment projects.

15. We will continue to use primarily concessional borrowing to fund much-needed investment responsibly subject to the implementation and absorptive capacity while containing risks of public debt. Our medium-term debt strategy is to maximize concessional lending, keeping non-concessional lending limited to around 2 percent of the external debt stock. However, the portfolio of new external financing is expected to shift towards a more balanced distribution of concessional and non-concessional debt beyond the medium-term.

16. We are defining a comprehensive revenue administration and revenue collection strategy to support our ambitious medium-term revenue mobilization plans:

- The gradual increase in the net tax-to-GDP ratio from 8.4 percent of GDP in 2014 to 10.4 percent of GDP in 2019 has been a major achievement. However, this level remains low in absolute and relative terms, compared with other SSA countries. In line with assumptions under the PEM, our goal is to increase the net tax-to-GDP ratio to 15 of GDP by 2023. This strategy will rely on further reforms to improve the functioning of tax administrations, and on new tax policy measures. It will build on the tax policy unit, which reports to the Secretary General of the Ministry of Economy and Finance and whose main task is to produce comprehensive domestic tax and custom revenue analyses, including tax policy options. The unit has already undertaken an impact analysis of tax expenditures for 2016, 2017 and 2018, and finalized an analysis of the tax potential in Madagascar, identifying significant margins of progress. We will also continue to build on IMF's FAD technical assistance recommendations.

- Specific efforts are needed for domestic tax collection. On the administrative side, we will focus on (i) the generalization of performance contracts at the Directorate General for Taxes (DGI) from 36 operational units in 2018 to 113 by the end of 2019; (ii) the consolidation of the taxpayer segmentation, considering that the largest taxpayers managed by the Directorate of Large Enterprises (DGE) account for 0.2 percent of total taxpayers and 80 percent of total tax collection; (iii) the development of online tax declaration and payments, already in place for large companies since October 2019; (iv) the strengthening of fiscal controls, based on risk analysis, , and use of the unique TIN; and (v) the strengthening of our recovery plan for outstanding tax payments (*Restes à recouvrer, RAR*),. In terms of tax policy, we plan: (i) a gradual reduction of tax expenditures by the cancellation of exemptions with limited beneficial impact; (ii) innovation through the digitization of tax transactions (for example the system for monitoring goods subject to excise tax such as cigarettes and alcoholic products); and (iii) the implementation of a national risk-based internal control plan.

- Regarding customs revenue, the aim is to build on the strong performance of recent years despite some lower tariffs arising from Madagascar's trade agreements. Building on recommendations of recent TA missions, we plan to adjust the performance indicators and expand performance contracts to smaller customs offices, the clearance center, and the risk analysis center. All managers will also sign *conventions d'objectif*. Nearly all major offices were equipped in 2018 with the ASYCUDA World system, which started to improve the sequencing and timeliness of clearance operations. We are also improving our control process, with systematic profiling and risk analysis as soon as the goods are loaded; and prices comparison declared by importers with other sources of objective transactional values. In order to secure the tax base, a control strategy targeting companies, free zones, and zones under exceptional tax regimes, coming with a chronogram of actions, has been established. We plan to improve the information system by putting open data online, contributing to the strengthening of internal control at Customs and the provision of tools external stakeholders. An analysis in collaboration with major universities is also underway to develop our tools for risk analysis. We are also planning the establishment of a specific statute for Customs Administration agents to optimize our Human Resources Management.

17. We are determined to ensure that new tax incentives for investment are effective and cost-efficient to safeguard our core objective **of boosting revenue collection.** For the implementation of the new law on Special Economic Zones approved by Parliament in April 2018, we reiterate our commitment to start with pilot projects limited to at most two geographic locations, which will focus exclusively on exports in one or two clearly defined sectors. The implementation of the Law for Industrial Development will likewise start with pilot projects limited to at most two geographic locations, which will focus on one or two clearly defined sectors. For these two laws, the tax code revisions and issuance of implementing decrees will rely on cost-based incentives (investment credits or accelerated depreciation exclusively for capital goods) rather than profit-based incentives, consolidate all tax incentives into the tax law, and adopt rules-based approaches to avoid discretion in granting tax incentives. Before taking any further actions, we will assess the costs and benefits of pilots for both laws. More broadly, we plan to review the tax code as the overarching legal framework governing tax incentives with a view to harmonizing the regimes in the medium-term (including the free trade zones or *zones franches*), drawing on technical assistance in this area from the IMF and other partners.

B. Enhancing Economic Governance and Fighting Corruption

18. The anti-corruption legal framework has been established and will be complemented by the issuance of some implementation decrees. We have significantly strengthened the legal framework with the adoption of several laws (*law against the traffic of precious woods* in 2015, *anti-corruption law* and *law on anti-corruption courts* in 2016, *international cooperation law in criminal matters* in 2017). The law on *anti-money laundering and combating the financing of terrorism (AML/CFT)*, which brings our AML/CFT framework into closer alignment with international standards, was enacted in February 2019, and the *asset recovery law*, which ensures that judicial authorities can seize and confiscate proceeds of crime, has been adopted through presidential ordinance in July 2019 (and published in August 2019). To expedite the application of these laws, we will issue the implementation decrees associated with the anti-corruption law and AML/CFT law in early 2020. To make further progress in terms of transparency, we also started publishing all reports and decisions of the Court of Accounts since February 2019.

19. We are also reinforcing the institutions for effective enforcement of this new legal framework. Quarterly statistics on corruption cases based on investigations made by the anti-corruption office (BIANCO) and the financial intelligence unit (SAMIFIN) (consistent with the technical memorandum of understanding, TMU) have been regularly published since April 2018, with statistics up to Q3 2019 published. The first anti-corruption court has been opened in Antananarivo in June 2018 and the establishment and operationalization of a second one in Mahajanga is ongoing. The online platform to publish all final court decisions by the anti-corruption courts providing searchable internet access (using the criteria of topics and presiding judges), has been operational since early December 2018. To implement the anti-corruption law, the establishment of a mechanism to verify asset disclosures from officials (covered under article 41 of the constitution and Article 2 of the anti-corruption law) will become operational with the adoption of the related decree (see preceding paragraph). Over the medium term, to ensure that asset declarations are comprehensive (covering both assets legally owned and beneficially owned), verifiable, subject to dissuasive sanctions for non-compliance, and progressively made publicly available online, we are drafting a strategy, starting with discussions with new authorities for the necessary legal reforms, including drafting the legal texts, for consideration by the government in 2019.

20. To facilitate private investment, we are making efforts to improve business environment. Over the last year, we made substantial improvements in three categories related to the Doing Business indicators. We strengthened construction quality control by appointing an independent architect in the commission tasked with reviewing building permit applications and reduced cost to obtain permits; made enforcing contracts easier by introducing an automated system that reduces by 300 days the time it takes to resolve disputes; and improved access to credit information through the introduction of a new law governing the establishment, licensing, and functioning of a credit bureau.

21. We remain committed to strengthen public financial management (PFM), as part of our efforts to enhance good governance, transparency, and sound public finances. The PEFA self-evaluation completed in January 2018 identified progress, but also some persistent weaknesses. In July 2018, we adopted an updated 2018-2026 Strategic Plan of Modernization of Public Financial Management, including its translation into an Action Plan for the 2018-2020 period, building on the conclusions of Fund FAD TA.

- We developed a medium-term fiscal framework in 2017, and we are working on strengthening the budget preparation process. Recent improvements include the publication of annexes to the budget on fiscal risks (starting with the 2018 budget) and on fiscal costs of key tax incentives (with the 2019 budget). We are also working to improve the wage bill and the civil pension fund forecasts, drawing on IMF TA, as well as revenue forecasts, relying on the Tax Policy Unit.
- The new draft law on treasury management was adopted by the Council of Government on November 20 and submitted to the Council of Minsters last step before submission to Parliament.
- We will continue to enhance the management of fiscal risks and the coverage of the budget, by better supervising and integrating autonomous entities, SOEs, and PPPs. The revised law

governing the National Public Establishments (*Etablissements publics nationaux*, EPN) was adopted in December 2018. Inter-ministerial discussions are ongoing to finalize the application decrees planned to be issued in 2020.

- To implement the Code of Public Procurement passed in 2017, the separation of the functions of regulation and control is now effective. We are also working on the decree to formalize and sustain the funding of the ARMP (Authority of Regulation of Public Procurement). Actions following up on the audit of ARMP completed in September 2017 have been incorporated into the broader PFM action plan. We are conducting outreach activities to inform the private sector and civil society of these improvements. We are ready to make public and easily accessible a registry of companies that have violated the procurement regulations and are prohibited from participating in future bids (SB for end-August 2019), but without any cases at this stage. Finally, we expect to conduct a study on migrating to an e-procurement system in 2020.
- We are strengthening our debt management strategy by updating and reporting statistics regularly, documenting contingent liabilities exhaustively, and extending the maturity of domestic debt instruments to reduce exposure to rollover and interest rate risks. The 2018 DEMPA (Debt Management Performance Assessment) noted the ongoing progress on this front as well as areas for further improvements.
- To reinforce ex post controls and the PFM system's contribution in the fight against corruption, we are strengthening audit bodies and internal inspections, especially the Court of Auditors (*Cour des comptes*). In 2018, we have started publishing the final decisions taken by the Council of Budgetary and Financial Discipline, as well as statistics on its action (including decisions).
- Finally, to improve coordination and leadership of our PFM reform strategy, we have reorganized the steering committee. We are also testing a portal dedicated to PFM reforms on the website of the Ministry of Economy and Finance to promote the exchange of information between all the stakeholders of the reforms, which should be launched in 2020.

C. Maintaining Stable Inflation and Building External Resilience

22. We remain committed to keeping inflation in single digits, with a focus on managing fluctuations in bank liquidity. We continue to actively manage bank liquidity, which remains volatile, in order to maintain an appropriate policy stance of our macroeconomic policy, closely monitoring potential inflation pressures. The BFM is strengthening its monetary policy framework by continuing the gradual transition from monetary aggregates targeting to interest rate targeting policy. With this objective, the BFM introduced a short-term interest rate corridor in May 2019 revised in November 2019 with a deposit facility rate (set at 0.9 percent), and a loan facility rate set at 5.3 percent. To support the use of collateral for interbank lending, the draft legislation on repo transactions was submitted to Parliament in December 2018 (structural benchmark) and could be examined by the current Parliament session. The principle of appropriate discounts on debt instruments when used as collateral for borrowing from the BFM, as commonly done internationally in monetary markets, has been introduced in this law. In preparation for these operations, a convention between the MEF and the BFM will grant the BFM real-time access to the database on Treasury bonds (BTFs). A law on collateral (*suretés*) is also in preparation with the Ministry of Justice. It is under review by the CRDA and will be submitted to Parliament for its first session in 2020.

23. In pursuit of our mission of safeguarding external stability, we will continue building international reserves, in the context of a flexible exchange rate regime. Our interventions on the foreign exchange market remain guided by an algorithm (developed with Fund technical assistance) to limit exchange rate volatility and build reserves. Successful implementation of the algorithm resulted in significant accumulation of international reserves in recent years, from about SDR 835 million at end-2016 to SDR 1238 million at end October-2019 (equivalent to 4.3 months of imports). Our long-term objective, consistent with convergence criteria at the regional level, is to gradually increase import coverage to 6 months or more, depending on the timing of external program support and other circumstances.

D. Building a Sound Financial Sector Supporting Growth

24. Efforts to promote greater access to financial services are ongoing. Following the modernization of the legal framework, by adopting and enacting a law regulating the establishment, the licensing, the operations, and the supervision of a private credit bureau, we selected an investor in July 2018. The bureau received its license in December 2018, and the migration of the data of the credit registry at the central bank towards the bureau is underway and will be completed in the second half of 2019, and data collection will begin in January 2020. After the issuance in September 2017 of decrees on the implementation of the law on electronic money and electronic money institutions, the development of payment through electronic money is ongoing, notably with the licensing of a first company to provide these services and the processing of two other applications.

25. Reinforcing financial stability, implementing risk-based supervision (RBS), and containing systemic risk remain priorities:

- The new banking law adopted by the Council of Government on November 20, 2019 was submitted to the Council of Ministers, last step before submission to Parliament and will: (i) improve the bank recovery and resolution framework in line with the Financial System Stability Assessment (FSSA) recommendations; (ii) enhance the powers and independence of the financial supervisor (CSBF), including legal protection of Commission members and supervisors; and (iii) reinforce the framework for corrective bank supervisory measures, with specific triggers, responsibilities, and time limits for an effective response to bank violations and vulnerabilities to be determined by the law or regulation.

- We will prepare the implementing text of this law in accordance with international standards and ESSF recommendations. We will approve updated prudential directives by end-June 2020 on capital adequacy, liquidity, concentration of risks, and classification and provisioning of credit risks, in line with international standards and FSSA recommendations

- A law on financial stability, in line with international best practices, has been drafted, has been validated by the Committee for the Reform of Business Laws (Commission de Reforme du droit des affaires, CRDA) and adopted by the Council of the Government on November 20, 2019. It will establish a national structure in charge of analyzing, identifying, and preventing systemic risks, as well as managing and addressing financial crises.

- Significant progress has been made towards the implementation of risk-based supervision (RBS) drawing on the action plan adopted in December 2017. The methodological framework for individualizing the risk profile of banks has been finalized with the technical support of a Fund AFRITAC South expert in May 2019, a new software has been deployed, and additional staff recruitment and training are underway with the view to start implementing effective RBS both in the banking and microfinance sectors.

26. Concerning non-bank financial institutions, the work to follow-up on recent audits of the CEM *(Caisse d'Epargne de Madagascar)* and PAOMA *(Paositra Malagasy)* is continuing. In March 2019, CEM obtained its license by the CSBF to operate as a microfinance institution, in line with the existing action plan. The government intends to set up a working group to elaborate a development plan for PAOMA, which has started taking stock of its property assets and is preparing a full audit of its customer accounts. The audit of the financial statements for the period 2015-2017, the audit of clients' accounts and the development of the procedures' manual are on track to be completed by the end of 2019.

27. With support of the IMF TA, we are working to further develop the foreign exchange market, which remains shallow and prone to volatility. This situation typically worsens during periods of volatile foreign exchange movements when some bank clients chose to keep significant balances in foreign currency accounts or not repatriate export proceeds for speculative reasons. Considering the situation, the MEF, in consultation with the BFM, introduced a surrender requirement of 100 percent in August 2014, which was reduced to 70 percent in June 2016. We have prepared a draft revised law on the foreign exchange market, based on Fund TA. After initially being presented to the banking sector, the law is currently undergoing additional revisions to help address contradictions across the legal corpus and to make the split in responsibility between the BFM and the MEF more explicit. The revised law is expected to be presented to Parliament in May 2020. Following adoption of the law, we intend to issue the implementing ordinances and to adopt the plan to phase out surrender requirement. The plan aims at gradual phasing out if conditions do not destabilize the market. In this regard, we have conducted further technical analysis of the market and anticipate additional new potential sources of volatility as repayment of foreign financing increases.

28. The BFM's modernization is continuing, with a reform agenda to increase transparency and to render it more financially independent. BFM remains committed to full adoption of International Financial Reporting Standards (IFRS) for the 2020 accounts (expected by April 2021). We have developed an action plan, supported by IMF technical assistance, to achieve this goal, and we in May finalized a gap analysis to be followed by pro-forma IFRS financial statements for fiscal year 2018. We have scheduled more capacity building for late 2019. We will also consider the capital adequacy of the BFM, including the possible impact following full IFRS implementation, as part of a longer-term strategy to safeguard the financial autonomy of the bank. We have also made progress with the destruction of old bank notes, and the stockpile that existed at end-December 2017 was eliminated by end-June 2018 and we are preventing any new backlog. In 2019, the internal audit department will conduct a review of the implementation of the revised bank-wide procurement policy approved in June 2017. This audit will be repeated periodically. More broadly, we will continue our efforts to strengthen our internal and external audit mechanisms as per the safeguards recommendations.

E. Improving the Quality of Statistics

29. A new statistics law, modernizing and regulating data collection, was enacted in April 2018. This law was prepared with technical assistance from the UNDP, and application decrees are being finalized to: (i) spell out organizational arrangements, including the institutional status of INSTAT (National Institute of Statistics); (ii) strengthen coordination among ministries, including the establishment of the National Council of Statistics; (iii) improve information and data flows; and (iv) set up a statistics development fund.

30. While data provision is broadly adequate for program monitoring, we are taking measures to address shortcomings in the areas of real sector, monetary and financial sector, balance of payments, and government finances statistics:

- On the real sector, revised series of annual national accounts for the 2007-2017 period with the base year 2007 based on SNA 1993 methodology were finalized and published. INSTAT also produced experimental quarterly GDP estimates under the new base year. The government is in the process of switching to use the rebased GDP series, which will be the case for the preparation of the 2020 budget. As of May 2019, INSTAT is producing a reweighted consumer price index (CPI) to better account for current consumption patterns.
- Regarding monetary and financial statistics, we achieved in 2018 the consolidation of balance sheets of larger micro-financial institutions and the CEM in the preparation of the monetary survey.
- We are implementing recommendations of IMF TA on balance of payments and international investment position (IIP) statistics. We are emphasizing the enhancement of information collection (including through more data-sharing across government), have assessed the foreign direct investment survey and have launched surveys to collect data on financial transactions and on international transport and tourism, insurance, and manufacturing services. We have compiled a preliminary version of the IIP and have started connecting some of the balance of payments data deficiencies identified by the mission. Moreover, a preliminary study on the repatriation of export revenues is due to be completed at the end of November 2019.
- On government finance statistics, we have published budget execution statistics for 2017 and 2018 under the 2014 GFSM. We plan to gradually extend the statistical coverage from the central government to the general government, including local authorities and national public establishments (EPNs).

31. A general census of the population and housing, the third since independence, is being finalized. The last census was completed in 1993. Data have been collected and are currently being processed. Preliminary results were published in August 2019.

32. We remain committed to allocate sufficient human, financial, and material resources to the production of statistics. The government will continue to support INSTAT in fulfilling its missions, in particular the production of national accounts, consumer price index, and production price index. We are working to fill vacancies for BOP compilation. We also count on increasing technical and financial assistance from our partners, including for forecasting using the rebased national accounts.

CONTINUING ENGAGEMENT WITH THE FUND

33. The government expressed its desire to start discussions on a successor arrangement after the completion of the last review of the current arrangement. We remain committed to preserving macroeconomic stability while pursuing economic and financial policies consistent with our development objectives. We are convinced that continued financial and technical support from the IMF will continue to support these objectives, including by helping catalyze private investment and financial support of donors. Discussions on the modalities of a successor arrangement could start as soon as the latest review of the current ECF-arrangement is completed.

Attachment II. Technical Memorandum of Understanding

1. This technical memorandum of understanding (TMU) contains definitions and adjuster mechanisms that clarify the measurement of quantitative performance criteria and indicative targets in Tables 1 and 2, which are attached to the Memorandum of Economic and Financial Policies for 2019. 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.

DEFINITIONS

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

3. Government is defined for the purposes of this TMU to comprise the scope of operations of the treasury shown in the *opérations globales du Trésor* (or OGT). The government does not include the operations of state-owned enterprises and sub-national authorities.

4. The program exchange rates for the purposes of this TMU[1] are as follows:

Program Exchange Rates	
Malagasy Ariary (MGA)/SDR	4,443.86
U.S. Dollar/SDR	1.389049
Euro/SDR	1.270538
Australian dollar/SDR	1.903723
Canadian dollar/SDR	1.926401
Japanese Yen/SDR	167.377024
Swiss Franc	1.375855
U.K. Pound Sterling/SDR	0.937470

5. Foreign currency accounts denominated in currencies other than the SDR will first be valued in SDRs and then be converted to MGA. Amounts in other currencies than those reported in the table above and monetary gold will first be valued in SDRs at the exchange rates and gold prices that prevailed on December 31, 2015, and then be converted to MGA.

6. Performance criteria included in the program, as defined below, refer to the net foreign assets and net domestic assets of the central bank, external payments arrears, non-concessional new external debt owed or guaranteed by the central government and/or the central bank, and the domestic primary balance (commitment basis). Performance criteria are set for end-December 2018 and end-June 2019, while indicative targets are set for end-March 2019.

7. Total government revenue is comprised of tax and nontax budget revenue (as defined under Chapter 5 of GFSM 2001) and grants. Revenue is recorded in the accounting system on a cash basis. Taxes on the import of petroleum products, paid through the issuance of promissory notes, are

[1] Data refer to the mid-point reference exchange rates published on the CBM's webpage for December 30, 2015.

recorded under revenue at the time of the issuance of the promissory notes: to reconcile the difference in timing between the issuance of the promissory note and its actual payment to the Treasury, an equivalent amount is recorded (negatively) under the line "other net transactions of the Treasury" until the actual payment.

8. The authorities will give prior notification to World Bank and IMF staff of any single source procurement contracts for JIRAMA's purchases of fuel and electricity and purchases and rentals of generators. Prior notification entails that World Bank and IMF staff will receive written communication at least 3 working days before the signing of the contract. The signing of addendums and extensions of previously signed contracts are also subject to the requirement of prior notification.

PROVISION OF DATA TO THE FUND

9. The following information will be provided to the IMF staff for the purpose of monitoring the program (see Table 1 for details):

- Data with respect to all variables subject to quantitative performance criteria and indicative targets will be provided to Fund staff monthly with a lag of no more than four weeks for data on net foreign assets (NFA) and net domestic assets (NDA) of the Central Bank of Madagascar (CBM) and eight weeks for other data. The authorities will promptly transmit any data revisions to the Fund.
- The Financial Intelligence Unit (SAMIFIN) will continue to publish, on a website that is freely available to the public, quarterly data (no later than the end of the month following the quarter) on reports sent to BIANCO in relation to suspicions of laundering of the proceeds of corruption (Table 2).
- The BIANCO will publish on a website, that is freely available to the public, quarterly data (no later than at the end of the month following the quarter) on the number of persons indicted, the number of persons convicted by a first instance court decision, the number of persons convicted pursuant a final court decision, and the number of verifications of assets disclosures of public officials (Tables 3-6).
- For variables assessing performance against program objectives but which are not specifically defined in this memorandum, the authorities will consult with Fund staff as needed on the appropriate way of measuring and reporting.

QUANTITATIVE PERFORMANCE CRITERIA

A. Fiscal Aggregates

Floor on Primary Balance (commitment basis)

10. The domestic primary balance (commitment basis) is measured as follows:

- Domestic tax and non-tax revenue less domestically-financed capital expenditures and current spending excluding interest payments.
- For the purposes of calculating the primary balance, tax revenues are measured on a net basis, i.e., net of the refund of VAT credits. Current spending excluding interest payments is the sum of expenditures on wages and salaries, goods and services, transfers and subsidies, and treasury operations (net) excluding the refund of VAT credits. The primary balance will be calculated cumulatively from the beginning of the calendar year. For reference, using data at end-December 2017, the value of the primary balance would be as follows:

Primary Balance Excluding Foreign Financed Investment and Grants (commitment basis)	**-362**
Domestic tax revenue (net of VAT refunds)	4,118
Domestic non-tax revenue	122
Less:	
Domestically-financed capital expenditures	700
Current expenditures	3,902
Wages and salaries	2,076
Goods and services	282
Transfers and subsidies	1,467
Treasury operations (net of VAT refunds)	77

B. External Debt

Ceiling on Accumulation of New External Payment Arrears

11. These arrears consist of overdue debt-service obligations (i.e., payments of principal and interest) related to loans contracted or guaranteed by the government or CBM. Debt service obligations (including unpaid penalties and interest charges) are considered overdue if they have not been paid 30 days after the due date or after the end of a grace period agreed with, or unilaterally granted by, each creditor before the due date. They exclude arrears resulting from nonpayment of debt service for which the creditor has accepted in writing to negotiate alternative payment schedules, as well as debt service payments in conformity with contractual obligations that fail to materialize on time for reasons beyond the control of the Malagasy authorities. This monitoring target should be observed on a continuous basis from end-May 2016.

Ceilings on New External Debt

12. For program monitoring purposes, a debt is concessional if it includes a grant element of at least 35 percent, calculated as follows; the grant element of a debt is the difference between the nominal value of debt and its present value (PV), expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rate used for this purpose is 5 percent. Debt is considered as semi-concessional if it includes a grant element of at least 20 percent, calculated as described above.

13. Where an external loan agreement contains multiple disbursements and where the interest rate for individual disbursement are linked to the evolution of a reference rate since the date of signature, the interest rate at the time of signature will apply for the calculation of the PV and grant element for all disbursements under the agreement.

14. For program monitoring purposes, the definition of debt is set out in *Point 8, Guidelines on Public Debt Conditionality in Fund Arrangements, Executive Board Decision No. 15688-(14/107), adopted December 5, 2014* (see Annex 1). External debt is defined by the residency of the creditor.

15. For loans carrying a variable interest rate in the form of a benchmark interest rate plus a fixed spread, the PV of the loan would be calculated using a program reference rate plus the fixed spread (in basis points) specified in the loan contract. The program reference rate for the six-month USD LIBOR is 3.37 percent and will remain fixed for the duration of the program. The spread of six-month Euro LIBOR or 3-month Euribor over six-month USD LIBOR is -249 basis points. The spread of six-month JPY LIBOR over six-month USD LIBOR is -286 basis points. The spread of six-month GBP LIBOR over six-month USD LIBOR is -108 basis points. For interest rates on currencies other than Euro, JPY, and GDP, the spread over six-month USD LIBOR is -209 basis points.[2] Where the variable rate is linked to a different benchmark interest rate, a spread reflecting the difference between the benchmark rate and the six-month USD LIBOR (rounded to the nearest 50 bps) will be added.

16. A performance criterion (ceiling) applies to the PV of new external debt, contracted or guaranteed by the government or CBM. The ceiling applies to debt contracted or guaranteed for which value has not yet been received, including private debt for which official guarantees have been extended. The PV and associated grant element (GE) are determined using the Fund's concessionality calculator or excel template available online. These monitoring targets should be calculated from January 1, 2018 and observed on a continuous basis from completion of the third review under the ECF arrangement. The ceiling is subject to an adjustor defined below.

17. Two continuous ceilings (see paragraph 24) apply to new non-concessional external debt with nonresidents with original maturities of more than one year contracted or guaranteed by the government or CBM. The ceilings apply to debt and commitments contracted or guaranteed for

[2] The program reference rate and spreads are based on the "average projected rate" for the six-month USD LIBOR over the following 10 years from the Fall 2015 World Economic Outlook (WEO).

which value has not yet been received. They apply to private debt for which official guarantees have been extended and which, therefore, constitutes a contingent liability of the government or CBM. The first ceiling concerns new non-concessional external debt with nonresidents with original maturities of more than one year contracted by the government or CBM with a grant element of less than 35 percent and the second ceiling concerns new non-concessional external debt with nonresidents with original maturities of more than one year contracted by the government or the CBM with a grant element of less than 20 percent. These monitoring targets should be calculated and observed on a continuous basis from January 1, 2016 until the completion of the third review under the ECF arrangement.

18. Excluded from the ceilings in paragraphs 15 and 16 are (i) the use of IMF resources; (ii) debts incurred to restructure, refinance, or prepay existing debts, to the extent that such debt is incurred on more favorable terms than the existing debt and up to the amount of the actually restructured/refinanced/prepaid debt (this also applies to liabilities of Air Madagascar assumed by the government in the context of a strategic partnership agreement); and (iii) debts classified as international reserve liabilities of CBM.

19. A continuous ceiling applies to new non-concessional external debt with nonresidents with original maturities of up to and including one year contracted or guaranteed by the government or CBM. The ceiling applies to debt and commitments contracted or guaranteed for which value has not yet been received. It applies to private debt for which official guarantees have been extended and which, therefore, constitutes a contingent liability of the government or CBM. This monitoring target should be calculated and observed on a continuous basis from end-May 2016 until the completion of the third review under the ECF arrangement. See paragraph 24.

20. Excluded from the ceiling are (i) concessional debts; (ii) debts incurred to restructure, refinance, or prepay existing debts, to the extent that such debt is incurred on more favorable terms than the existing debt and up to the amount of the actually restructured/refinanced/ prepaid debt (this also applies to liabilities of Air Madagascar assumed by the government in the context of a strategic partnership agreement); (iii) debts classified as international reserve liabilities of CBM; and (iv) normal import financing. A financing arrangement for imports is considered to be "normal" when the credit is self-liquidating.

C. Monetary Aggregates

Floor on Net Foreign Assets of the Central Bank of Madagascar

21. The target floor for NFA of the CBM is evaluated using the end-period stock, calculated using program exchange rates. The NFA of CBM is defined as the difference between CBM's gross foreign assets and total foreign liabilities, including debt owed to the IMF. All foreign assets and foreign liabilities are converted to SDRs at the program exchange rates, as described in paragraph 4. For reference, at end-December 2017, NFA was SDR 782 million, calculated as follows:

Foreign Assets	
MGA billions, end-2017 exchange rates (A)	4,988.039
SDR millions, end-2017 exchange rates (B)	1,086.925
SDR millions, program exchange rates (C)	1,099.836
Foreign Liabilities	
MGA billions, end-2017 exchange rates (D)	1,458.186
SDR millions, end-2017 exchange rates (E)	317.748
Net Foreign Assets	
SDR millions, program exchange rates (F) = (C) – (E)	782.088

Ceiling on Net Domestic Assets of the Central Bank of Madagascar

22. The target ceiling on NDA of the CBM is evaluated using the end-period stock, calculated at program exchange rates. The NDA of CBM are defined as the difference between reserve money and the NFA of the CBM valued in MGA using the program exchange rates as described in paragraphs 4. It includes net credit to the government, credit to the economy, claims on banks, liabilities to banks (including the proceeds of CBM deposit auctions—*appels d'offres négatifs,* and open market operations), and other items (net). For reference, at end-December 2017, NDA at program exchange rates was MGA 1,083 billion, calculated as follows:

Net Foreign Assets	
SDR millions, program exchange rates (A)	782.088
MGA billions, program exchange rates (B)	3,475.489
Base Money	
MGA billions, end-2017 exchange rates (C)	4,558.154
Net Domestic Assets	
MGA billions, program exchange rates (D) = (C) – (B)	1,082.665

INDICATIVE TARGETS

D. Floor on Priority Social Spending

23. Priority social spending includes domestic spending primarily related to interventions in nutrition, education, health, and the provision of social safety nets. The floor on priority social spending by the central government will be calculated cumulatively from the beginning of the calendar year. The floor is set as the sum of the budget allocations in the *Loi de Finance* to the Ministries of Health, Education, Population and Water, excluding salaries and externally financed investment.

E. Floor on Gross Tax Revenue

24. Government tax revenue is measured on a gross basis, that is, before the refund of VAT credits. It comprises all domestic taxes and taxes on foreign trade received by the central government treasury. Tax revenue excludes: (1) the receipts from the local sale of in-kind grants, (2) any gross inflows to the government on account of signature bonus receipts from the auction of hydrocarbon and mining exploration rights, and (3) tax arrears recorded in the context of regularization operations, such as those related to the recapitalization of Air Madagascar in 2016. 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 and Budget. The floor on gross tax revenue will be calculated cumulatively from the beginning of the calendar year. For reference, for the year ending December 2017, gross government tax revenue was MGA 4,329 billion, comprised of net tax revenue of MGA 4,118 billion and VAT refunds of MGA 211 billion.

F. Ceilings on New Non-Concessional External Debt

25. From the completion of the third review under the ECF arrangement onwards, the ceilings for non-concessional debt with maturities of more than one year (paragraph 16; cumulative since January 1, 2016) and of less than one year (paragraph 18; cumulative since end-May 2016) serve as indicative targets.

STRUCTURAL BENCHMARKS

26. For the purposes of the structural benchmark on fuel pricing, avoiding budget costs from fuel pricing is defined and monitored as follows:

- Until the adoption and implementation of an automatic fuel pricing mechanism with a smoothing formula no later than end-September 2019, the authorities will set prices in a manner that prevents total estimated net liabilities to fuel distributors from rising above MGA 175 billion (measured as a cumulative stock) and aims to reduce the level gradually. The estimated total net liabilities to fuel distributors include the existing stock at end-December 2018 (MGA 132.1 billion as reference) and any new liabilities generated by a difference between the reference prices and the pump prices. The estimated total net liabilities to fuel distributors will be calculated by the Malagasy Office for Hydrocarbons (OMH), using the fuel price structure in place as of end-December 2018 or a new fuel price structure established in accordance with prevailing laws and regulations.

- No later than end-September 2019, the authorities will implement an automatic fuel pricing mechanism with a smoothing formula, based on the fuel price structure in place in June 2019. In agreement with the fuel distributors, this automatic pricing mechanism will be combined with possible discretionary adjustments (for social stability reasons), limited as follows: (i) the discretionary adjustments cannot be applied to reduce pump prices (but can be applied to limit price increases or decreases given by the formula); and (ii) the additional cumulative liabilities to fuel distributors linked to these discretionary adjustments will not exceed MGA 50 billion.

- Avoiding budget cost from fuel pricing includes: (i) the estimated total net liabilities to fuel distributors (defined above), including new liabilities from both automatic adjustments associated with a smoothing formula and those generated by discretionary adjustments to the fuel price, is at most MGA 140 billion (i.e. the government has a liability to the distributors of at most MGA 140 billion) by end-2019; (ii) the difference between average pump prices and average reference prices is eliminated for each of the products: super gasoline, kerosene, and diesel by end-August 2019; and (iii) the remaining stock of net liabilities to fuel distributors at-end 2019 (maximum of MGA 140 billion) will be settled by end-2020 at the latest through a price surcharge and, consequently, no transfers will be due to be paid by the government budget to the fuel distributors.

- The authorities will provide to IMF staff the calculations for the estimate of the monthly flow and stock for these net liabilities for each month, as well as the minutes of the agreement with the fuel distributors, by the 14th day of that month.

MEMORANDUM ITEMS

27. Official external program support is defined as grants and loans, including 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 the private sector and incorporated into the budget. Official external support does not include grants and loans earmarked to investment projects. Official external program support is calculated as a cumulative flow from January 1, 2016.

28. Official external program grants are defined as grants, including 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. Official external program grant support does not include grants earmarked to investment projects. Official external program grants calculated as a cumulative flow from the beginning of the calendar year.

29. New concessional external debt contracted or guaranteed with original maturity of more than one year by the central government or the CBM measures such debt with a grant element of at least 35 percent.

USE OF ADJUSTERS

30. The performance criteria on net foreign assets of the CBM and net domestic assets of the CBM will be adjusted in line with deviations from amounts projected in the program for official external program support. These deviations will be calculated cumulatively from January 1, 2016. The following is an explanation of these adjustments:

- The floor on NFA will be adjusted *downward (upward)* by the cumulative deviation downward (upward) of actual from projected budget support (official external program support). This adjustment will be capped at the equivalent of SDR75 million, evaluated at program exchange rates as described in paragraph 4.

- The ceiling on NDA will be adjusted *upward (downward)* by the cumulative deviation downward (upward) of actual from projected budget support (official external program support). This adjustment will be capped at the equivalent of SDR75 million, evaluated at program exchange rates as described in paragraph 4.

31. The performance criteria on the primary balance will be adjusted in line with deviations from amounts projected in the program for official external program grants. These deviations will be calculated cumulatively from the beginning of each calendar year. The following is an explanation of these adjustments:

- The floor on the primary balance excluding foreign-financed investment and grants (commitment basis) will be adjusted downward by the cumulative upward deviation of actual from projected official external program support (grants or loans on concessional terms), calculated at quarterly period-average actual exchange rates as described in paragraph 4.

32. An adjustor of up to 5 percent of the external debt ceiling set in PV terms applies in case deviations are prompted by a change in the financing terms. Changes in interest rates, maturity, grace period, payment schedule, commissions, fees of a debt or debts are candidates for the adjuster. The adjustor cannot be applied when deviations are prompted by an increase in the nominal amount of total debt contracted or guaranteed and are subject to debt sustainability.

Table 1. Madagascar: Data Reporting Requirements

Item	**Periodicity**
Exchange rate data	
Central Bank of Madagascar (CBM)	
Total daily CBM gross purchases of foreign exchange – break down by currency purchased	Daily, next working day
The weighted average exchange rate of CBM gross purchases, the highest traded exchange rate, and the lowest traded exchange rate –break down by currency purchased	Daily, next working day
Total daily CBM gross sales of foreign exchange – break down by currency purchased	Daily, next working day
The weighted average exchange rate of CBM gross sales, the highest traded exchange rate, and the lowest traded exchange rate – break down by currency purchased	Daily, next working day
Total CBM net purchases/sales of foreign exchange - break down by currency purchased	Daily, next working day
Total interbank foreign exchange transactions (net of CBM transactions) - break down by currency purchased	Daily, next working day
Total interbank and retail foreign exchange transactions (net of CBM transactions) - break down by currency purchased	Daily, next working day
Monetary, interest rate, and financial data	
Central Bank of Madagascar (CBM)	
Foreign exchange cash flow, including foreign debt operations	Monthly
Stock of gross international reserves (GIR) and net foreign assets (NFA), both at program and market exchange rates	Monthly
Detailed data on the composition of gross international reserves (GIR), including currency composition	Monthly
Market results of Treasury bill auctions, including the bid level, bids accepted or rejected, and interest rates	Monthly
Stock of outstanding Treasury bills	Monthly
Data on the secondary market for Treasury bills and other government securities	Monthly
Bank-by-bank data on excess/shortfall of required reserves	Monthly
Money market operations and rates	Monthly
Bank lending by economic sector and term	Monthly
Balance sheet of CBM	Monthly, within two weeks of the end of each month
Balance sheet (aggregate of deposit money banks	Monthly, within six weeks of the end of each month
Monetary survey	Monthly, within six weeks of the end of each month
Financial soundness indicators of deposit money banks	Quarterly, within eight weeks of the end of the quarter

Table 1. Madagascar: Data Reporting Requirements (continued)

Item	**Periodicity**
Fiscal data	
Ministry of Finance and Budget (MFB)	
Preliminary revenue collections (customs and internal revenue)	Monthly, within three weeks of the end of each month
Treasury operations (OGT)	Monthly, within eight weeks of the end of each month
Stock of domestic arrears, including arrears on expenditure and VAT refunds	Monthly, within eight weeks of the end of each month
Priority social spending as defined by the indicative target	Monthly, within eight weeks of the end of each month
Subsidies to JIRAMA's suppliers	Monthly, within eight weeks of the end of each month
State-owned enterprise data	
Data summarizing the operational and financial position of JIRAMA	Monthly, within four weeks of the end of each month, for operational and financial data. Quarterly, by the end of the following month, for the Table on "Total impayés fournisseurs"
Data summarizing the financial position of AIR MADAGASCAR	Quarterly, by the end of the subsequent quarter.
Debt data	
Ministry of Finance and Budget (MFB)	
Public and publicly-guaranteed debt stock at end of month, including: (i) by creditor (official, commercial domestic, commercial external); (ii) by instrument (Treasury bills, other domestic loans, external official loans, external commercial loans, guarantees); and (iii) in case of new guarantees, the name of the guaranteed individual/institution.	Monthly, within four weeks of the end of each month
External public or publicly guaranteed loans signed since January 1, 2016, specifying the nominal value; calculated grant element and PV; and terms, including the interest rate (using the program reference rate for variable rate loans), maturity, commissions/fees, grace period, repayment profile, and grant component.	Quarterly
External data	
Central Bank of Madagascar (CBM)	
Balance of payments	Quarterly, by the end of the subsequent quarter

Table 1. Madagascar: Data Reporting Requirements (concluded)	
Real sector and price data	
INSTAT	
Consumer price index data (provided by INSTAT)	Monthly, within four weeks of the end of each month
Details on tourism	Monthly, within twelve weeks of the end of each month
Electricity and water production and consumption	Monthly, within twelve weeks of the end of each month
Other data	
OMH	
Petroleum shipments and consumption	Monthly, within four weeks of the end of each month

Table 2. Madagascar: Reports sent by SAMIFIN to BIANCO

Reports disseminated	Members of the Executive Power	Members of the Legislative Power	Members of the Judicial Power	Heads of province and district, Commissaries, Prefects, Mayors	SOE Managers	Others
Aggregated value of suspected money laundering						

Table 3. Madagascar: Number of Persons Indicted						
Penal Code Article	President Members of Parliament High Constitutional Court Magistrates	Magistrates	Heads of province and district, Commissaries, Prefects, Mayors	Director of Ministry or equivalent	SOE Managers	Others
Art. 174						
Art. 174.1						
Art. 174.2						
Art. 174.3						
Art. 175						
Art. 175.1						
Art. 175.2						
Art. 176						
Art. 177						
Art. 177.1						
Art. 177.2						
Art. 178						
Art. 179						
Art. 179.1						
Art. 180						
Art. 180.1						
Art 180.2						
Art. 181						
Art. 182						
Art. 183						
Art. 183.1						
Art. 183.2						

Table 4. Madagascar: Number of Persons Convicted—First Instance

Penal Code Article	President Members of Parliament High Constitutional Court Magistrates		Magistrates		Heads of province and district, Commissaries, Prefects, Mayors		Director of Ministry or equivalent		SOE Managers		Others	
	Fine	Jail	Fine	Jail	Fine	Jail	Fine	Jail	Fine	Jail	Fine	Jail
Art. 174												
Art. 174.1												
Art. 174.2												
Art. 174.3												
Art. 175												
Art. 175.1												
Art. 175.2												
Art. 176												
Art. 177												
Art. 177.1												
Art. 177.2												
Art. 178												
Art. 179												
Art. 179.1												
Art. 180												
Art. 180.1												
Art 180.2												
Art. 181												
Art. 182												
Art. 183												
Art. 183.1												
Art. 183.2												

For fines, total value in ariary. For jail, total months (and suspended jail).

Table 5. Madagascar: Number of Persons Convicted—Final Decision

Penal Code Article	President Members of Parliament High Constitutional Court Magistrates		Magistrates		Heads of province and district, Commissaries, Prefects, Mayors		Director of Ministry or equivalent		SOE Managers		Others	
	Fine	Jail	Fine	Jail	Fine	Jail	Fine	Jail	Fine	Jail	Fine	Jail
Art. 174												
Art. 174.1												
Art. 174.2												
Art. 174.3												
Art. 175												
Art. 175.1												
Art. 175.2												
Art. 176												
Art. 177												
Art. 177.1												
Art. 177.2												
Art. 178												
Art. 179												
Art. 179.1												
Art. 180												
Art. 180.1												
Art 180.2												
Art. 181												
Art. 182												
Art. 183												
Art. 183.1												
Art. 183.2												

For fines, total value in ariary. For jail, total months (and suspended jail).

Table 6. Madagascar: Verification of Asset Disclosure Forms				
	Forms received	Forms verified	Cases submitted for investigation for non-declaration	Cases submitted for investigation for inconsistencies in the declaration
President Members of Parliament High Constitutional Court Magistrates				
Magistrates				
Heads of province and district, Commissaries, Prefects, Mayors				
Director of Ministry or equivalent				
SOE Managers				
Others				

Annex I. Guidelines on Performance Criteria with Respect to External Debt

Excerpt from paragraph 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), adopted December 5, 2014.

1. (a) For the purpose of these guidelines, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and

iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of these guidelines, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(b) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MADAGASCAR

January 9, 2020

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION AND SIXTH REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT—DEBT SUSTAINABILITY ANALYSIS

Approved By
David Owen and Zuzana Murgasova (IMF) and Marcello Estevão (IDA)

Prepared by the staffs of the International Monetary Fund (IMF) and the International Development Association (IDA)[1]

Madagascar: Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	***Low***
Overall risk of debt distress	***Moderate***
Granularity in the risk rating	***n/a***
Application of judgment	***No***

Madagascar, classified as having a medium level of debt carrying capacity, is assessed at low risk of external debt distress, in line with the July 2019 DSA.[2] Under the baseline, external public and publicly guaranteed (PPG) debt is well below applicable thresholds and stress tests do not breach the thresholds. Overall (external plus domestic) risk of debt distress remains moderate, consistent with the July 2019 DSA. Total public debt is below the benchmark under the baseline, but a growth shock drives the present value of debt to GDP above the benchmark at the end of the projection period and it is on a persistent upward trajectory. Moreover, shocks could introduce liquidity problems, as the debt-service to revenue ratio could exceed 75 percent over the long term under the growth shock. These assessments continue to be supportive of Madagascar's plans to scale up its borrowing to meet its investment needs; however, several factors—a faster execution of the government's ambitious medium-term borrowing, poorly selected public investment projects, and less favorable financing terms—may lead to a faster than expected deterioration in external and public debt indicators.

[1] Prepared by the IMF and the World Bank. This DSA follows the Guidance Note of the Join Bank-Fund Debt Sustainability Framework for Low Income Countries, February 2018. This new framework builds on the 2019 framework used for the previous Madagascar DSA, which was published in July 2019 (IMF Country Report No. 19/262).

[2] Madagascar has a Composite Indicator score of 2.82 and is classed as having medium debt-carrying capacity.

PUBLIC DEBT COVERAGE

1. **This DSA includes debt coverage of public and publicly guaranteed external and domestic debt, including State-owned Enterprises' domestic debt as well as central bank external liabilities (Text Table 1).** This is in line with coverage under the July 2019 DSA (Text Table 1). PPG debt includes all external liabilities held by the central bank, including all borrowing from the IMF; debts owed by state-owned enterprises (SOEs) in cases where the government has at least 50 percent of the shares; and direct guarantees provided by the central government. Borrowing by local governments requires the authorization from the Ministry of Finance and no request of such authorization has been submitted to date. The measure of debt is on a gross basis and the currency criterion is used to distinguish between domestic and external debt.[3]

Text Table 1. Madagascar: Public Debt Coverage Under the Baseline Scenario

	Subsectors of the public sector	Sub-sectors covered
1	Central government	X
2	State and local government	X
3	Other elements in the general government	
4	o/w: Social security fund	
5	o/w: Extra budgetary funds (EBFs)	
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	X

Text Table 2. Madagascar: Coverage of the Contingent Liabilities' Stress Test

1	**The country's coverage of public debt**	The central, state, and local governments, central bank, government-guaranteed debt, non-guaranteed S			
		Default		**Used for the analysis**	**Reasons for deviations from the default settings**
2	Other elements of the general government not captured in 1.	0	percent of GDP	0.0	
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2	percent of GDP	2.0	Captures potential additional contingent liabilities not captured in the available data from SOEs.
4	PPP	35	percent of PPP stock	0.0	Exposures through PPPs are set to zero since, as per the World Bank's PPP database, PPPs comprise less than ½ percent of GDP.
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5	percent of GDP	5.0	
	Total (2+3+4+5) (in percent of GDP)			7.0	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

2. **The coverage assumed for contingent liabilities is a shock of 7 percent of GDP.** This reflects the default setting for SOEs, PPPs, and financial markets (Text Table 2).

- Following guidance, we include estimated debt for SOEs in which the government has a majority stake in the baseline; this debt is exclusively domestic. However, government recognition of some other SOE liabilities could require external financing. Other potential contingencies include future recapitalization of the postal savings scheme and the Madagascar Savings Fund (*Caisse d'Epargne de Madagascar, CEM*), which would likely amount to less than 1 percent of GDP.

[3] Locally-issued debt denominated in local currency held by non-residents and/or locally-issued debt denominated in foreign currency held by residents is likely insignificant. Owing to limitations in available data, the results would likely be the same if selecting the residency criterion.

- Exposures to PPPs are set to zero since, as per the World Bank's PPP database, PPPs comprise less than ½ percent of GDP. The authorities plan to develop more PPPs in future and the potential vulnerabilities associated with such PPPs could increase rapidly.

- The default value of 5 percent is programmed for financial markets. Most banks are financially solid with deposits exceeding loans and majority foreign shareholders. Dollarization of deposits and credits is not pronounced, and banks' foreign assets generally exceed their foreign liabilities.

BACKGROUND

A. Recent Debt Revisions and Developments

3. **Madagascar's historical debt to GDP ratios have fallen due to a rebasing of GDP.** In close coordination with Fund staff and through technical assistance, the authorities have rebased their GDP, leading to upward revisions of about 16 percent on average. The revision, relatively minor compared to other countries' rebasing experiences, resulted in a drop in Madagascar's debt ratios. For instance, 2018's debt/GDP ratio now stands at 40 percent instead of 46 percent (see Text Table 3).

Text Table 3. Madagascar: Total PPG Debt/GDP Revisions (2015-18)

(Percent of GDP)	2015	2016	2017	2018
Old GDP	**48.4**	**47.1**	**46.0**	**45.7**
New GDP	**43.4**	**40.3**	**40.0**	**39.9**

4. **The 2019 PPG debt ratio will reach 40.1 percent, rising by less than 1 percent of GDP relative to 2018.** The debt ratio increased from 39.9 percent in 2018 to 40.1 percent in 2019, owing to a primary deficit and lower than initially forecasted nominal GDP growth (mainly due to lower vanilla and cobalt prices and under-execution of capital investment). The ratio of domestic debt fell slightly with external PPG debt rising by slightly less than ½ a percent of GDP (Text Table 4). The level of 2019 PPG debt is lower than previously forecast for the July 2019 DSA, reaching $5,572 million instead of $5,649 million.[4]

5. **External sources continue to account for two-thirds of PPG debt** (Text Table 4). The contribution of external debt continues to rise following Madagascar's re-engagement with the international community. At end-2019, roughly two-thirds of external debt is owed to multilateral creditors, in particular to the World Bank and African Development Bank, on highly concessional terms, including long maturities. Non-Paris club creditors account for 5.9 percent of PPG debt, which is a lower share than at the start of the program. Domestic debt increased slightly in absolute terms in 2019 but fell as a percent of GDP. Government securities are the largest category, followed by estimated debts of SOEs in which the government has a majority stake. JIRAMA accounts for the majority of SOE debt and reflects arrears to suppliers, not contracted loans. Projections of SOE debts assume they will remain at a level consistent with their current share of GDP (~4.5 percent) through the full projection period. There are current efforts to

[4] If the July 2019 forecast for total PPG debt had materialized, this would have amounted to 40.6 percent of GDP using current estimates of 2019 GDP.

restructure and reduce in the near-term. By including these projected SOE debts in our baseline, we are adopting a particularly conservative approach for the DSA.

Text Table 4. Madagascar: Breakdown of Total PPG Debt (2015-19)

Creditor	2015	2016	2017	2018	2019 (Est)
			Amount (US$m)		
Domestic debt, *of which:*	**1,689**	**1,682**	**1,827**	**1,763**	**1,784**
Securities inc. BTA, BTF, BTS[1]	370	526	719	726	833
Debt to the Central Bank	386	337	297	272	282
Arrears	346	210	146	71	42
Other inc. SOE debt	587	610	665	693	628
External debt, *of which:*	**2,816**	**2,845**	**3,262**	**3,549**	**3,788**
Multilateral	2,006	2,052	2,276	2,368	2,493
Paris Club	146	137	165	189	219
Non-Paris Club	356	324	290	308	329
Commercial & Guaranteed	25	23	83	204	192
External debt of the Central Bank	282	310	449	480	556
Total PPG debt	**4,505**	**4,528**	**5,089**	**5,312**	**5,572**
			Percent of GDP		
Domestic debt, *of which:*	**16.3**	**15.0**	**14.4**	**13.2**	**12.8**
Securities inc. BTA, BTF, BTS	3.6	4.7	5.7	5.5	6.0
Debt to the Central Bank	3.7	3.0	2.3	2.0	2.0
Arrears	3.3	1.9	1.2	0.5	0.3
Other inc. SOE debt	5.7	5.4	5.2	5.2	4.5
External debt, *of which:*	**27.1**	**25.3**	**25.7**	**26.7**	**27.2**
Multilateral	19.3	18.3	17.9	17.8	17.9
Paris Club	1.4	1.2	1.3	1.4	1.6
Non-Paris Club	3.4	2.9	2.3	2.3	2.4
Commercial & Guaranteed	0.2	0.2	0.7	1.5	1.4
External debt of the Central Bank	2.7	2.8	3.5	3.6	4.0
Total PPG debt	**43.4**	**40.3**	**40.0**	**39.9**	**40.1**
			Percent of total		
Domestic debt, *of which:*	**37.5**	**37.2**	**35.9**	**33.2**	**32.0**
Securities inc. BTA, BTF, BTS	8.2	11.6	14.1	13.7	14.9
Debt to the Central Bank	8.6	7.4	5.8	5.1	5.1
Arrears	7.7	4.6	2.9	1.3	0.7
Other inc. SOE debt	13.0	13.5	13.1	13.0	11.3
External debt, *of which:*	**62.5**	**62.8**	**64.1**	**66.8**	**68.0**
Multilateral	44.5	45.3	44.7	44.6	44.7
Paris Club	3.3	3.0	3.2	3.6	3.9
Non-Paris Club	7.9	7.1	5.7	5.8	5.9
Commercial & Guaranteed	0.5	0.5	1.6	3.8	3.4
External debt of the Central Bank	6.3	6.8	8.8	9.0	10.0
Total PPG debt	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Sources: Malagasy authorities; and staff estimates.

[1]BTA are Treasury bills with less than one year maturity; BTF and BTS are Treasury bonds with maturity ranging from 1 to 3 years.

B. Macroeconomic Assumptions

6. DSA projections remain consistent with the authorities' plan to scale up much needed infrastructure investment, albeit from a lower base than assumed in the previous DSA due to ongoing under-execution.

- GDP growth projections for 2019 have been revised down from 5.2 to 4.8 reflecting a downward revision of 0.4 percentage points due to the rebasing and the net effect of several other factors.

These include under-execution of capital investment (especially in the first half of the year), a wait-and-see attitude by the private sector during the election cycle, a fall in vanilla prices, a reduction in clove export volumes associated with cyclical production factors, and positive developments in mining, textiles, and tourism. Relative to July 2019 DSA, government investment is expected to scale up over the medium-term, but from a lower base.[5] Meanwhile, private investment is still expected to remain stable through the medium-term, but off of a higher base. Growth is expected to peak over the medium-term at 5.6 percent in 2024, with some deceleration in growth thereafter. In 2029, growth is expected to hit 5.2 percent relative to the July 2019 projection of 4.6 percent.

- Inflation expectations are lower than earlier estimates for 2019 but are revised up beyond the medium-term.
- The non-interest current account deficit has been revised down over the short term behind under-execution of capital projects, despite a fall in vanilla prices from their peak. Over the next 5 years, vanilla prices are expected to fall by 30 percent, contributing to a decline in the current account balance together with an expected rise in capital spending that will boost construction-related imports (e.g., equipment and primary materials).
- We project lower primary deficits over the medium term, reaching 0.6 and 3.5 percent of GDP in 2019 and 2024, respectively, behind ongoing gains in revenue mobilization and PFM reforms (for more detail on these measures, see the AIV Staff Report).

Text Table 5. Madagascar: Baseline Macroeconomic Assumptions for DSA

	2019		2020		2024		2029	
(In percent of GDP, unless otherwise indicated)	5th Review	Current	5th Review	Current	5th Review	Current	5th Review	Current
Real GDP growth (percent)	5.2	4.8	5.3	5.2	4.8	5.6	4.6	5.2
Inflation, end of period (percent)	6.7	6.0	6.3	6.2	5.0	5.6	5.0	5.3
Non-interest CA deficit	1.3	-0.5	2.8	0.9	3.8	1.7	2.9	1.7
Primary deficit	1.3	0.6	3.5	1.9	4.5	3.5	2.4	2.8

Sources: Malagasy authorities, World Bank and IMF.

7. **Financing assumptions are broadly consistent with the 2019-21 and 2020-2022 debt strategy documents, as well as the July 2019 DSA**. For domestic financing, short-term local currency treasury bills will remain the main source of financing over the medium and longer-term. While medium-term local currency bond issuance is expected to scale up over time, this is off a low base (5 percent of the entire portfolio in the near-term) and reflects the shallow nature of Madagascar's financial market. We expect medium-term issuance to increase based on feedback from both the authorities and banking sector. However, there are currently no plans to issue long-term domestic securities. For external financing, the share of external to total debt will not exceed the upper limit of 85 percent; use of concessional loans will be maximized (over 90 percent of near-term external borrowing through 2022 is expected to be on concessional terms); and the portfolio of new external financing is expected to shift towards a more balanced distribution of concessional and non-concessional debt beyond the medium-term. As part of the

[5] The authorities recently released the Emergence Plan (PEM), which outlines ambitious increases in investment, revenues, and growth. However, the implementation details of this plan have yet to be fully developed and therefore our baseline assumptions do not reflect the PEM. For more details on the PEM, see the AIV and 6th Review Staff Report.

drafting for the Finance Act 2020, an external debt borrowing ceiling of $1,952 million is being included to ensure external debt levels remain sustainable. Broadly, the assumption is that Madagascar will continue to borrow over the long run for development but at a slower pace than the scaled-up pace envisaged for the medium-term. To be conservative, we exclude budget support that has not been finalized by donors from the baseline.

8. Realism tools suggest our assumptions are in line with reasonable bounds. Across a range of realism checks (see Figure 4) that include examining potential growth paths under various fiscal multipliers, the projected adjustment for the primary balance, and investment plans, our underlying assumptions appear to not raise any flags.

9. The favorable outlook remains subject to both domestic and external risks. Growth could be lower than forecast if under-execution of investment continues and unexpectedly large transfers to state-owned enterprises (e.g., JIRAMA) crowd out investment and social protection spending. Moreover, stalls in governance and corruption-related reforms place Madagascar at risk of a slow down or delay donor support plans, reducing private investment (including the development of PPPs), and related-structural reforms (e.g., fuel pricing). Turning to external risks, Madagascar remains highly vulnerable to terms-of-trade shocks and natural disasters, as well as a synchronized slowdown in global growth and trade.

C. Drivers of Debt Dynamics

10. Over the medium term, scaling up of foreign-financed public investment drives an increase in debt compared with the 5-year historical average (Figure 3). Relative to the period between 2013 to 2018, external and total public debt to GDP ratios are expected to rise faster (by an additional 0.6 and 0.2 percentage points, respectively) over the medium term, reflecting a gradual increase in borrowing costs and higher capital investments, accompanied by increasing deficits. A shift away from grant financing towards more concessional lending due to Madagascar's prior low external debt distress rating is also a contributing factor. Higher growth and an expected appreciation in the exchange rate help offset such factors. A residual that includes unrepatriated mining receipts and reserve accumulation remains broadly similar to recent history (and is of a similar magnitude under the July 2019 DSA).

11. Government capital spending has been revised downward, but average 5-year real growth is nonetheless expected to rise (see Figure 4). Relative to the July 2019 DSA, government investment as a share of GDP is expected be roughly 3 percentage points lower in 2019. From this lower base, it is expected to rise as public capital investments scale up from 5 percent to 9 percent of GDP over 2019-24. This downward revision reflects ongoing and expected under-execution of government-financed capital projects. Private investment is broadly in line with prior estimates for 2019 and is expected to increase from 14 to 16 percent of GDP between 2019 and 2024. The authorities are pivoting towards scaling up PPPs in energy and infrastructure (for more detail, see AIV Staff Report). Given Madagascar's large infrastructure needs, the conservative assumed baseline fiscal multiplier suggests a significant upside risk to growth. However, the current average for the projected contribution of public investment to real GDP growth over the next 5 years is expected to be slightly lower than suggested by the previous DSA, largely due to 2019's unexpectedly low outturn for public investment; the contribution of government capital to growth in 2021 and beyond is higher than in the previous DSA. Continued under execution of government-led capital projects may warrant further downward revisions to government investment rates.

D. Country Classification and Determination of Stress Test Scenarios

12. Madagascar's debt carrying capacity continues to be classified as medium. Based on a calculation of a composite indicator score based on factors such as the CPIA index, real growth rates, reserve coverage, remittances, and world growth, Madagascar continues to be rated as having medium debt-carrying capacity (Text Table 6). The 10 year-average values are based on an average over 2014-23, where latest macroeconomic data and projections are based on the October 2019 *World Economic Outlook*. Text Figure 1 highlights the differences in composite indicator cut-off values and the corresponding external debt burden thresholds and public debt benchmarks at different debt-carrying capacities.

Text Table 6. Madagascar: Calculation of Debt-Carrying Capacity

Components	Coefficients (A)	10-year average values (B)	Current: CI Score components (A*B) = (C)	Current: Contribution of components	July 2019: CI Score components	July 2019: Contribution of components	June 2018
CPIA 1/	0.385	3.246	1.25	44%	1.24	44%	1.22
Real growth rate (in percent)	2.719	4.540	0.12	4%	0.12	4%	
Import coverage of reserves (in percent)	4.052	34.431	1.40	50%	1.35	48%	
Import coverage of reserves^2 (in percent)	-3.990	11.855	-0.47	-17%	-0.44	-16%	
Remittances (in percent)	2.022	2.357	0.05	2%	0.05	2%	
World economic growth (in percent)	13.520	3.500	0.47	17%	0.48	17%	
CI Score 2/			2.82	100%	2.80	100%	
Debt Carrying Capacity			**Medium**		**Medium**		**Weak**

1/ The 10-year average scores for the current period are based on an average over 2014-2023.

2/ Composite Indicator Score Threshold for medium capacity is 2.69.

Text Figure 1. Composite Indicator Cut-off Values and Respective Debt Burden Thresholds & Benchmarks

Cut-off values			
Weak	CI <	2.69	
Medium	2.69	≤ CI ≤	3.05
Strong	CI >	3.05	

EXTERNAL debt burden thresholds	Weak	Medium	Strong
PV of debt in % of			
Exports	140	180	240
GDP	30	40	55
Debt service in % of			
Exports	10	15	21
Revenue	14	18	23
TOTAL public debt benchmark			
PV of total public debt in percent of GDP	35	55	70

13. Stress tests generally follow standardized settings and include shocks for natural disasters and commodity export prices. The contingent liability stress test is based on the quantification of potential contingent liabilities discussed above (including SOE-related concerns that extend beyond the baseline SOE debt coverage), and the standardized stress tests apply the default settings. In addition, Madagascar remains exposed and vulnerable to natural disaster shocks, like cyclones, and hence qualifies for the natural disaster shock.[6] Since commodities (e.g., vanilla, nickel, cobalt, etc.) comprise about half of goods and services exports, we also include a commodity shock stress test. The standardized settings of this stress test are customized to better reflect Madagascar's country-specific circumstances. In particular, we assume an illustrative fall in prices equivalent to 10 percent of commodity exports, with no mitigating effect on imports, alongside declines in real GDP growth of 0.5 percent and in fiscal revenue of 0.25 percent of GDP. The shock occurs in 2020 and unwinds gradually by 2029. Residual financing for external debt stress tests is assumed to be from external sources with rates 25 percent above current concessional rates and with lower average maturities (75 percent of current average maturity periods). For overall public debt stress tests, limited recourse to domestic sources in the short run prompts us to assume 65 percent of additional financing would come from external sources and that the remaining domestic financing would be more expensive than under the baseline.[7]

DEBT SUSTAINABILITY RESULTS

A. External Debt Sustainability

14. Under the baseline, rising external PPG debt remains well below thresholds (Table 1, Figure 1). External PPG debt is projected to rise from 27 percent of GDP in 2019 to 37 percent of GDP in 2029 before reaching 40 percent of GDP in 2039. The July 2019 DSA projected an increase in external PPG debt ratios of 7.5 percent of GDP from 2019 to 2039; this DSA projects an increase of 13.0 over the same period. Debt-creating flows include a steadily rising current account deficit over the medium term (owing to declines in the trade balance and falling inflows from official transfers) and weaker endogenous debt dynamics (higher interest rates).[8] In present value terms, external PPG debt is projected to rise from 16 percent of GDP in 2019 to 25 percent of GDP in 2029 and 29 percent in 2030. The long-term rise in PV terms is the result of our assumption that borrowing will become less concessional over the long term, with increases in borrowing costs. Together with expiring grace periods for some loans, this explains why debt service indicators rise substantially off their low base. For example, the projected debt service to exports ratio rises from 3 in 2019 to 5 in 2029. Nonetheless, all indicators remain well below the applicable thresholds for Madagascar (see Figure 1).

15. None of the shock scenarios breach the external medium-carrying capacity thresholds applied for Madagascar by 2029 (Table 3; Figure 1). The most serious shocks are to export growth, which is set to one standard deviation of the projection or historical average (whichever yields lower

[6] We apply the default settings for this one-off shock in the template, namely a 10 percentage-point rise in the debt-to-GDP ratio alongside a fall in real GDP growth (1.5 percent) and exports (3.5 percent), in 2020.

[7] We view this as reasonable given the continued underdevelopment of Madagascar's domestic bond market and its re-engagement with international donors and investors. The authorities have also communicated that there is significant international appetite for lending to Madagascar.

[8] The residual, which includes reserve accumulation, unrepatriated mining receipts, and potentially other misclassified BOP entries, is assumed to decline steadily over time as the share of mining exports declines and reserve accumulation slows.

exports) in 2020 and 2021 and to a combined shock (which applies shocks to GDP, exports, the primary balance, current transfers, and depreciation at half their standard magnitudes). Using the applicable thresholds for Madagascar's medium debt-carrying capacity, the most extreme shocks do not breach any of the four thresholds.[9] Under the combined shock, the PV of debt to GDP rises to 30 percent of GDP in 2024 and 32 in 2029, below the indicated threshold of 40.[10]

16. The historical scenarios and granularity of assessment are less applicable to Madagascar. The historical scenario shows the PV of debt to GDP approaching 46 by 2029 but, as discussed in prior DSAs, is currently not a useful stress test or measure of realism since it includes data with atypically high current account deficits related to private mining investment. For countries that breach external debt thresholds, further granularity can be provided by assessing the gap between baseline debt projections and the threshold between moderate and high debt distress. This is not the case for Madagascar given its low risk of debt distress.

17. Private sector debt is not assessed to pose a significant threat to external sustainability (see Table 1). Private external debt is projected to decline as the loans related to a major mining project are repaid. Using information on financial plans, including on mining, the share of private external debt in GDP is anticipated to fall by half within the next decade. Given the exceptional nature of the mining projects, the DSA does not forecast substantial new external borrowing from the private sector over the corresponding period. However, in line with the July 2019 DSA, we have conservatively assumed more borrowing would be needed to sustain mining exports towards the end of the DSA horizon, contributing to private debt equivalent to about 7 percent of GDP in 2039. Such debt is not assessed to pose a significant threat to external sustainability. Consistent with recent experience leading to slower amortization, the ultimate liability for these loans is held by the multinational shareholders rather than resident entities (such as domestic banks or the government).

B. Total Public Debt Sustainability

18. Under the baseline, total public debt levels are projected to remain well below benchmarks (Table 2). Total public debt (both external and domestic) is projected to rise from 40 percent of GDP in 2019 to 47 percent of GDP in 2029, before reaching 51 percent by 2039. In the July 2019 DSA, total public debt was projected at 57 percent of GDP in 2029 and 2039. In PV terms, total public debt/GDP is expected to rise from 29 percent in 2019 to 36 percent in 2029 and 40 percent in 2039; the projected level in 2039 is below the expected level from the July 2019 DSA and below the benchmark of 55 percent for medium-capacity countries. Projected primary deficits are also lower than previously assumed; for example, the 2019 and 2020 primary deficits were previously projected to reach 1.3 and 3.5 percent, respectively; they are now expected to reach 0.6 and 1.9 percent behind strong revenue mobilization and ongoing PFM reforms.[11] This is also reflected by the more gradual increase in the PV of debt to revenue and grants compared to the PV of debt to GDP since the share of tax revenue in GDP is projected to rise in the medium to long term.

[9] However, the debt-service-to-revenue ratio peaks at about 15, which is above the threshold of 14 for weak capacity countries. Madagascar was previously classified as having weak debt-carrying capacity in June 2018.

[10] The PV of debt-to-GDP would breach the threshold of 30 for countries with weak debt-carrying capacity.

[11] Of course, the re-basing of GDP (e.g., 2018 PV debt to GDP is now 5 percentage points lower than previously calculated) is also a contributing factor.

Despite this, and consistent with a shift to less concessional financing sources, the rise in debt service to revenue and grants increases slightly towards the end of the projection horizon.

19. Total public debt is vulnerable to growth shocks over the long term (Figure 2; Table 4). The most severe test is the simulated GDP shock, where growth in 2020 and 2021 is one standard deviation lower than its historical average or the forecast (whichever yields lower GDP) with interacting effects on the primary balance and inflation. Under this shock, the PV of debt to GDP exceeds 55 percent of GDP at the end of the period and is on a persistent upward trajectory. The benchmark for medium capacity countries like Madagascar is 55. Moreover, such a shock would also result in a debt service to revenue ratio above 75 percent before 2029 and a PV of debt to revenue above 400 in 2029. Although no explicit benchmark exists for these ratios, the projections point to potentially severe debt service and liquidity difficulties in the long run if no action to contain borrowing is taken soon after the shock. An export shock, a natural disaster shock, a commodity price shock, or the contingent liability shock would also increase total public debt burdens.

RISK RATING AND VULNERABILITIES

20. Madagascar is classified as being at low risk of external debt distress. Under the baseline, no thresholds are breached. Stress tests produce no breaches of the higher thresholds that apply to Madagascar's medium capacity to carry debt.

21. The overall assessment is that Madagascar is at moderate risk of overall debt distress. The overall PPG debt stress test that applies to GDP growth leads to a breach of the applicable benchmark in the final years of the projection period and is on a persistent upward trajectory. Moreover, shocks could introduce liquidity problems as the debt-service to revenue ratio could exceed 75 percent over the long term. Together with potentially high debt service burdens, the breach classifies Madagascar's overall risk of debt distress as moderate.

22. These assessments continue to be supportive of Madagascar's current plans to scale up its borrowing to meet its investment needs, however several factors may lead to increased vulnerability. A steeper-than-expected increase in borrowing in line with a rapid execution of the government's ambitious medium-term borrowing plan would carry significant risks. Also, poorly selected public investments and less favorable financing terms could affect debt vulnerability. *There are countries in the region that have experienced sharp deterioration in their external debt distress rating from low to high within a short period of time.* As relayed in the July 2019 DSA, in addition to debt sustainability, other crucial considerations for the pace of borrowing include the economy's vulnerability to terms-of-trade shocks, natural disasters, general absorptive capacity, public financial management, and public investment management.

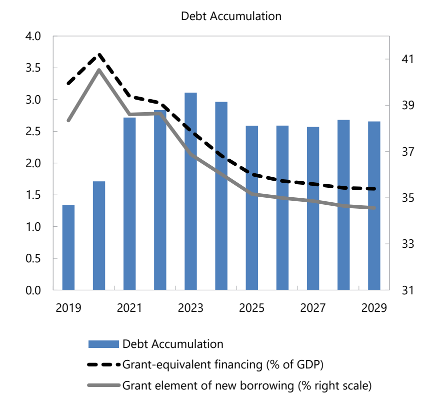
23. Relevant factors that could affect future assessments include data revisions and the speed of realization of borrowing plans. Staff have assumed a slightly slower pace of project disbursement than the authorities. Further shortfalls in disbursements on borrowing or alternatively more ambitious borrowing plans beyond the medium term would affect the debt profile. The state of SOE liabilities could also influence future assessments. Less grant financing and a switch to a less concessional mix of borrowing would raise the debt burden, especially when measured in PV terms, as well as debt service risks. Efforts to enhance external statistics could improve private debt coverage. Finally, Madagascar's ability to preserve and build on its debt-carrying capacity, including by strengthening the capacity and quality of its institutions, remains important.

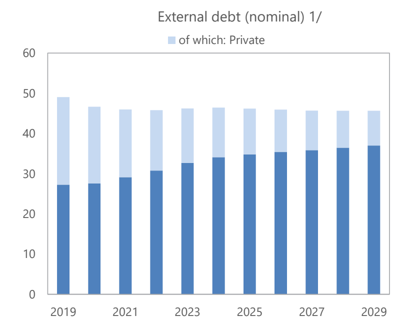
Table 1. Madagascar: External Debt Sustainability Framework, Baseline Scenario, 2016-2039

(In percent of GDP; unless otherwise indicated)

	Actual			Projections								Average 8/	
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029	2039	Historical	Projections
External debt (nominal) 1/	51.0	50.2	50.6	49.1	46.7	46.0	45.8	46.2	46.4	45.7	47.4	39.3	46.3
of which: public and publicly guaranteed (PPG)	25.3	25.7	26.7	27.2	27.6	29.1	30.8	32.7	34.1	37.0	40.3	24.8	32.8
											13.0		
Change in external debt	-1.9	-0.8	0.5	-1.6	-2.4	-0.7	-0.2	0.4	0.2	0.0	-0.3		
Identified net debt-creating flows	-6.6	-7.4	-5.7	-4.9	-3.6	-3.5	-3.4	-3.1	-2.8	-2.4	-3.6	-0.4	-3.1
Non-interest current account deficit	-0.8	0.0	-1.2	-0.5	0.9	1.0	1.2	1.5	1.7	1.7	0.2	4.6	1.3
Deficit in balance of goods and services	1.9	3.3	3.4	3.6	4.7	4.2	4.5	4.9	5.1	5.4	4.0	7.7	4.8
Exports	28.3	30.9	31.5	29.9	29.2	30.2	29.9	29.1	28.8	28.1	27.7		
Imports	30.2	34.2	34.9	33.5	33.9	34.4	34.4	34.1	33.9	33.4	31.7		
Net current transfers (negative = inflow)	-5.8	-5.6	-7.0	-6.1	-5.9	-5.1	-5.1	-5.1	-5.0	-4.8	-4.4	-5.3	-5.2
of which: official	-2.9	-2.5	-2.6	-2.5	-2.5	-1.4	-1.2	-0.6	-0.4	-0.1	0.0		
Other current account flows (negative = net inflow)	3.1	2.3	2.4	2.0	2.1	2.0	1.8	1.6	1.5	1.2	0.6	2.2	1.6
Net FDI (negative = inflow)	-3.8	-2.7	-2.6	-2.6	-2.7	-2.7	-2.8	-2.8	-2.8	-2.8	-2.8	-4.4	-2.8
Endogenous debt dynamics 2/	-2.0	-4.8	-1.9	-1.8	-1.7	-1.8	-1.8	-1.7	-1.6	-1.3	-0.9		
Contribution from nominal interest rate	0.4	0.4	0.5	0.6	0.6	0.5	0.6	0.6	0.7	0.9	1.2		
Contribution from real GDP growth	-2.0	-1.8	-2.2	-2.4	-2.4	-2.3	-2.4	-2.3	-2.4	-2.2	-2.1		
Contribution from price and exchange rate changes	-0.3	-3.3	-0.3	...	...	...	...	...	...	...	...		
Residual 3/	4.7	6.6	6.2	3.3	1.2	2.8	3.2	3.4	3.0	2.4	3.2	3.0	2.6
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		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	...	...	15.3	16.4	16.6	17.8	19.1	20.4	21.6	25.0	28.9		
PV of PPG external debt-to-exports ratio	...	...	48.7	54.7	56.8	59.1	63.8	70.2	75.0	88.9	104.4		
PPG debt service-to-exports ratio	3.1	5.6	2.6	2.7	3.2	3.1	3.5	4.3	4.6	5.0	7.1		
PPG debt service-to-revenue ratio	9.3	16.7	7.9	7.6	8.2	8.1	8.8	10.1	10.1	10.1	12.8		
Gross external financing need (Million of U.S. dollars)	-425.0	12.5	-349.7	104.0	294.6	302.5	352.8	409.8	435.2	511.8	221.3		
Key macroeconomic assumptions													
Real GDP growth (in percent)	4.0	3.9	4.6	4.8	5.2	5.4	5.6	5.6	5.6	5.2	4.7	2.2	5.4
GDP deflator in US dollar terms (change in percent)	0.6	7.0	0.5	-2.8	3.5	2.7	2.7	2.8	2.7	2.7	2.8	0.6	2.3
Effective interest rate (percent) 4/	0.7	0.8	1.1	1.1	1.4	1.2	1.4	1.5	1.7	2.2	2.6	0.7	1.7
Growth of exports of G&S (US dollar terms, in percent)	7.2	21.6	7.0	-3.1	6.3	12.0	7.3	5.8	7.1	7.7	6.5	6.3	6.7
Growth of imports of G&S (US dollar terms, in percent)	3.3	26.2	7.1	-2.1	10.1	9.8	8.5	7.5	7.9	7.9	4.2	0.9	7.4
Grant element of new public sector borrowing (in percent)	...	...	...	38.3	40.5	38.6	38.6	36.9	36.0	34.6	33.9	...	36.7
Government revenues (excluding grants, in percent of GDP)	9.5	10.3	10.5	10.6	11.2	11.7	12.0	12.5	13.0	14.0	15.3	9.1	12.6
Aid flows (in Million of US dollars) 5/	606.2	606.6	634.9	511.6	715.1	843.6	948.6	1032.9	1030.8	1114.2	1912.0		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	3.3	3.7	3.0	2.9	2.5	2.1	1.6	1.3	...	2.4
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	70.4	68.0	53.2	50.8	43.5	40.5	36.8	33.9	...	47.1
Nominal GDP (Million of US dollars)	11,849	13,176	13,851	14,106	15,365	16,639	18,045	19,575	21,221	31,487	66,858		
Nominal dollar GDP growth	4.6	11.2	5.1	1.8	8.9	8.3	8.5	8.5	8.4	8.1	7.6	2.9	7.8
	17%	15%	15%	12%	12%	13%	13%	14%	15%	18% #	23%		
Memorandum items:													
PV of external debt 7/	...	...	39.3	38.2	35.7	34.7	34.1	34.0	33.9	33.6	36.0		
In percent of exports	...	...	124.9	127.6	122.2	114.8	114.2	116.7	117.9	119.7	130.0		
Total external debt service-to-exports ratio	3.8	9.0	4.1	12.8	12.8	11.7	11.8	11.8	11.2	9.6	10.8		
PV of PPG external debt (in Million of US dollars)			2122.0	2308.0	2549.5	2967.0	3438.7	3999.9	4580.1	7859.2	19335.8		
(PVt-PVt-1)/GDPt-1 (in percent)				1.3	1.7	2.7	2.8	3.1	3.0	2.7	2.1		
Non-interest current account deficit that stabilizes debt ratio	1.1	0.9	-1.7	1.1	3.3	1.7	1.3	1.1	1.4	1.8	0.5		

Definition of external/domestic debt	Currency-based
Is there a material difference between the two criteria?	No





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

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

6/ 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).

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

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

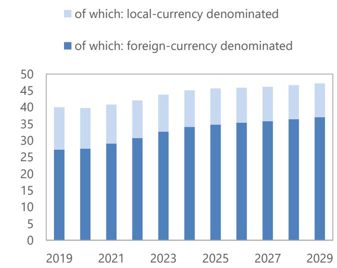
Table 2. Madagascar: Public Sector Debt Sustainability Framework, Baseline Scenario, 2016-2039

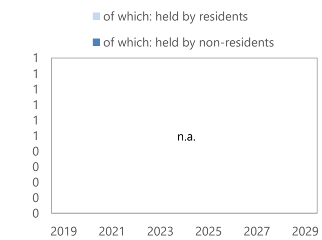
(In percent of GDP; unless otherwise indicated)

	Actual			Projections								Average 6/	
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029	2039	Historical	Projections
Public sector debt 1/	**40.3**	**40.0**	**39.9**	**40.1**	**39.8**	**40.8**	**42.1**	**43.8**	**45.1**	**47.2**	**51.1**	**36.6**	**43.9**
of which: external debt	**25.3**	**25.7**	**26.7**	**27.2**	**27.6**	**29.1**	**30.8**	**32.7**	**34.1**	**37.0**	**40.3**	**24.8**	**32.8**
Change in public sector debt	-3.8	-0.2	-0.1	0.2	-0.2	1.0	1.3	1.7	1.3	0.5	-0.2		
Identified debt-creating flows	**-3.5**	**-2.6**	**-1.9**	**-1.2**	**-0.1**	**1.0**	**1.3**	**1.9**	**1.5**	**0.5**	**-0.2**	**-0.3**	**0.7**
Primary deficit	**0.4**	**1.4**	**0.6**	**0.6**	**1.9**	**3.6**	**3.8**	**4.1**	**3.5**	**2.8**	**2.0**	**1.3**	**2.8**
Revenue and grants	12.4	12.8	12.9	13.0	13.8	13.0	13.2	13.1	13.3	14.1	15.3	**10.9**	**13.5**
of which: grants	2.9	2.5	2.5	2.4	2.5	1.4	1.2	0.6	0.4	0.1	0.0		
Primary (noninterest) expenditure	12.8	14.2	13.5	13.5	15.7	16.6	16.9	17.2	16.8	16.9	17.3	**12.3**	**16.4**
Automatic debt dynamics	**-3.9**	**-4.0**	**-2.5**	**-1.8**	**-2.5**	**-3.0**	**-2.9**	**-2.6**	**-2.4**	**-2.7**	**-2.6**		
Contribution from interest rate/growth differential	-3.1	-2.4	-3.0	-2.3	-2.3	-2.7	-2.6	-2.4	-2.2	-2.5	-2.3		
of which: contribution from average real interest rate	-1.4	-0.9	-1.3	-0.5	-0.3	-0.7	-0.5	-0.2	0.1	-0.1	-0.1		
of which: contribution from real GDP growth	-1.7	-1.5	-1.7	-1.8	-2.0	-2.0	-2.2	-2.2	-2.3	-2.3	-2.3		
Contribution from real exchange rate depreciation	-0.8	-1.5	0.6	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	**0.0**	**0.0**	**0.0**	**0.0**	**0.5**	**0.5**	**0.5**	**0.5**	**0.5**	**0.4**	**0.4**	**0.0**	**0.4**
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 contingent liabilities (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		
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 debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.5	0.5	0.5	0.5	0.5	0.4	0.4		
Residual	**-0.3**	**2.3**	**1.8**	**1.9**	**-0.4**	**-0.3**	**-0.3**	**-0.4**	**-0.5**	**-0.2**	**-0.3**	**1.8**	**-0.1**
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	**...**	**...**	**29.2**	**29.4**	**29.2**	**29.8**	**30.6**	**31.8**	**32.9**	**35.5**	**40.1**		
PV of public debt-to-revenue and grants ratio	**...**	**...**	**225.7**	**226.2**	**212.0**	**228.9**	**232.1**	**243.6**	**246.6**	**251.2**	**261.4**		
Debt service-to-revenue and grants ratio 3/	**7.0**	**7.0**	**6.4**	**43.9**	**48.2**	**55.3**	**57.0**	**62.2**	**65.8**	**62.5**	**62.8**		
Gross financing need 4/	1.2	2.3	1.4	6.6	9.1	11.3	11.8	12.7	12.7	12.1	12.0		
									1.12		1.36		
Key macroeconomic and fiscal assumptions									1.09		1.16		
Real GDP growth (in percent)	4.0	3.9	4.6	4.8	5.2	5.4	5.6	5.6	5.6	5.2	4.7	**2.2**	**5.4**
Average nominal interest rate on external debt (in percent)	0.8	0.9	1.1	1.2	1.4	1.2	1.3	1.3	1.3	1.4	1.6	**0.6**	**1.3**
Average real interest rate on domestic debt (in percent)	-8.2	-4.7	-7.0	-3.0	-1.2	-4.1	-2.3	0.2	3.4	0.8	1.3	**-6.8**	**-0.1**
Real exchange rate depreciation (in percent, + indicates depreciation)	-3.0	-6.3	2.3	...	...	...	...	...	...	...	...	**1.0**	**...**
Inflation rate (GDP deflator, in percent)	9.0	5.0	7.6	5.9	7.2	6.5	5.6	5.5	5.4	5.2	5.0	**7.3**	**5.7**
Growth of real primary spending (deflated by GDP deflator, in percent)	8.0	15.6	-1.0	5.2	21.6	11.6	8.0	6.8	3.3	5.9	3.8	**1.7**	**7.6**
Primary deficit that stabilizes the debt-to-GDP ratio 5/	4.1	1.7	0.7	0.4	2.1	2.6	2.5	2.4	2.2	2.3	2.2	**2.2**	**2.2**
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central, state, and local governments, central bank, government-guaranteed debt, non-guaranteed SOE debt . Definition of external debt is Currency-based.

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

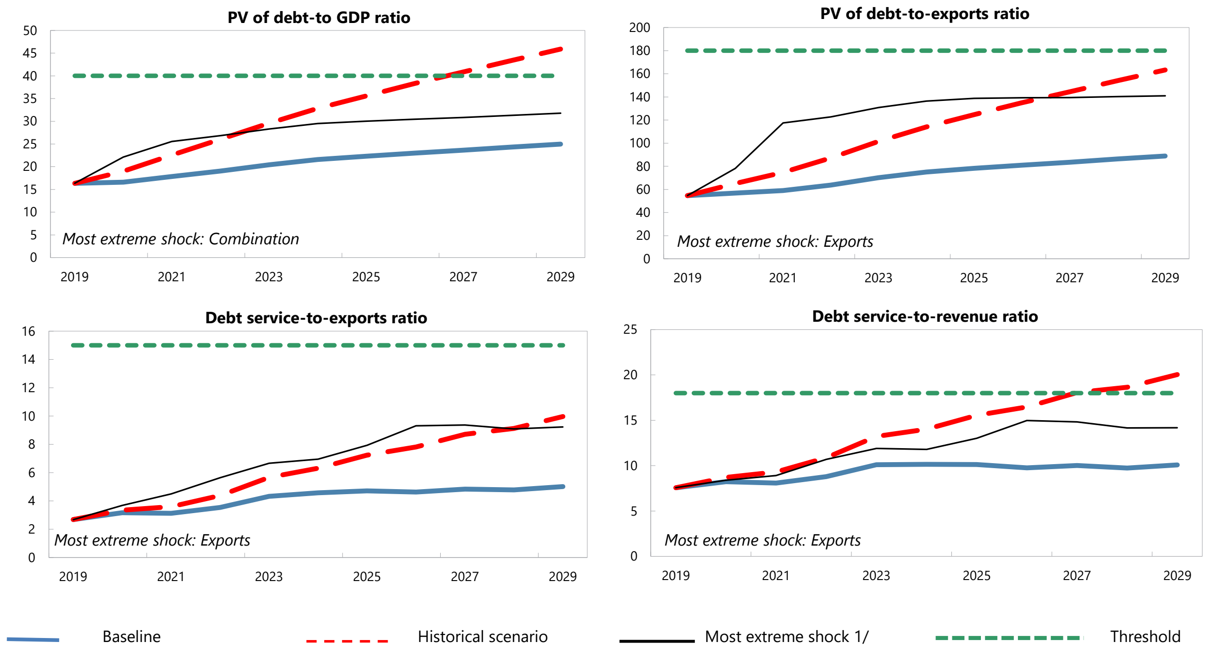
3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

4/ 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 and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Figure 1. Madagascar: Indicators of Public and Publicly Guaranteed External Debt Under Alternatives Scenarios, 2019-2029



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	No	
Natural disaster	No	No
Commodity price	Yes	Yes
Market financing	n.a.	n.a.

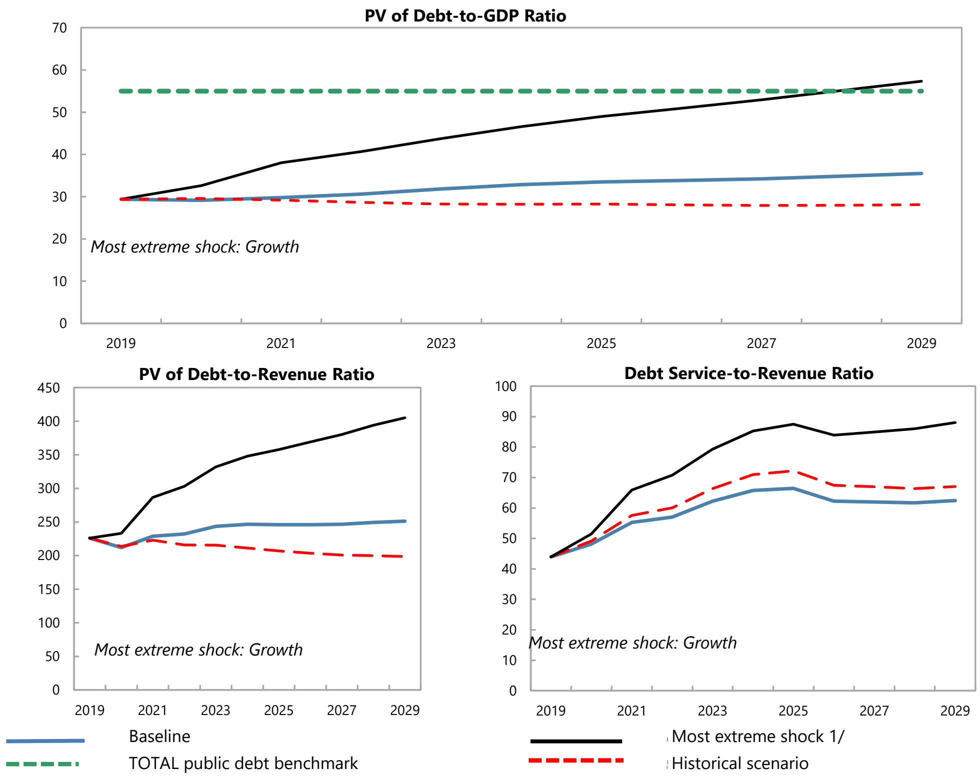
Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.5%	1.8%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	26	20
Avg. grace period	4	4

* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in or before 2029. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 2. Madagascar: Indicators of Public Debt Under Alternative Scenarios, 2019-2029



Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	36%	65%
Domestic medium and long-term	5%	15%
Domestic short-term	59%	20%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.5%	1.8%
Avg. maturity (incl. grace period)	26	20
Avg. grace period	4	4
Domestic MLT debt		
Avg. real interest rate on new borrowing	3.0%	4.0%
Avg. maturity (incl. grace period)	2	4
Avg. grace period	1	1
Domestic short-term debt		
Avg. real interest rate	2.7%	3.5%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2029. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Table 3. Madagascar: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2019-2029

(In percent)

	Projections 1/										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
PV of debt-to GDP ratio											
Baseline	16	17	18	19	20	22	22	23	24	24	25
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	16	19	23	26	30	33	36	38	**41**	**43**	**46**
B. Bound Tests											
B1. Real GDP growth	16	18	21	23	24	26	27	27	28	29	30
B2. Primary balance	16	17	19	20	21	22	23	24	24	25	26
B3. Exports	16	20	27	28	29	30	30	30	30	30	30
B4. Other flows 3/	16	19	22	23	24	25	26	26	26	27	27
B5. Depreciation	16	21	20	22	23	25	26	27	28	29	30
B6. Combination of B1-B5	16	22	26	27	28	30	30	30	31	31	32
C. Tailored Tests											
C1. Combined contingent liabilities	16	20	22	23	24	26	26	27	27	28	28
C2. Natural disaster	16	22	24	25	27	28	29	30	30	31	31
C3. Commodity price	16	17	19	20	22	23	24	24	25	25	26
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	40	40	40	40	40	40	40	40	40	40	40
PV of debt-to-exports ratio											
Baseline	55	57	59	64	70	75	78	81	84	86	89
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	55	65	75	87	102	114	125	135	144	154	163
B. Bound Tests											
B1. Real GDP growth	55	57	59	64	70	75	78	81	84	86	89
B2. Primary balance	55	58	61	66	73	78	81	84	86	89	91
B3. Exports	55	78	117	123	131	136	139	139	140	140	141
B4. Other flows 3/	55	65	73	77	84	88	90	92	93	95	97
B5. Depreciation	55	57	53	58	64	69	73	76	79	82	85
B6. Combination of B1-B5	55	74	71	88	95	100	102	104	106	108	110
C. Tailored Tests											
C1. Combined contingent liabilities	55	68	71	77	84	89	92	95	97	99	101
C2. Natural disaster	55	75	80	86	94	100	103	106	109	112	114
C3. Commodity price	55	60	64	69	76	80	83	85	87	90	92
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	180	180	180	180	180	180	180	180	180	180	180
Debt service-to-exports ratio											
Baseline	3	3	3	4	4	5	5	5	5	5	5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	3	3	4	4	6	6	7	8	9	9	10
B. Bound Tests											
B1. Real GDP growth	3	3	3	4	4	5	5	5	5	5	5
B2. Primary balance	3	3	3	4	4	5	5	5	5	5	5
B3. Exports	3	4	5	6	7	7	8	9	9	9	9
B4. Other flows 3/	3	3	3	4	5	5	5	6	6	6	6
B5. Depreciation	3	3	3	3	4	4	5	4	4	4	5
B6. Combination of B1-B5	3	3	4	4	5	6	7	6	7	6	7
C. Tailored Tests											
C1. Combined contingent liabilities	3	3	3	4	5	5	5	5	5	5	5
C2. Natural disaster	3	3	4	4	5	5	5	5	5	5	6
C3. Commodity price	3	3	3	4	5	5	5	5	5	5	5
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	15	15	15	15	15	15	15	15	15	15	15
Debt service-to-revenue ratio											
Baseline	8	8	8	9	10	10	10	10	10	10	10
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	8	9	9	11	13	14	16	16	**18**	**19**	**20**
B. Bound Tests											
B1. Real GDP growth	8	9	10	10	12	12	12	12	12	12	12
B2. Primary balance	8	8	8	9	10	10	10	10	10	10	11
B3. Exports	8	8	9	11	12	12	13	15	15	14	14
B4. Other flows 3/	8	8	9	10	11	11	12	12	12	12	12
B5. Depreciation	8	10	10	11	12	12	12	11	11	11	12
B6. Combination of B1-B5	8	9	10	11	13	13	14	14	14	14	14
C. Tailored Tests											
C1. Combined contingent liabilities	8	8	9	9	11	11	11	10	11	10	11
C2. Natural disaster	8	8	9	10	11	11	11	11	11	11	11
C3. Commodity price	8	8	8	9	11	11	11	11	11	10	11
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Threshold	18	18	18	18	18	18	18	18	18	18	18

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. Madagascar: Sensitivity Analysis for Key Indicators of Public Debt, 2019-2029

	Projections 1/										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
PV of Debt-to-GDP Ratio											
Baseline	29	29	30	31	32	33	33	34	34	35	35
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	29	30	29	29	28	28	28	28	28	28	28
B. Bound Tests											
B1. Real GDP growth	29	33	38	41	44	47	49	51	53	**55**	**57**
B2. Primary balance	29	30	31	32	33	34	35	35	35	36	36
B3. Exports	29	32	38	39	40	41	41	40	40	40	40
B4. Other flows 3/	29	32	34	35	36	37	37	37	37	37	38
B5. Depreciation	29	32	31	30	30	30	29	29	29	28	28
B6. Combination of B1-B5	29	30	32	33	34	35	36	36	37	38	38
C. Tailored Tests											
C1. Combined contingent liabilities	29	35	35	36	37	37	38	38	38	39	39
C2. Natural disaster	29	38	38	39	40	40	41	41	41	42	43
C3. Commodity price	29	31	34	37	41	44	47	49	51	53	**56**
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
TOTAL public debt benchmark	55	55	55	55	55	55	55	55	55	55	55
PV of Debt-to-Revenue Ratio											
Baseline	226	212	229	232	244	247	246	246	247	249	251
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	226	214	223	216	216	211	207	204	201	200	199
B. Bound Tests											
B1. Real GDP growth	226	233	286	303	332	348	358	369	380	394	405
B2. Primary balance	226	217	239	242	253	255	254	253	253	256	257
B3. Exports	226	234	296	295	305	305	299	293	288	286	283
B4. Other flows 3/	226	230	262	263	274	275	272	269	267	267	267
B5. Depreciation	226	232	237	230	230	224	217	211	206	203	201
B6. Combination of B1-B5	226	216	241	247	261	265	264	265	266	269	270
C. Tailored Tests											
C1. Combined contingent liabilities	226	254	270	270	280	281	278	276	276	277	278
C2. Natural disaster	226	275	292	293	303	304	301	299	299	301	301
C3. Commodity price	226	227	266	288	318	336	347	356	368	383	395
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Debt Service-to-Revenue Ratio											
Baseline	44	48	55	57	62	66	66	62	62	62	62
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2019-2029 2/	44	49	58	60	66	71	72	67	67	66	67
B. Bound Tests											
B1. Real GDP growth	44	51	66	71	79	85	87	84	85	86	88
B2. Primary balance	44	48	56	59	63	67	67	63	63	62	63
B3. Exports	44	48	56	59	64	67	69	67	66	66	66
B4. Other flows 3/	44	48	56	58	63	66	68	65	64	64	64
B5. Depreciation	44	46	54	54	60	63	64	60	59	59	59
B6. Combination of B1-B5	44	48	57	59	65	70	71	67	67	66	67
C. Tailored Tests											
C1. Combined contingent liabilities	44	48	67	63	67	70	69	64	63	63	63
C2. Natural disaster	44	49	73	66	70	73	71	66	66	65	66
C3. Commodity price	44	49	59	65	73	79	81	77	78	79	81
C4. Market Financing	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

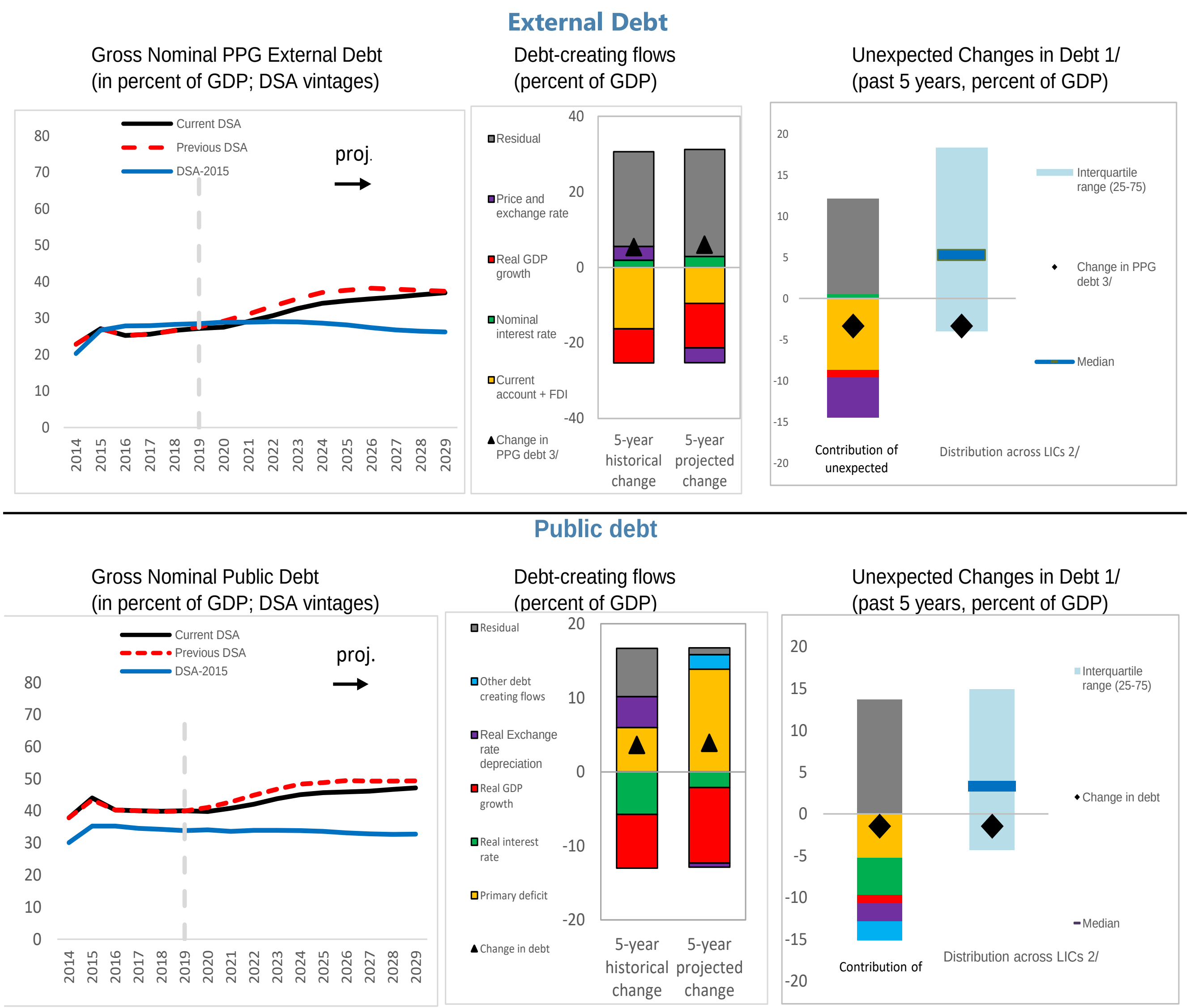
Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the benchmark.

2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.

3/ Includes official and private transfers and FDI.

Figure 3. Madagascar Debt Dynamics - Baseline Scenario: Drivers of External Debt



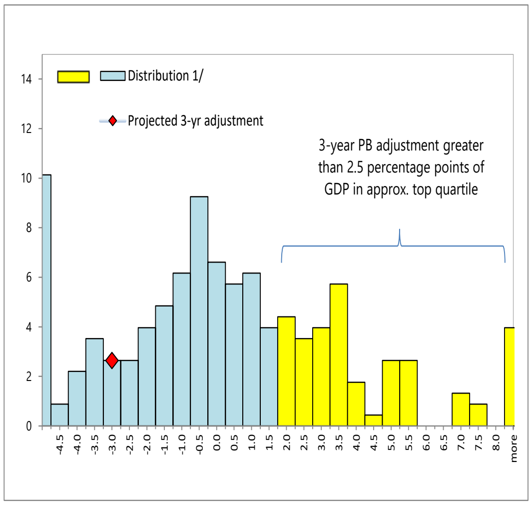
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

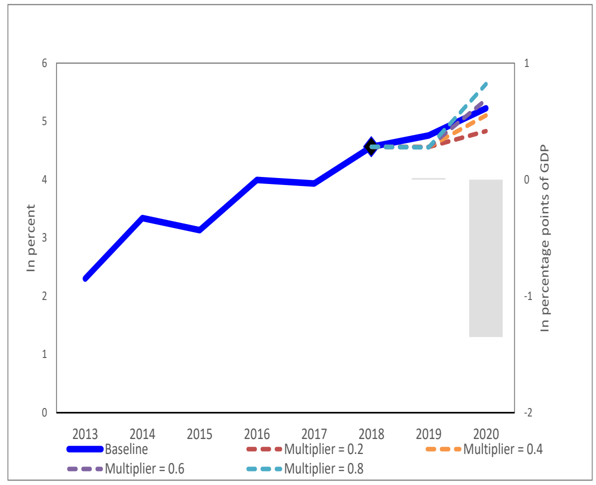
Figure 4. Madagascar: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



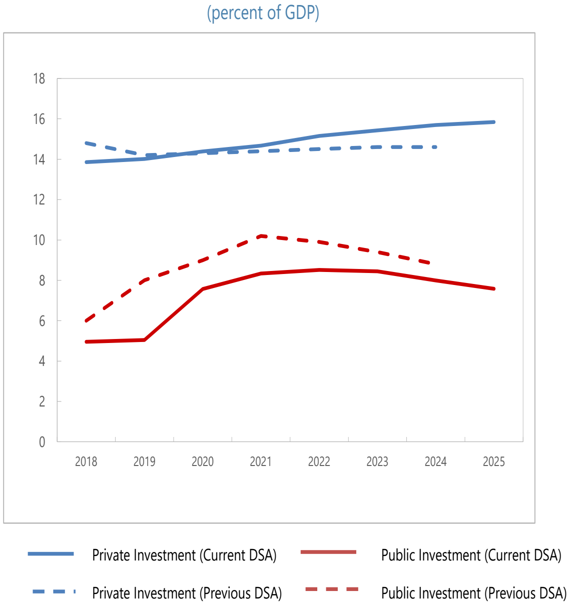
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/

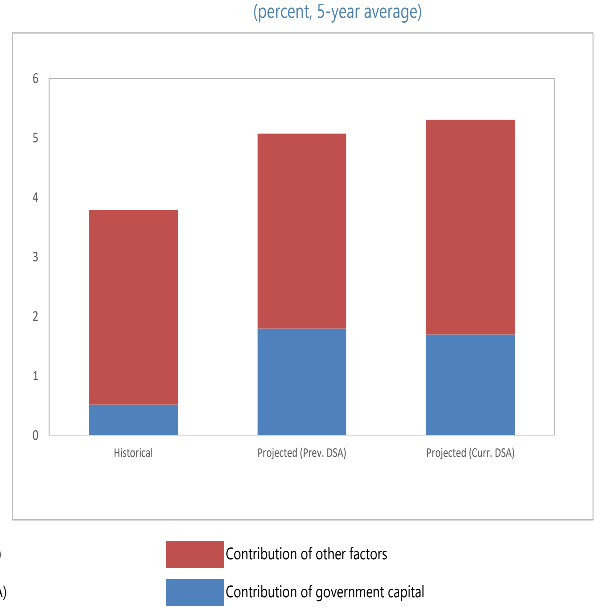


1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates1/
(percent of GDP)



Contribution to Real GDP growth
(percent, 5-year average)



1/ The previous DSA was completed prior to the rebasing of GDP. The shares are calculated using nominal data.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MADAGASCAR

January 9, 2020

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION AND SIXTH REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT—INFORMATIONAL ANNEX

Prepared By | The African Department

CONTENTS

FUND RELATIONS

(As of October 31, 2019)

Membership Status: Joined: September 25, 1963; Article VIII

General Resources Account:	**SDR Million**	**%Quota**
Quota	244.40	100.00
IMF's Holdings of Currency (Holdings Rate)	213.78	87.47
Reserve Tranche Position	30.63	12.53

SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	117.09	100.00
Holdings	1.84	1.57

Outstanding Purchases and Loans:	**SDR Million**	**%Allocation**
RCF Loans	61.10	25.00
ECF Arrangements	219.12	89.66

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF	Jul 27, 2016	Nov 26, 2019	250.55	219.12
ECF[1/]	Jul 21, 2006	Jul 20, 2009	73.32	53.03
ECF[1/]	Mar 01, 2001	Mar 01, 2005	91.65	91.65

[1/] Formerly PRGF.

Overdue Obligations and Projected Payments to Fund [2/]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2019	2020	2021	2022	2023
Principal	3.06	6.11	12.22	18.51	37.19
Charges/Interest	0.26	0.94	0.93	0.94	0.94
Total	3.31	7.05	13.15	19.44	38.12

[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
I. Commitment of HIPC assistance	
Decision point date	Dec 2000
Assistance committed by all creditors (US$ Million) [1/]	835.75
Of which: IMF assistance (US$ million)	19.17
(SDR equivalent in millions)	14.73
Completion point date	Oct 2004
II. Disbursement of IMF assistance (SDR Million)	
Assistance disbursed to the member	14.73
Interim assistance	5.62
Completion point balance	9.11
Additional disbursement of interest income [2/]	1.69
Total disbursements	16.42

[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 at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

Implementation of Multilateral Debt Relief Initiative (MDRI):

I. MDRI-eligible debt (SDR Million)[1/]	137.29
Financed by: MDRI Trust	128.50
Remaining HIPC resources	8.79

II. Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGT**	**Total**
January 2006	N/A	137.29	137.29

[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.

Implementation of Catastrophe Containment and Relief (CCR): Not Applicable

Exchange Rate Arrangement

The currency of the Republic of Madagascar is the Malagasy ariary. The de jure exchange rate arrangement is free floating; the de facto exchange rate arrangement is classified as floating. As of November 20, 2019, the rate was US$1 = 3660 ariary. Effective September 18, 1996, Madagascar accepted the obligations of Article VIII of the Fund's Articles of Agreement.

Safeguards Assessment

The March 2017 update safeguards assessment of the Banky Foiben'i Madagasikara (BFM) found that significant progress had been made in implementing recommendations from the 2015 assessment, including strengthening the legal framework and establishing an audit committee to oversee the internal and external audit process. The July 2018 Safeguards Monitoring Report followed up on the implementation of the recommendations from the 2017 assessment and found a stronger safeguards framework. Notably, controls in currency operations and procurement processes were enhanced. BFM had continued to modernize its audit processes and transparency in financial reporting was improved through timely publication of annual audited financial statements. The central bank is making progress in transitioning to IFRS with IMF technical assistance.

Article IV Consultation

Madagascar is on 24-month Article IV consultation cycle. The previous Article IV consultation was concluded on June 28, 2017 (IMF Country Report No. 17/223).

Technical Assistance (TA) since January 2017

Fiscal Affairs Department (FAD)

2017

Data Matching of Customs and Domestic Tax Data (AFS)
Medium-Term Budget Framework and Public Investment
AFS: Ensuring that adequate controls are in place to prevent fraud and revenue leakage
AFS: Ensure a robust risk management capability to balance trade facilitation and compliance
AFS: Management of Natural Resources and Public Investment
AFS: Debt Management Strategy/Program
AFS: Compliance Risk Management Strategy Fiscal Risks Tax Incentives for Investment

2018

Modernization of tax and customs administrations and revenue mobilization
Customs administration: control and clearance operations
Strengthening capacity to manage tax arrears (AFS)
AFS: Provide advice and guidance on the development of customs modernization and reform program
Tax and Customs Administration
AFS Wage Bill Management PFM Reform Management
AFS: Follow up on inputs to enhance the effectiveness and sustainability of PCA
AFS: Improving multiyear projects management
AFS: Customs Code (Offsite) AFS: Improving Multiyear Projects Management

2019

Public Investment Management
Management of Fiscal Risks
Revenue Mobilization Strategy (planned October)
Quarterly AFS missions on tax, customs, debt management, fiscal statistics
PIMA Follow up mission
AFS PFM regulations
AFS: Progress on implementation of debt management & recovery strategy reviewed
AFS: Reform action plan adopted and regularly updated
AFS: National Risk based audit plan & quality standards developed and implementation support
AFS: Customs-Trade Agreements-Updating the Customs Code
Pension Reform
Management of Tax Arrears
Strengthening Audit Capacity
Multi-year Reform Plan

Monetary and Capital Markets Department (MCM)

2017

Liquidity Management and Preparations for Introducing Repurchase Operations
Internal Audit and Risk Management

Regulation and Functioning of the Interbank Foreign Exchange Market (AFS)
AFS: Liquidity Forecasting and Management
AFS: Monetary Policy Implementation and Money Market
Regional Seminar on Banking Supervision
Regional Seminar on Regulation and Supervision of Institutions and Activities linked to Payment Services and Electronic Money

2018
Modernizing the Forex Regulations to Develop the Forex Markets (with LEG)
New banking Law
AFS: Preparation of RBS manual
Business Survey
Regulation and Banking Supervision
Regional Seminar on Risk-Based Supervision

2019
Adoption of IFRS
FX operations FX policy implementation (HQ and/or AFS, planned)
Insurance regulation and supervision (planned AFS)
AFS: Peer-Learning program for Transitioning from Money Targeting to an Interest Rate Based Framework

Statistics Department (STA)
2017
AFS: National Accounts
Balance of Payments Statistics (HQ)
AFS: Price Statistics
AFS: Prices and Index Numbers

2018
AFS: National Accounts
AFS: Price Statistics (work-at-home)
AFS: National Accounts: compilation of quarterly GDP
AFS: Consumer Prices/Producer Price - Disseminate data and metadata (PPI)
Money and Banking Statistics Mission
External Statistics

2019
AFS: National Accounts
Implementation of the e-GDDS, launch of the dedicated web page.

Resident Representative:
Mr. Marc Gérard is the IMF's Resident Representative in Antananarivo since August 2018.

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

World Bank: https://www.worldbank.org/en/country/madagascar

African Development Bank: https://www.afdb.org/en/countries/southern-africa/madagascar

STATISTICAL ISSUES

(As of December 2019)

I. Assessment of Data Adequacy for Surveillance
General: Data are broadly adequate for surveillance and program purposes, with shortcomings being addressed gradually. A new statistics law, modernizing and regulating data collection, was enacted in April 2018. There has been an effort to improve the compilation of timely and internally consistent data, including better information sharing between data producing and collecting agencies. Overall, there is a lack of automation, centralization and specialization which leads to inefficient and ineffective practices.
National accounts: Revised series of annual national accounts for the 2007-2018 period with the base year 2007 based on SNA 1993 methodology were finalized and published. INSTAT started to produce experimental quarterly GDP estimates that will be disseminated at end-June 2020. The authorities continue to receive TA from the Fund, World Bank, and AFRITAC in completing a 2018 base year rebased GDP. A general census of the population and housing is being finalized. In 2019, INSTAT conducted a Household Budget Survey that will be used to update household consumption of GDP series. **Prices statistics**: As of May 2019, INSTAT is producing a reweighted consumer price index (CPI) with 2016 as base year, to better account for current consumption patterns. The new series are available on a timely basis. Efforts are underway to extend geographic coverage and add new products to the basket. Compilation of producer price index (PPI) is ongoing but funding for the survey is uncertain.
Government finance statistics: Authorities are planning to gradually extend the statistical coverage from the central government to the general government, including local authorities and national public establishments.
Monetary and financial statistics: The Banky Foiben'i Madagasikara (BFM) is finalizing the adoption of International Financial Reporting Standards (IFRS) that will strengthen the transparency and credibility of BCM's financial reporting practices. The BFM consolidated the sectoral balance sheets by expanding the coverage of the monetary statistics to include microfinance institutions (MFIs) and Caisse d'Epargne de Madagascar (CEM), a public financial institution which collect deposits, so that the full depository corporations survey may be calculated. In 2018 the consolidation of balance sheets of larger micro-financial institutions and the CEM in the preparation of the monetary survey. **Financial soundness indicators (FSIs)**: A broad range of information on the financial sector, including both core and a number of non-core FSIs, is compiled by the BFM.

Balance of payments: The BFM (BFM) has made commendable progress in the improvement of external sector statistics data collection and compilation. The quarterly data are compiled on the basis of the ESRI and should be supplemented by the collection of quarterly data using a simple survey of major public and private enterprises. The annual surveys, which have much broader coverage and detail, will be used to revise the quarterly data. The choice of data sources is based on the availability principle, no comprehensive overview is applied to ensure that composition of data sources for the IIP purpose provides for sufficient IIP scope and coverage. The compilation system is still hampered by such recurring issues as excessive processing lags due to partial automation of customs reports and inadequate coverage of several transactions.

External debt: The compilation of external debt statistics is generally satisfactory. Private debt data coverage remains incomplete. The authorities are working to reduce debt data gaps as they improve various components of external sector statistics by drawing on IMF technical assistance.

II. Data Standards and Quality

Participant in the enhanced General Data Dissemination System (e-GDDS) since April 2017. As of April 2019, Madagascar launched a web-based National Summary Data Page.	No Data ROSC.

National Accounts Rebasing

In August 2019, Madagascar officially adopted an improved series of national accounts based on: (i) the 1993 System of National Accounts (SNA93) compilation methodology; (ii) a change in the base year from 2000 to 2007; and (iii) use of expanded data sources and surveys. As a result, the national accounts statistics now capture a larger part of the economy than before, leading to an increase of about 16 percent in the size of the economy.

The rebased GDP reflects use of a new standard (SNA93) and a new base year (2007). In the process of switching from SNA68 to SNA93, Madagascar benefited from a multi-year program of intensive technical assistance from AFRITAC South.[1] New and more robust series have been compiled for 2007-2017, as well as for 2018 on a preliminary basis[2]. The year 2007 was chosen as the base year since in that year there were no major shocks or distortions, and because of available household survey data. The revised GDP series incorporate broader coverage of the economy based on new household surveys, improved enterprise surveys, agricultural census, and an informal sector survey. The new methodology attributes higher weights to the primary sector, though the tertiary sector (trade, services and public administration) still dominates the economy (followed by the secondary) and accounted for most of the nominal GDP increase.

The revised GDP data resulted in upward adjustment of about 16 percent. While the distribution of GDP between primary, secondary and tertiary sectors shows some limited changes, the GDP is re-evaluated upward significantly, by 17.8 percent in 2007, by about 19 percent on average over the 2007-2014 period, and by 12 percent on 2016 (Fig. 1). The main explanations for the nominal GDP increase are:

- The implementation of the SNA93 methodology, which accounts for auto-consumption in addition to sales of agricultural goods. The inclusion of imputed rents accounts for 4.9 percent increase in the new GDP.
- The inclusion of the consumption of fixed capital accounts for another 6.5 percent increase.
- The inclusion of financial intermediation services by banks and micro-finance organizations account for another 0.9 percent increase.
- The inclusion of wood used for heating and cooking purposes accounts for another 1.5 percent increase.
- Significant improvements in agricultural sector based on the 2005 census. New products were added, while some products were reclassified between primary and secondary ones. For

[1] This technical assistance included: hand-on-training; use of appropriate statistical techniques, including dealing with data sources and or assessment of intermediate data; software upgrade; data compilation using the concepts and definitions of the manual; developing appropriate methodologies and choosing a base year; improving the legal framework; robustness tests, validation and quality assessments of compiled data; data dissemination and publication.

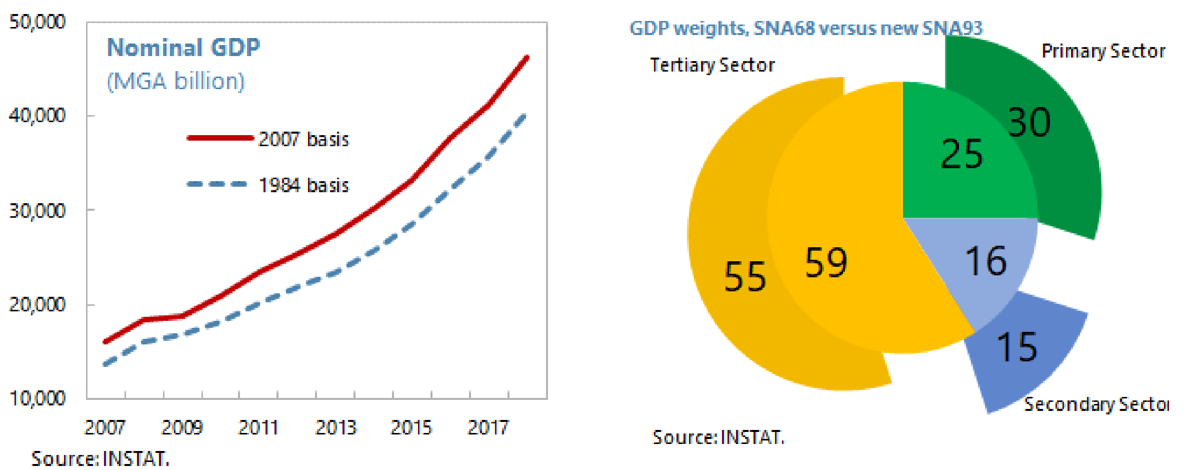
[2] The new series of National Accounts statistics were produced by INSTAT, the National Statistical Institute, with the support of the World Bank and IMF AFRITAC South.

example, green vanilla is produced and classified in primary sector, while its transformation, the exported vanilla, is part of the secondary one.

- Disaggregation of sectors, for example public administration now is separated from education and health. Overall data was expanded from 25 to 33 sectors.
- Introduction of new products and services related to information technology and telecommunication.
- Use of double deflators, CPI and PPI, as opposed to only CPI in the past.

Associated changes for real GDP growth were limited to a small downward revision in 2018 (from 5.2 to 4.6 percent) and another in 2019 (from 5.2 to 5.0 percent).

Figure 1. Madagascar: Rebasing of National Accounts



The impact of the revised GDP series on program monitoring is minimal. Starting in September 2019, both the IMF team and Madagascar authorities switched to the new rebased GDP to prepare the 2020 budget. Using the new GDP data in the macro-framework will impact the main economic ratios expressed as a percentage of GDP. On the positive side, the revisions imply a more favorable debt to GDP ratio and greater potential to increase fiscal revenues. On negative side, the rebasing of GDP reduced the already low tax revenue-to-GDP ratio (10.5 percent of GDP in 2018), confirming the large size of the informal sector). Nevertheless, this does not change the targets for the authorities' program supported by the ECF arrangement, as all quantitative targets are expressed in nominal terms.

Madagascar: Table of Common Indicators Required for Surveillance
(As of December 6, 2019)

	Date of latest observation	Date received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]
Exchange Rates	Dec. 2019	Dec. 2019	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	Nov. 2019	Dec. 2019	M	M	M
Reserve/Base Money	Nov. 2019	Dec. 2019	M	M	M
Broad Money	Oct. 2019	Dec. 2019	M	M	M
Central Bank Balance Sheet	Nov. 2019	Dec. 2019	M	M	M
Consolidated Balance Sheet of the Banking System	Oct. 2019	Dec. 2018	M	M	M
Interest Rates[3]	Nov. 2019	Dec. 2019	M	M	M
Consumer Price Index	Oct. 2019	Dec. 2019	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[4] – General Government[5]	NA				
Revenue, Expenditure, Balance and Composition of Financing[4] – Central Government	Oct. 2019	Dec. 2019	M	M	A
Stocks of Central Government and Central Government-Guaranteed Debt[6]	2018	Mar. 2019	A	A	A
External Current Account Balance	Mar. 2019	Sep. 2019	Q	Q	Q
Exports and Imports of Goods and Services	Nov. 2019	Dec. 2019	Q	Q	Q
GDP/GNP	2018	Jun. 2019	A	A	A
Gross External Debt	Mar. 2019	Sep. 2019	Q	Q	Q
International Investment Position[7]	Dec. 2018	Jun. 2019	Q	Q	Q

[1] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

[2] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[3] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[4] Foreign, domestic bank, and domestic nonbank financing.

[5] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[6] Including currency and maturity composition.

[7] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

Statement by Mr. Raghani, Executive Director for Madagascar, and
Mr. Nguema-Affane, Senior Advisor to Executive Director
January 29, 2020

1. Our Malagasy authorities thank Executive Directors, Management and staff for their continued support to Madagascar in implementing their reform program supported by the ECF arrangement. They are particularly thankful for the candid discussions with staff held in Antananarivo in the context of the sixth and final review of the program. The report gives a good account of these discussions. The Malagasy authorities are also grateful for the timely technical assistance provided to support their reform efforts. Likewise, we welcome the *Selected Issues* paper which highlights issues of interest for the authorities as the national development plan is being finalized.

2. Program implementation during the period under review has been strong. All the performance criteria for end-June 2019 were met. All but one indicative targets at end-June 2019 were respected. The structural reforms advanced despite some delays related to the electoral period and the installation of the new Parliament. Overall, there has been significant progress towards the ECF-supported program which aimed to strengthen macroeconomic stability, promote inclusive and sustainable growth, and reduce poverty. Going forward, the Malagasy authorities will pursue prudent macroeconomic and structural policies in the context of their ambitious medium-term national development plan, *Plan Emergence Madagascar (PEM)*, to address economic, social and climate change challenges facing the country. In addition, the authorities have formally expressed their interest in a successor arrangement to support the implementation of the PEM.

3. In light of the strong achievements under the program and their continued commitment to pursue prudent policies beyond the current arrangement, our authorities are requesting the completion of the sixth and final review of the Fund-supported program under the Extended Credit Facility.

I. Recent developments and outlook

4. **Macroeconomic conditions improved in 2019**. Economic activity accelerated in the second half of 2019 following a slight slowdown in the first half of the year due to delayed budget execution and the private sector’s wait-and-see attitude during the election period. Growth increased from 4.6 percent in 2018 to 4.8 percent in 2019. Inflation declined from 6.9 percent in 2018 to 6.0 percent in 2019. External position remains broadly positive despite a current account balance estimated to have turned negative in 2019 due mainly to lower commodity exports. International reserves have continued to grow and stood at 4.3 months of imports. Fiscal deficit at end-June 2019 was better than programmed, owing to increased revenue mobilization and budget under-execution in the first half of 2019, which notably affected execution of social spending.

The updated debt sustainability analysis (DSA) shows that overall risk of debt distress remains moderate and the risk of external debt distress is still low. The central bank (*Banky Foiben'i Madagasikara*, BFM) continued to successfully manage the volatile liquidity in a banking system which remains profitable, well capitalized, and liquid.

5. **The macroeconomic outlook continues to be favorable.** The *Plan Emergence Madagascar* seeks to further ameliorate macro-economic prospects, including by accelerating economic growth driven by higher private sector activity and the ongoing scaling up of public investment. The PEM assumes a gradual increase in real GDP growth from 4.8 percent in 2019 to 5.5 percent in 2020 and to 7 percent in 2023. These projections, which are higher than those in the current ECF arrangement, are based on improvements in both the quality and quantity of public investment in infrastructure, and on rising private sector activity, especially tourism, light manufacturing (e.g., textiles), mining, and agriculture. Inflation is projected to remain subdued over the medium term and a deterioration of the current account expected owing to higher public investment. The authorities agree with staff assessment of downside risks to the outlook, including a slowdown in public investment execution and terms-of-trade shocks. However, they believe that, given the greater political stability and higher private sector confidence following the election period, a substantial portion of announced investment projects could materialize more rapidly than forecast.

II. Program performance

6. **All performance criteria for end-June 2019 were met. Four out of the five indicative targets at end-June 2019, including the one on tax revenue, were also achieved.** As expected at the time of 5th review, the end-June 2019 indicative target on increasing social spending was not met due to the late adoption of the 2019 revised budget, but it has picked up significantly since then. Progress in the implementation of the structural reforms monitored in the program continued. Four of the eight remaining structural benchmarks (SBs) were completed albeit one, the submission of the banking law to Parliament, was implemented with delay. As regard the remaining four SBs, the draft law on financial stability has been prepared and is being reviewed by the Council of Ministers, before its submission to Parliament. The use of the new Tax Identification Number is completed in the major ministries and is being expanded to all ministries. In the context of severe electricity shortages in the capital city and to ensure the continuity of fuel supply to JIRAMA, the public utility company, one single source contract for fuel supply has been signed in August 2019 without prior notification to Fund and World Bank staff, thereby failing to observe the related continuous benchmark. With this exception, the practice of single source contracts in use until 2016 has been eliminated. Residual uncertainties on the application of the reference price structure delayed the implementation of the automatic fuel pricing mechanism, now scheduled for March 2020. However, no fuel subsidies have been paid since the implementation of the revised fuel price structure in June 2019.

III. Policies for 2020 and beyond

7. **The authorities are determined to address Madagascar's development challenges stemming notably from its fragile situation, high poverty rate, and vulnerabilities to natural disasters and terms of trade shocks.** To this end, the PEM targets (i) higher and sustained economic growth, based on the mobilization of tax revenues and the prioritization of spending, particularly towards investment; (ii) more inclusion, supported by strengthened social policies and spending, with the objective of reducing poverty and a better access to education, health, and housing; and (iii) better governance and institutions. The authorities will focus on gradually enhancing the productivity of smallholder agriculture and developing export-oriented agribusiness to support inclusive growth. The reform agenda puts a special emphasis on completing reforms initiated during the ECF arrangement, notably those related to JIRAMA, fuel pricing and financial sector stability. Continued donors' financial and technical assistance will be crucial to achieving these medium-term objectives. The recent assessments of debt sustainability are supportive of the authorities' plans to increase borrowing to finance higher public investment.

Growth-Friendly and Inclusive Fiscal Policy

8. **The authorities will pursue a prudent fiscal policy consistent with the objectives of the PEM.** In particular, fiscal policy will continue to focus on pursuing domestic revenue mobilization efforts and streamlining non priority spending to create fiscal space required for priority investment and social spending. The recently-adopted budget for 2020 is in line with those objectives. It targets achieving a fiscal primary surplus in 2020. Tax revenue is expected to increase with ongoing improvements in tax and customs administrations, and new tax measures included in the budget law. The composition of expenditure will shift towards priority investment and social spending through the rationalization of current outlays, notably transfers. Although picking up in 2020, the wage bill will be contained at a sustainable level over the medium-term with notably the modernization of the payroll management. Priority social spending is projected to augment steadily over the medium-term, with enhanced monitoring and social programs. Public investment will increase significantly in 2020 and over the medium-term to address infrastructure gaps. Moreover, the authorities will continue, with the support of development partners, their efforts on the identification, monitoring and, where possible, mitigation of fiscal risks, including those related to state-owned enterprises (SOEs), especially JIRAMA, PPPs or the deficit of the public pension fund. They are ready to implement contingency measures if revenue assumptions do not materialize, while protecting social and investment priority spending. These measures would be part of a revised budget law.

Enhancing Economic Governance and Fighting Corruption

9. **The authorities remain resolved to sustain their ongoing efforts to enhance public financial management, improve governance and transparency and reduce corruption vulnerabilities**. In this regard, as extensively described in the MEFP, they will fully enforce the public financial management and anticorruption reform legislations approved during the program period. In particular, measures to strengthen budget preparation, public procurement, public investment management, treasury management, fiscal risk management and debt management in the context of the updated 2018-2026 Strategic Plan of Modernization of Public Financial Management and the 2018-2020 Action Plan will be implemented based on the recommendations of technical assistance missions. In addition, the implementation decrees of the 2016 anti-corruption law and 2019 AML/CFT law will be issued in early 2020. Moreover, improvement in transparency is continuing with increasing publication of institutional activity reports, notably from the institutions in charge of enforcing the anti-corruption framework. The authorities are of the view that pursuing progress in those areas is essential to improve the business climate and stimulate both domestic and foreign investment.

Maintaining Stable Inflation and Building External Resilience

10. **The authorities remain committed to price stability in the context of a flexible exchange rate regime, while pursuing a gradual monetary policy transition from monetary aggregates targeting to interest rate targeting policy**. Consistent with the price stability objective, the BFM will continue to closely monitor potential inflationary pressures and actively manage bank liquidity, in order to maintain an appropriate policy stance. It is also strengthening its monetary policy framework to improve the effectiveness of the interest rate transmission channel with the revision of the short-term interest rate corridor and the preparation of legislations on repo transactions and collateral to be submitted to Parliament in 2020. The central bank will also continue to build international reserves, consistent with its mission to safeguard external stability. The long-term objective is to gradually increase import coverage to 6 months or more. The BFM's modernization is continuing, with a reform agenda to increase transparency and to enhance its financial independence. The central bank remains committed to full adoption of International Financial Reporting Standards (IFRS) for the 2020 accounts.

Building a Sound Financial Sector Supporting Economic Development

11. **The authorities will continue to reinforce financial stability while promoting greater access to financial services.** Pending the Parliament approval of the banking law, the authorities will prepare the related implementation text in accordance with international standards and FSSA recommendations. The law on financial stability is expected to be submitted to the Parliament in 2020. The authorities will also approve updated prudential directives by end-June 2020 on capital adequacy, liquidity,

concentration of risks, and classification and provisioning of credit risks, also in line with international standards and FSSA recommendations. A revised law to improve the functioning of the foreign exchange market, prepared in consultation with the banking sector and the support of the Fund, is expected to be presented to the Parliament in May 2020. As regard financial inclusion, the authorities have partnered with a local bank and a mobile phone operator to launch the KRED Initiative, a mobile digital platform to provide financing to micro and small enterprises in the context of the *Fihariana* program, and they are very encouraged by its early success. Progress is being made in the implementation of action plans regarding the restructuring of two public financial institutions, the *Caisse d'Epargne de Madagascar* (CEM) and *Paositra Malagasy* (PAOMA), which have the potential to improve access to financial services.

IV. Conclusion

12. The implementation of the ECF-supported program has been strong, which demonstrates the Malagasy authorities' continued commitment to sound policies and reforms. Going forward, the authorities are determined to pursue their reform program agenda with a view to address economic, social and environmental challenges facing Madagascar. In this regard, they are contemplating a successor arrangement to support the implementation of the *Plan Emergence Madagascar*. In light of the above, we would appreciate Executive Directors' favorable consideration of the Malagasy authorities' request for the completion of the sixth and final review of the ECF-supported program.