

Chad: 2001 Article IV Consultation, Third Review Under the Second Annual Program Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Requests for Augmentation of Access and for Waiver of Performance Criteria—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Chad

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the combined discussion of the 2001 Article IV Consultation with Chad and Third Review Under the Second Annual Program Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Requests for Augmentation of Access and for Waiver of Performance Criteria, the following documents have been released and are included in this package:

- the staff report for the 2001 Article IV Consultation, Third Review Under the Second Annual Program Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Requests for Augmentation of Access and for Waiver of Performance Criteria prepared by a staff team of the IMF, following discussions that ended on **November 13, 2001**, with the officials of Chad on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on December 21, 2001.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- the Public Information Notice (PIN) summarizing the **views of the Executive Board as expressed during its January 16, 2002 discussion** of the staff report that concluded the Article IV consultation.
- a statement by the Executive Director for Chad.

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

Letter of Intent sent to the IMF by the authorities of Chad*

Memorandum of Economic and Financial Policies by the authorities of Chad*

*May also be included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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CHAD

Staff Report for the 2001 Article IV Consultation, Third Review Under the Second Annual Program Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Requests for Augmentation of Access and for Waiver of Performance Criteria

Prepared by the African Department

(In consultation with Fiscal, Legal, Monetary and Exchange Affairs, Policy Development and Review, Statistics, and Treasurer's Departments)

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December 21, 2001

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EXECUTIVE SUMMARY

- Chad has had a reasonably good year in 2001, reversing the policy slippages in 2000. Economic performance, including in the area of governance, has improved measurably. Growth prospects are also good, with real GDP projected to grow at an annual rate of 10 percent in 2001–03. While the main reason is the acceleration of the construction of the Chad-Cameroon pipeline, structural reforms and improving governance have also played a role.
- In the short term, the main area of concern is revenue performance, on which most of the program measures focus. Key will be the implementation of the action plan, based on the findings of the international audit of customs.
- In the longer term, Chad faces two main challenges in the run-up to the petroleum era. First, it should avoid the development of a dual economy, with the oil sector segregated from the rest of the economy; accordingly, actions have been identified to foster a fuller integration of the oil economy in the areas of training, banking, and information sharing with domestic economic agents. Second, Chad must strengthen domestic institutions so as to prepare for the effective absorption of oil revenues, in accordance with laws guiding the equitable distribution of Chad's oil wealth.
- Chad has been hit hard by a decline in the world market price for cotton, its main export commodity. Projections for 2002 indicate a significant uncovered balance of payments need, for which the government seeks additional support from the international community, including the Fund, in the form of an augmentation of access to PRGF resources by 10 percent of quota.
- The authorities have prepared their PRSP preparation status report, which is subject to a joint staff assessment by the Fund and the World Bank in a separate document. Overall, the participatory process has been exemplary and the draft PRSP fully homegrown. The authorities expect to finalize the PRSP by March 2002.
- The staff appraisal urges the authorities to build on the policy momentum and highlights the need for a rapid and full implementation of the revenue measures included in the 2002 budget. Further improvements in expenditure management and governance are also needed to consolidate progress and press ahead with institution building, for which the authorities request additional technical assistance. Finally, the staff appraisal supports the authorities' request for an augmentation of access to PRGF resources to make up for part of the revenue loss arising from the cotton sector crisis.

I. INTRODUCTION

1. Discussions on the 2001 Article IV consultations and the third review under the Poverty Reduction and Growth Facility (PRGF) arrangement, as well as on the authorities' poverty reduction strategy paper (PRSP) preparation status report were held in N'Djaména during October 31–November 13, 2001.¹ A three-year arrangement under the PRGF was approved on January 7, 2000 in an amount equivalent to SDR 36.4 million (65 percent of quota). At the time of the second review, on May 16, 2001, this amount was augmented by SDR 5.6 million (10 percent of quota) to address emergency food import needs.²

2. On the occasion of the discussion of the 2000 Article IV consultation on July 25, 2000 (EBS/00/133; 7/10/00), Executive Directors welcomed the authorities' efforts to keep the program on track through the first half of 2000, while urging them to strengthen expenditure control and accelerate structural reforms. The Executive Board concluded the second review of the PRGF arrangement on May 16, 2001. Executive Directors noted the authorities' efforts to introduce a series of measures to improve transparency and governance, while bringing the PRGF-supported program back on track, after policy slippages that occurred in the second half of 2000. They stressed the need for further enhancing governance, and strengthening revenue mobilization and expenditure management. At the same time, Chad reached its decision point under the Enhanced HIPC Initiative, which entailed a debt relief of about US\$170 million in net present value (NPV) terms. In June, the Paris Club provided a flow debt rescheduling of Chad's external debt on Cologne terms. On September 28, 2001, the Executive Board approved, on a lapse of time basis, the evaluation of Chad's performance at end-June 2001 (EBS/01/170; 9/25/01).

¹ The mission met with President Déby, Prime Minister Yamassoum, Minister of Finance Idriss, the National Director of the Bank of Central African States (BEAC), and other senior officials. The staff team consisted of Ms. Nagy (Head-AFR), Mr. Karangwa, Mr. Dauphin, and Ms. Jagatsing (Assistant) (all AFR). Ms. Allain, Resident Representative for Chad, also participated in the mission. Mr. Donovan (AFR) joined the policy discussions for a couple of days. Mr. Nyambal, Advisor for the Executive Director for Chad, participated in several policy discussions. The representatives of the World Bank's local office participated in many of the meetings.

² Chad's outstanding use of Fund resources amounted to SDR 71 million (equivalent to 126.8 percent of quota) as of November 30, 2001. Chad has accepted the obligations of Article VIII, Sections 2, 3, and 4 effective June 1, 1996, and the exchange system remains free of restriction on payments and transfers for current international transactions.

3. In the attached letter of December 20, 2001 (Appendix I), Prime Minister Yamassoum and Finance Minister Idriss review developments under the program in 2001 and request waivers for the nonobservance of the performance criteria at end-September 2001 on (i) total fiscal revenue; (ii) the nonaccumulation of external payments arrears; and (iii) the preparation of the audit of the use of the bonus as of December 31, 2000 (the latter measure was implemented with a few weeks of delay). The letter also sets out the government's policies for 2002, for which the government of Chad seeks the Fund's support in the context of a second annual program under the PRGF arrangement. Chad also requests an augmentation of the PRGF arrangement by an amount equivalent to SDR 5.6 million, representing 10 percent of quota to help cover the additional balance of payments financing need resulting from the decline in the world market price of cotton, Chad's main export commodity.³

II. PERFORMANCE UNDER THE PROGRAM IN 2001

4. **Overall, the Chadian economy had a reasonably good year in 2001, clearly reversing the policy slippages of 2000.** Fiscal policies have returned to a more prudent path, structural reforms have advanced broadly as programmed or even accelerated,⁴ and past slippages in transparency and governance have been corrected. In the latter regard, the audit of the use of the oil bonus by the General Auditor's Office of the Supreme Court, undertaken in line with international standards and with commendable objectivity and frankness, represented an important milestone.

5. **These achievements have been made against the backdrop of a worsening external environment.** First, Chad was hit hard by extreme weather conditions during the 1999/2000 agricultural season, with parts of the country brought to the brink of famine. With prompt assistance from the international community—including from the Fund in the form of an increase in PRGF access—famine has been averted. Second, there was a substantial shortfall in external financing, amounting to CFAF 30 billion (equivalent to some 3½ percentage points of GDP) at end-September, making the timely implementation of the

³ Summaries of Chad's relations with the Fund and the World Bank Group are contained in Appendices II and III, respectively. Structural reforms supported by the World Bank are discussed in Appendix IV, and a summary of progress toward meeting the HIPC Initiative completion point conditions is presented in Appendix V. Finally, statistical issues are presented in Appendix VI.

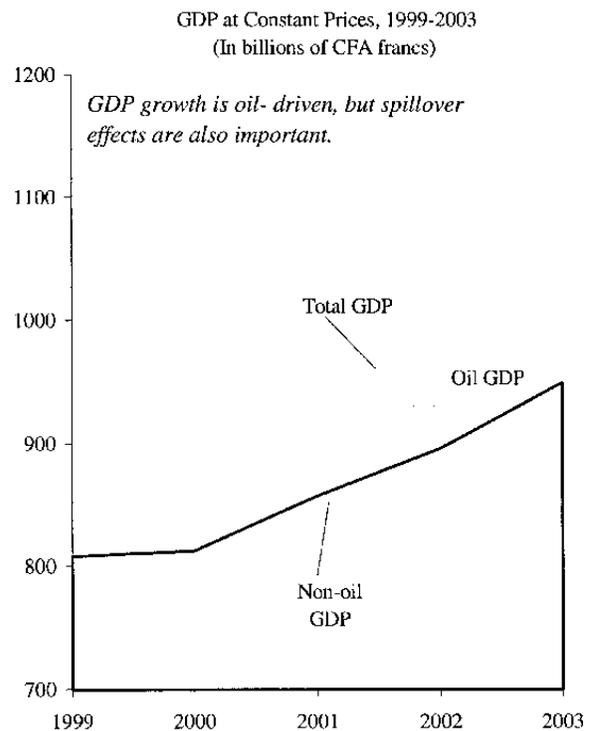
⁴ The World Bank's Fourth Structural Adjustment Credit (SAC IV) for Chad, approved on December 18, 2001, states that structural reforms have been accelerated in the areas covered by the Bank's conditionality (IDA/R2001-0188).

budget increasingly difficult.⁵ Third, sharp recent declines in the world market price of cotton, Chad's main export commodity, have started to exert a negative impact, although the brunt of the blow is expected to be felt in 2002.

6. **Notwithstanding the overall progress, advances in certain areas have been slower than programmed.** First, revenue collection, while on track through the first half of the year, weakened in the third quarter. Weak administrative capacity, including constant staff turnover at all levels of the administration and persistent problems at customs, appears to be the main reason; a shortfall in taxes from the state cotton company, Cotontchad, also played a role. Second, progress in governance has been constantly challenged by pressures from vested interests to conclude business deals in the energy sector that may not be in the global Chadian interest. The delay in implementing the measure concerning energy sector taxation and pricing policy (a structural benchmark at end-September) may have also been related to these pressures.

7. **Overall economic results in 2001 have been broadly satisfactory:**

- **Real GDP** growth is now projected to reach about 9 percent in 2001, compared with 8 percent targeted under the program, thanks mainly to the acceleration of the construction of the Chad-Cameroon pipeline. Structural reforms—such as the liberalization of domestic petroleum prices and privatization—have also played a role.
- **Consumer prices** increased by 14 percent on average in the year ended October 2001, reflecting mainly the impact of food shortages related to last year's drought; prices have declined since September as food supplies have improved. In addition, strong oil sector-related demand may have also put some



⁵ The delay was explained by slower-than-expected disbursement procedures of the European Union, and the latter's possible hesitance to disburse approved loans following alleged irregularities during the May 2001 presidential elections. In addition, the above-mentioned World Bank's SAC IV was approved in December 2001, somewhat later than originally envisaged.

pressure on prices. At the same time, **broad money** grew by 12 percent.

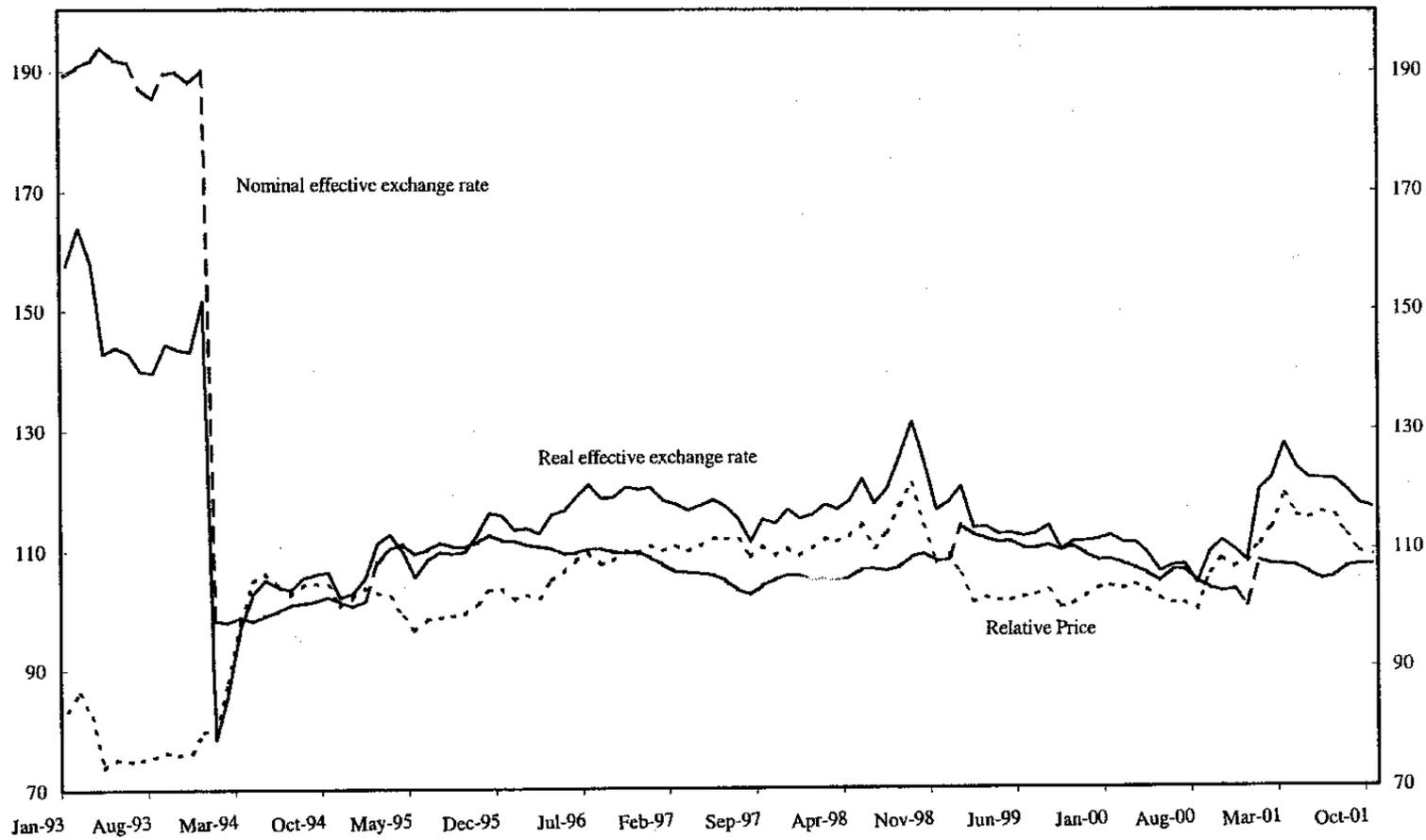
- **The primary current fiscal deficit** (excluding spending on elections and on food emergency) reached about 0.6 percent of GDP at end-September 2001, somewhat less than programmed. There are, however, two main areas of concern: (i) the above-mentioned shortfall in revenues; and (ii) a somewhat unfavorable expenditure structure, with defense spending slightly higher than envisaged and expenditure on social sectors lower than programmed. The higher defense spending reflected increased rebel activity in the north, while the lower-than-programmed expenditure was due to a delay in social sector spending by the Poverty Fund. This delay in turn was the consequence of both a slowness in finalizing agreements with Paris Club⁶ and non-Paris club bilateral creditors, and in making the body overseeing the spending of oil-related revenue operational.⁷ Against the backdrop of the shortfall in external financing, the government accumulated domestic payments arrears (about 1 percent of GDP), as well as a small amount of external arrears.
- **The external current account deficit** (excluding official transfers) is projected to widen from 16 percent of GDP in 2000 to 42 percent in 2001, somewhat higher than programmed, owing to higher imports related to the exploitation of Chad's two oil fields. The current account deficit is being financed by foreign direct investment and official loans. Net official foreign exchange reserves increased in the third quarter to reach CFAF 18 billion, partially reversing a decline in the first half of the year.
- Until the beginning of 2001, Chad managed to maintain much of its gains in external competitiveness following the devaluation of the CFA franc in 1994. A worsening in the Consumer Price Index (CPI)-based real effective exchange rate (REER) indicator in the first half of the year is now starting to be reversed as food price inflation abates (Figure 1).
- According to the Central African Banking Commission (COBAC), the **financial sector's health has remained good**, with all but one bank complying with the main prudential ratios at end-June 2001. This bank has received a capital injection from its private owner, thereby improving its solvency. Microfinance has expanded (albeit from a very small base), with most of the operations catering to demand by women heading small businesses (the repayment record has been an impeccable 100 percent during the last 12 months).

⁶ Owing to factors outside the Chadian authorities' control. The Paris Club Secretariat has recently notified Chad that the deadline to negotiate the bilateral debt rescheduling agreements was extended to March 31, 2002.

⁷ Resources of the virtual Poverty Fund are derived from two sources: interim external debt relief under the HIPC Initiative, with the remainder from the oil bonus (for details, see EBS/01/64, para. 20).

Figure 1. Chad: Effective Exchange Rate and Relative Price, January 1993–October 2001

(Index 1994 = 100)



- **Governance has considerably improved.** In addition to the completion of the audit of the use of the oil bonus⁸ (albeit with a few weeks delay), the preparation of the international audit of the customs⁹ as well as that of the five largest public procurement contracts is proceeding as scheduled. After an intense policy dialogue between the Bank and the Fund staffs and the authorities in the context of the enhanced program monitoring, some potentially damaging developments in governance relating to the energy sector have been averted.¹⁰
- **Structural reforms** have also proceeded broadly as programmed. A series of fiscal structural measures were completed. In the area of revenues, the value-added tax (VAT) administration has improved, with technical assistance from the Fund; the SYDONIA system for computerizing the customs database has been installed in the N'Djaména customs offices; the assignment of tax identification numbers (TIN) to all identified economic agents has been completed, and firms without TINs are now excluded from public procurement bidding, as well as from any government supply orders. In the area of expenditure management, good progress has been made: the new procedural handbook on the streamlined expenditure circuit and the first quarterly bulletin on public procurement have been published; public expenditure reviews (PERs) have been prepared for the health and education sectors; and a number of inactive government accounts have been closed. In areas covered by World Bank conditionality (see Appendix IV), privatization has proceeded as planned, and the reforms of the civil service, procurement system, and the cotton sector have also advanced as scheduled. However, the guidelines for the determination of the taxation and pricing policy for Chad's second-largest oil and gas field, Sédigi, envisaged for end-September 2001, have not yet been adopted.

8. **In terms of performance criteria, Chad met all but two quantitative targets at end-September 2001** (Table 1). Performance criteria were met on (i) net credit to

⁸ The audit (i) confirmed the off-budget use of the oil bonus through the summer and early fall of 2000, at variance with Chad's laws and regulations; (ii) identified inconsistencies relating to the recording of the expenditures; (iii) indicated areas where further investigation was needed; and (iv) provided a set of recommendations for government disciplinary actions and follow-up.

⁹ Following a competitive bidding process, the auditing firm has been selected, and it is expected to start its work shortly.

¹⁰ Namely, the government has decided not to sign an unfavorable draft contract concerning the exploitation of the Sédigi gas resources, and it has requested additional technical assistance from the World Bank in this area.

government;¹¹ (ii) the current primary fiscal balance; (iii) new nonconcessional external debt with maturities of more than one year; and (iv) net change in external debt with a maturity of up to and including one year. The performance criterion on total fiscal revenue and the continuous performance criterion on the nonaccumulation of external arrears were not observed; the latter nonobservance was mainly due, as mentioned, to a shortfall in external financing. All external arrears have been cleared as of December 18, 2001. The completion of the oil bonus audit, a structural performance criterion at end-September, was satisfied with a few-weeks' delay. In addition, as mentioned, the structural benchmark relating to the Sédigi oil and gas field was not observed (Table 2).

Box 1: Structural Conditionality

Coverage of structural conditionality in the current PRGF-supported program

As indicated in Table 2 of the staff report and Table 2 of the authorities' MEFP (Appendix I), the structural conditionality of the current program focuses on (i) **governance** (audits of the use of the oil bonus, the customs administration, and of the five largest procurement contracts signed in 2001); (ii) **public expenditure management** (enhanced use of treasury cash plan; simplification and computerization of the expenditure circuit, elimination of off-budget operations, simplification of government bank accounts); (iii) **revenue measures** aimed at strengthening tax administration (particularly in the area of VAT, customs computerization, and distribution of taxpayer identification numbers); and (iv) **liberalization of domestic petroleum prices**.

Status of structural conditionality in the previous PRGF-supported programs

Measures that were programmed under the previous arrangement have been implemented, albeit some with delays (EBS/99/234, Appendix VI).

Structural areas covered by World Bank lending conditionality

As described in detail in Appendix IV, the World Bank's structural conditionality covers the following main areas: the reforms of the civil service, the procurement system, the cotton sector, as well as the government's privatization program. In addition, in a complementary manner, both the Fund and the World Bank have conditionality in the areas of governance and expenditure management.

Structural reforms covered by the HIPC Initiative completion point conditionality

Good progress has been made in several areas, including governance, budget cycle, health indicators, basic infrastructure. These are listed in Appendix V.

¹¹ Net credit to government reached CFAF 6 billion at end-September 2001, against an adjusted target of CFAF 15.7 billion. (The target was adjusted for the shortfall in external financing and the accumulation of domestic payments arrears, see Table 1).

III. REPORT ON THE DISCUSSIONS AND THE OUTLOOK FOR 2002

9. The discussions focused on five main topics:

- What are the reasons for the lackluster revenue performance, particularly against the backdrop of a brisk economic activity?
- What is the outlook for the Chadian economy for 2002 and beyond, particularly in light of the nearing petroleum era? What are the government's policy priorities for 2002, and how are these reflected in the 2002 budget? How much progress had already been made toward meeting the HIPC Initiative completion point conditions, and was the 2002 budget appropriately tailored to meet those conditions?
- What is the outlook for financial sector sustainability, regional integration, and trade liberalization within the monetary zone context?
- How advanced is the preparation of the fully participatory PRSP?

A. The Medium-Term Outlook

10. The Chadian authorities are cautiously optimistic about the economic prospects for 2002 and beyond. With oil sector-related investment being accelerated—oil now is expected to flow in early 2004, a year earlier than previously envisaged—**their primary concern is to ensure that Chad escapes the pitfalls of developing a dual economy**, namely, to avoid an industrial oil enclave with close connections to the outside world that is cut off from the country's non-oil economy. The staff shared the authorities' concern and discussed ways to foster a fuller integration of the ongoing oil pipeline construction and the Doba project into the Chadian economy. Certain factors indeed constituted a regrettable bias toward developing an industrial enclave, such as the tax-exempt status of the Doba project, which clearly favored tax-exempted imports by the oil consortium in charge of the Doba project¹² over domestically-provided supplies, which did not enjoy such tax benefits.

11. At the same time, other obstacles in the way of a stronger and more rapid integration were easier to overcome. First, the apparent shortage of skilled labor could be eased by training seminars, some in collaboration with the consortium. Second, domestic commercial banks could take more risks—reflected in the interest charged—in granting loans to creditworthy customers with credible orders from the consortium.¹³ Third, a concern not to

¹² The consortium consists of ExxonMobil, Chevron, and Petronas.

¹³ Banks thus far have been reluctant to lend to local businesses with large potential orders but small collateral bases. At the same time, microcredit institutions are planning to increase their operations in the Doba project area.

create shortages and price hikes by sharply increasing demand for local products in the context of the Doba project may need to be revisited to some degree. While the staff agreed that major domestic market disturbances needed to be avoided, in the absence of increased demand and its manifestation through relative price changes—and perhaps temporary price increases—local supply is not likely to be stimulated. The staff therefore suggested that the authorities and the consortium revisit this issue with a view to stimulating local supply by the consortium purchasing more products locally. Finally, the staff urged the authorities to start an information campaign, explaining to domestic economic agents the possibilities offered by the Doba project. In this regard, the staff welcomed the idea of private sector representatives to organize a tripartite conference with the representatives of the oil consortium, the government, and the private sector. The authorities endorsed this idea and asked for Fund and World Bank participation. **The staff also pointed out to the authorities another major challenge of the pre-oil-producing era, namely, that domestic institutional capacity must be rapidly developed**, so as to ensure the equitable and efficient use of the revenue once it starts flowing. The authorities assented to the staff's viewpoint that giving wide publicity to this challenge was equally important as part of the preparation for the oil era.

12. **The short-term outlook is somewhat dampened by the decline in the world market price for cotton**, Chad's main export commodity. The authorities are deeply concerned about these negative developments, both because of the impact on farmers' income and because they fear that the developments may, to some extent, undermine the ongoing reform of the cotton sector (Box 2 and Appendix IV). They also noted the adverse consequences of subsidies to cotton producers in some advanced economies. The projections of the staff, the World Bank, and the authorities point to an additional balance of payments financing need of about US\$24 million in 2002, a part of which will be covered by a further fiscal effort—through cuts in nonwage nonpriority spending. The remaining financing gap of about US\$17 million could be covered by assistance from the international community, including from the Fund in the form of an augmentation of the PRGF arrangement amounting to 10 percent of quota (equivalent to SDR 5.6 million) (see below).

Box 2. The Reform of the Cotton Sector

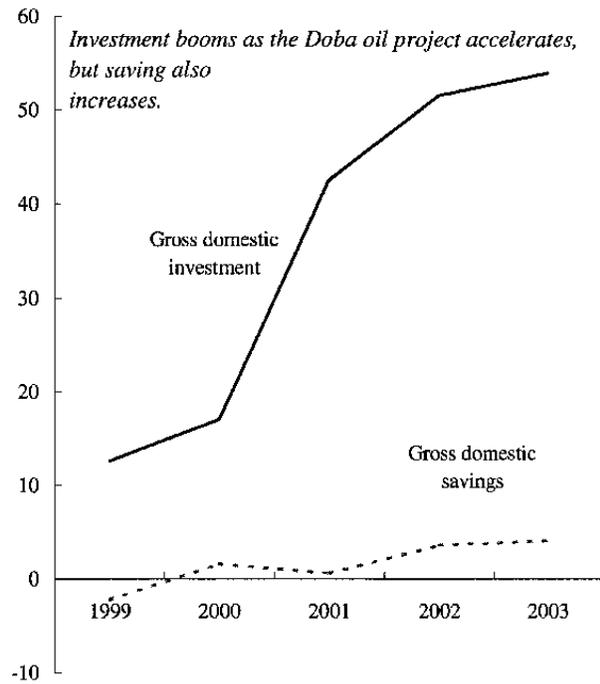
Since the beginning of 2000, Chad has embarked on a major reform of the cotton sector, aimed at changing the state determination of prices and liberalizing the sector. These reforms are covered by World Bank conditionality (Appendix V).

The pricing system was reformed in early 2000. Since that date, farmers' prices have been linked, through a predetermined formula, to world market prices. Nevertheless, the farmers still receive a low price; for example, in the 1999/2000, they received 49 percent of the lint equivalent world market price. At the beginning of the season (March/April) the farmers' associations agree with Cotontchad on the pre-planting price; actual prices in the following six months then serve as basis for an adjusted price at the end of the season (September/October). The difference between the pre-season agreed and the actual price is subsequently distributed/absorbed by Cotontchad and the farmers' associations.

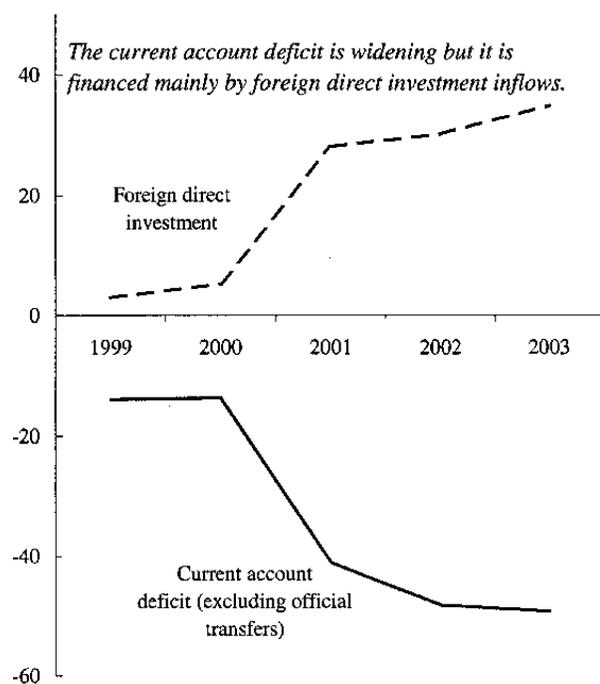
The sector's liberalization strategy involves the spinning off of the oil and soap component of Cotontchad (completed in November 2001), and the eventual privatization of these units as well as Cotontchad by mid-2003. In addition, the product market will be liberalized via a series of measures, such as the elimination of penteritorial pricing in 2002. The expected outcomes of these reforms are: (i) improved incentive system for farmers, increasing productivity, yields, and farmers' income; (ii) completion of the state divestiture from the cotton sector, leading to major efficiency gains.

13. On the basis of these discussions, the updated macroeconomic framework is predicated on the following assumptions: (i) the construction of the Chad-Cameroon pipeline will be completed by the end of 2003, a year earlier than programmed, and the Doba project will be integrated into the rest of the economy; (ii) prudent fiscal policies are maintained; and (iii) structural reforms are sustained, as discussed below. The terms of trade are projected to deteriorate in 2002 because a drop in the export price of cotton will more than offset the projected decline in oil import prices. Under these conditions, real GDP would grow by about 10 percent per annum in 2001–03 (Table 3). Cumulative per capita real growth would amount to about 17 percent in this period and start to make a dent in poverty in conjunction with increasing poverty-related spending. Foreign savings (excluding debt relief) will increase further as a result of the accelerated timetable for the Doba petroleum project that is almost entirely financed by foreign direct investment. As a share of GDP, foreign savings will increase to 42 percent in 2001, 49 percent in 2002, and 50 percent in 2003. Gross domestic savings will temporarily decline in 2001 before rising in 2002–03, as private savings increase in reaction to large increases in real income; government savings will also improve in 2003. Gross domestic investment is expected to rise sharply to 43 percent in 2001 and further to 52 percent and 54 percent in 2002 and 2003, respectively, owing to massive increases in private investment in the petroleum sector, as well as in construction.

Gross Investment and Savings, 1999-2003
(In percent of GDP)



External Developments, 1999-2003
(In percent of GDP)



14. **The economic landscape will change dramatically in 2004**, when oil production will start.¹⁴ Real GDP growth is projected at around 50 percent, boosted by oil exports. At the same time, investment growth will decelerate with the gradual completion of the Doba investment project, bringing about a fall in associated imports. As a result, the external current account balance, excluding grants, would swing from a deficit of 50 percent of GDP into a surplus of 15 percent of GDP. Debt sustainability will improve dramatically, with the external debt to exports ratio falling from 230 percent in 2003 to about 90 percent in 2004. Fiscal revenues are projected to double, reflecting the arrival of the oil revenue. Overall expenditures, and within it the share of poverty-reducing spending, will also increase, as some ¾ of total oil revenue will be used to finance priority sectors under the Law on Petroleum Management.

15. **The medium-term framework is broadly in line with that outlined in Chad's interim PRSP**, including sustained high rates of economic growth spearheaded by oil sector-related private investment in a low-inflation environment. Specific quantified targets have been changed somewhat from those envisaged in the interim PRSP to take account of the latest economic developments. These revisions, which are expected to be reflected in the macroeconomic framework prepared for the full PRSP, pertain mostly to higher real growth and wider current account deficit projections in 2001-03 stemming from the acceleration of the Doba project, and the associated dynamism of oil sector investment and its spillover effects.

B. Update for end-2001 and Key Elements of the Authorities' Program in 2002

Objectives

16. The staff has reached an understanding with the authorities on an update of the end-December 2001 targets and proposes to convert these into performance criteria and structural benchmarks. Two changes have been introduced. First, as mentioned, the target for revenue collection has been revised downward by CFAF 4 billion (0.3 percent of GDP), under the consideration that most of the agreed revenue measures would have their full impact only beyond December. Second, the target for net credit to government has been tightened to reflect essentially the expectation that not all of the US\$40 million budget financing from the World Bank's fourth Structural Adjustment Credit will be spent by end-December.¹⁵

¹⁴ The detailed projections for 2004 will be included in the staff report on the next PRGF review.

¹⁵ An associated modification in the adjuster to the performance criterion on net credit to government has also been introduced (see Appendix I, Attachment II).

17. Consistent with the above medium-term economic framework, economic policies in 2002 aim at achieving a real GDP growth of about 11 percent and reducing inflation to an annual average of 4 percent, bringing that rate in line with inflation rates elsewhere in the Economic and Monetary Community of Central Africa (CEMAC) zone.

The 2002 budget

18. **The authorities' fiscal policies in 2002 seek to increase public spending on poverty-reducing areas while maintaining a financeable budgetary position** (Tables 4 and 5). Accordingly, the 2002 budget allows for a widening of the current primary deficit from a projected 1.3 percent of GDP in 2001 to 1.5 percent of GDP in 2002, following increases in poverty-reducing spending and exceptional transfers to the crisis-hit cotton sector and the national water and electricity company (STEE). With an increase in the—almost exclusively foreign-financed—public sector investment of 6 percentage points of GDP, the overall fiscal deficit, on a commitment basis and excluding grants, will widen from 12.9 percent of GDP in 2001 to 19.3 percent in 2002.

19. **Fiscal revenue is targeted to increase from 7.8 percent of GDP in 2001 to 7.9 percent in 2002.** As much of the oil-related GDP is tax exempt, a better indicator for the revenue effort is the ratio of revenue to non-oil GDP, which shows a more substantial improvement of 0.6 percentage point of (non-oil) GDP (Table 6). This improvement will be achieved by the introduction of additional measures to enhance revenue collection, including, inter alia, measures based on the findings of the customs audit; the ex post verification procedures for tax-exempt imports under the Doba project; a reform of the system of taxing small taxpayers, and actions to reinforce cattle taxation, so as to bring part of the informal sector under the tax net (see para. 28, Box 3, and the authorities' Memorandum of Economic and Financial Policies (MEFP), Appendix I, paras. 6 and 13).

20. **The staff noted that revenue performance had weakened recently and that the near-term outlook for revenues remained precarious.** The Chadian authorities attributed their weakening revenue performance in large measure to weak administrative capacity, including high staff turnover and alleged irregularities at customs. They added, however, that other factors also played a role. First, reflecting the cotton sector's deteriorating performance, revenues from Cotontchad were below projections. Second, the Doba oil project had not benefited revenue collection to the extent that had been hoped for. While the project is fully exempted from import duties, the authorities had wanted to collect the two percent statistical fee on imports for the Doba project. However, the consortium has refused to pay it, claiming its tax-exempt status. The staff agreed with the authorities that a statistical fee, in principle, was a service fee and not a tax, and urged both parties to arrive rapidly at a mutually agreeable solution. The staff also expressed concern about the clear risk

Chad: Main Fiscal Trends, 2000–02
(In percent of GDP)

	2000 Est.	2001 Rev. Prog.	2002 Rev. Prog.	Change in 2002
	(A)	(B)	(C)	(C)-(B)
Overall fiscal balance 1/	-12.3	-12.9	-19.3	-6.3
Primary current fiscal balance	-0.9	-1.3	-1.5	-0.2
Total revenue	8.0	7.8	7.9	0.1
Total primary current expenditure	8.9	9.1	9.4	0.2
Baseline primary current expenditure 2/, 3/	8.8	7.9	7.6	-0.3
Exceptional outlays 4/	0.2	1.0	1.3	0.3
Poverty Fund financed	0.0	0.2	0.5	0.4
Investment	10.3	10.7	16.8	6.1
Baseline budget domestically financed 2/	1.1	1.2	1.4	0.2
Poverty Fund financed	0.0	0.2	0.9	0.7
Foreign financed	9.2	9.3	14.5	5.2
Memorandum items:				
Primary base balance 5/	-2.0	-2.7	-3.9	-1.1
Poverty-reducing spending 6/	10.6	11.2	15.8	4.6
Baseline budget spending 2/	10.6	10.8	14.4	3.6
Poverty Fund financed	0.0	0.5	1.4	1.0

1/ Commitment basis, excluding grants.

2/ Excluding spending financed by the Poverty Fund.

3/ Excluding exceptional outlays.

4/ Including outlays related to famine and elections and, in 2002, exceptional subsidies to the cotton and energy sectors.

5/ The base primary fiscal balance, a convergence indicator in the CEMAC zone, is defined as the current primary fiscal balance minus domestically financed investment.

6/ In 2002, excluding the exceptional subsidy to the cotton sector (0.8 percent of GDP).

of customs revenue losses as a result of the smuggling of noneligible imports under the Doba project's tax-exempt status. The authorities agreed and reiterated their commitment to remedy the evident weaknesses of customs collection, including through an independent audit of customs, whose preparation was under way, and the setting up of procedures for verifying ex post import tax exemptions. They also noted that, with the introduction of several other fiscal measures under the 2002 budget, revenue collection should improve.

Box 3. Chad: Revenue Measures

Fiscal revenue measures have been at the core of the PRGF-supported government program since its inception in January 2000. Nevertheless, while improvements have been made and revenue collection increased somewhat in real terms, these outcomes have fallen short of the program targets and are considered to be particularly weak against the background of a briskly growing economy. As a result, domestic fiscal revenues have remained below 8 percent of GDP, one of the lowest levels in the world.

While there are some objective reasons for this lackluster performance—weakening cotton sector performance, the tax-exempt status of much of the rapidly growing part of the economy—the staff and the authorities are in broad agreement that the main reasons relate to administrative weaknesses, persistent and deep problems at customs administration, and concerns that the tax-exempt status of the Doba oil project is being abused, thereby seriously undermining customs collection.

These problems point beyond the usual need for identifying and introducing a series of fiscal measures. While these are necessary for improving revenue collection, without sustained high-level political support for serious reforms, particularly at customs and for measures aimed at cracking down on tax evasion, well-intentioned and technically well-designed measures—such as those in the 2002 budget—will not yield the desired results, and revenue collection will remain sluggish. This, in turn, will ultimately undermine the government's objective of financing large-scale poverty-reducing expenditures.

Therefore, at this juncture, clearly demonstrated high-level political support for improved revenue collection is key. In this regard, President Déby's declared personal commitment to the international audit of the customs administration, as well as to a full follow-up on the audit's recommendation, is welcome. The staff also believes that a measure of staff stability and continuity is needed in the tax administration. In addition, a visible campaign against major tax evaders would need to be launched, together with an education campaign explaining to the population that nonpayment of taxes leads to a lack of financing of critical social services and poverty-related expenditures. Only strong political support for the revenue measures, combined with increased public awareness of the perils of tax evasion, could make the introduction of yet another round of measures a success.

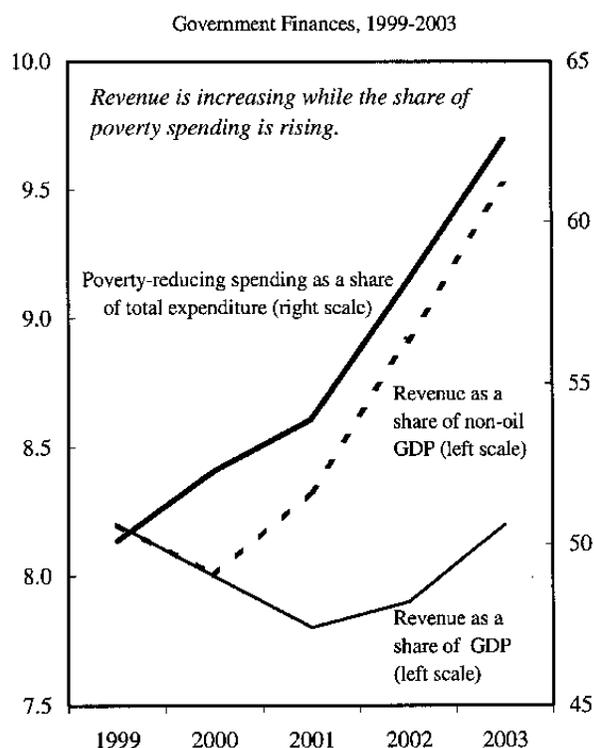
21. As a share of GDP, current primary expenditure is projected to increase from 9.1 percent in 2001 to 9.4 percent in 2002, on account of, as mentioned, an increase in poverty-related spending, as well as a budgeted CFAF 10.3 billion (equivalent to 0.8 percent of GDP) transfer to the cotton sector in the wake of the adverse developments in the world market for cotton, and a CFAF 4.7 billion (0.3 percent of GDP) transfer to the STEE.¹⁶ The

¹⁶ The exceptional transfer to STEE is part of a long-term plan to rehabilitate the energy sector, supported by the World Bank and bilateral donors.

nonmilitary wage bill is projected to increase by 14.7 percent in 2002, mainly owing to an increase in the wage bill of the priority social sectors (including new recruitment and a 10 percent wage increase in the health sector), as well as to the impact of the statutory promotion and the first effects of the civil service reform. The military wage bill is projected to increase by 5.6 percent in real terms, reflecting the ongoing regularization of military personnel. However, as spending on goods and services will be frozen in nominal terms, total military spending will decline slightly as a share of GDP, falling from 1.5 percent in 2001 to 1.4 percent in 2002.

22. **Public investment** is projected to rise strongly from 10.7 percent of GDP in 2001 to 16.8 percent in 2002, owing to the completion of the pipeline construction from the Sédigi oil field to N'Djaména and to the projected increase in investment under projects financed by agreed loans and grants from the multilateral institutions and bilateral donors. Poverty-fund financed investment is also projected to rise by 0.6 percentage point of GDP.

23. **Total poverty-reducing spending¹⁷ is targeted to rise sharply from 11 percent of GDP in 2001 to close to 16 percent of GDP in 2002, reflecting the explicit objective of the government of reaching the quantitative targets for the HIPC Initiative completion point by year's end, as well as of deferring to 2002 part of the Poverty Fund-financed spending originally planned in 2001** (MEFP, para. 15 and Box 4). Considerable progress toward the HIPC Initiative completion points has already been made (Appendix V). This poverty-reducing spending will also help achieve the government's poverty-reduction objectives as laid down in Chad's interim PRSP.



¹⁷ Defined as current and total investment spending in the health, education, rural development, infrastructure, and governance sectors.

Box 4: Chad—PRGF and Poverty and Social Outcomes

The PRGF-supported program approved in early 2000 focuses directly on poverty reduction:

Increasing transparency, good governance, and effectiveness in the use of public resources. The future exploitation of Chad's energy wealth will provide the country with a historic opportunity to achieve deep and sustainable poverty reduction, provided these resources are spent in an equitable and transparent manner. To this end, the government discontinued its off-budget operations, and several important audits have been undertaken. Budget monitoring is also being strengthened, and ex-post control mechanisms are introduced. These measures are complemented by reforms of the procurement system, public expenditure review, and pilot programs to track expenditure in education and health to their final beneficiaries. Management of public resources will also improve as a result of the ongoing civil service reform. A positive social impact of these measures is expected from higher efficiency in the use of public resources.

Increasing total poverty-reducing spending. Poverty-reducing spending is projected to rise from less than 11 percent of GDP in 2000 to close to 16 percent in 2002, directed to education, health, rural sector development, basic infrastructure, and governance.

Enhancing revenue collection, including through the enlargement of the tax base, and thereby bringing often wealthy tax evaders under the tax net. This, coupled with the rise in poverty-related spending, should result in an income redistribution in favor of the poor.

Liberalizing domestic petroleum prices. The government's liberalization of the domestic price of petroleum products in April 2001 is estimated to have had an overall positive social impact. First, the price liberalization led to improvements in energy supplies after years of persistent shortages. Second, effective prices declined overall. Third, the shrinking of the informal markets led to safety improvements as less petroleum is transported and stocked hazardously.

Reforming the cotton sector. The sector's reform strategy, adopted in December 1999, is to increase cotton farmers' revenue and overall productivity by liberalizing the sector. Starting in 2000, farmers' prices are linked, via a predetermined formula, to world market prices (albeit they still get a low lint-equivalent world market price). However, a substantial drop in world market prices for cotton, Chad's main export commodity, could severely affect the situation of cotton producers and undermine ongoing reforms. Chad is seeking therefore additional assistance from the international community, including from the Fund, to offset part of the decline in the farmers' income.

Reinforcing food security. In 1999/2000, extreme weather conditions led to food shortages. In order to avert famine, the international community provided substantial food aid and assistance, in which the Fund participated through a 10 percent augmentation in Chad's access to PRGF resources. As a result, famine was averted, with a clear and direct positive impact on the poorest segments of society.

Involving the poor in policymaking. The Chadian authorities have completed an extensive participatory process in the context of the elaboration of its poverty reduction strategy paper. This process is considered as exemplary, allowing the poorest members of society to have a voice in policymaking. Problem areas identified through this process—such as good governance and accountability—have been incorporated in the Fund's and the World Bank's program design in 2001.

Monetary prospects and financial sector issues

24. **Monetary policy** is conducted at the regional level by the Bank of Central African States (BEAC), covering member states of the CEMAC. The BEAC's key objective is to maintain price stability over the medium term by maintaining the peg between the CFA franc and the euro, and to build up the monetary zone's official reserves. It is expected that, after a 12 percent increase in 2001, consumer price inflation in Chad will be limited to about 4 percent on average in 2002. **Banking supervision** will continue to be strengthened by COBAC, according to which priority should be given to strengthening the management, as well as the computerization, of commercial banks. Moreover, further capital injection is needed for the commercial bank in financial difficulty. The government supports the efforts to adopt a unified banking licensing system within the CEMAC, to establish a regional capital market, and to adopt a common legal framework for microfinance by the beginning of 2002. In addition, the government has participated in the preparation of the payments system reform, which aims to provide for a large payments system with settlements in real time and the development of the card business within the CEMAC zone.

External sector

25. The external current account deficit (excluding official transfers) is projected to widen further from 42 percent of GDP in 2001 to 49 percent in 2002, as exports decline and imports continue to rise steadily with the execution of the Doba project. Exports in value terms are projected to decline by close to 9 ½ percent in 2002 as a result of the drop in cotton exports. Imports in value terms are projected to increase by over 21 percent, mainly reflecting the increase in oil project-related imports; other imports will also rise as a result of an increase in foreign-financed public investment programs (Table 8).

26. Much of the current account deficit will be financed by the expected foreign direct investment (including the Cameroon-Chad pipeline project) and sizable project-related loans. Nevertheless, after the assumed Fund disbursement, there remains a financing gap of CFAF 63 billion (4.7 percent of GDP). This is expected to be covered by support from the World Bank (CFAF 21.6 billion), the European Union (CFAF 15.7 billion), and the African Development Bank (CFAF 8 billion), as well as from bilateral creditors under the HIPC Initiative interim assistance (CFAF 5.2 billion). The residual financing gap of CFAF 12.5 billion (US\$17 million) reflects the negative impact of the cotton sector crisis (see Box 5) and could be covered by (i) additional financing of CFAF 5.2 billion from the World Bank and the Fund, each; and (ii) CFAF 2 billion from a bilateral donor.

Box 5: Additional Financing Need in 2002

Relative to staff projections presented at the approval of the second annual PRGF-supported program in May 2001, the outlook for the cotton sector has worsened dramatically. For 2002, both cotton prices and exports volume are projected to be lower than programmed by 24 percent and 4½ percent, respectively. As a result, an additional financing need of US\$24 million (equivalent to CFAF 17.3 billion or 1.3 percent of GDP) has emerged. The authorities have agreed with the staff on additional fiscal measures to reduce this financing gap by CFAF 4.8 billion; however, an uncovered financing need of CFAF 12.5 billion remains. The authorities seek to cover this gap by requesting additional financing from the international community, including from the Fund (see paras. 12 and 26).

Structural policies

27. **The program continues to focus on structural fiscal policies.** The government also plans to press ahead with reforms in other areas—civil service, the procurement system, the cotton sector, and privatization—that are being covered by World Bank conditionality (Appendix IV).

28. **Structural fiscal policies** will primarily focus on strengthening revenue collection through the following measures: (i) the collection of tax arrears will be accelerated, and, in the area of customs, a short-term measure will aim at increasing the frequency of random visits at the two main customs entry points. In addition, customs revenues would be increased durably on the basis of the recommendations of the international audit of customs, to be finalized by end-April 2002; (ii) procedures will be established to verify tax-exempt imports ex-post under the Doba project by mid-March 2002; (iii) a study on the reform of the taxation of small taxpayers (IGL) will be prepared by end-June 2002, with a view to introducing the reform in the context of the 2003 budget; (iv) the computerization of the customs database will be finalized via the use of SYDONIA; (v) the computerization of the large taxpayers unit will be finalized by the middle of 2002; (vi) the linking up of computer networks among customs administration, the large taxpayers unit, and the expenditure circuit will be started, with a view to sharing and verifying basic information on economic agents and budget execution; (vii) income revenue information will be cross-checked with that on public procurement contracts, with a view to spotting tax evasion; and (viii) the collection of the cattle tax will be reinforced, so as to bring an important part of the informal sector under the tax net.

29. **Expenditure management will be further strengthened through a number of measures:** (i) budget monitoring will improve following the full implementation of the new expenditure circuit. The monitoring of budget execution through the much-simplified and computerized expenditure circuit will be helped by the biweekly updates of the expenditure-monitoring tables, which depict spending through the main four stages (commitment, validation, payments order, and cash payment); (ii) starting January 1, 2002, the

implementation of the investment budget will be included in the treasury cash plan, based on monthly information from the project managers; (iii) the government has set up a contingency mechanism to shelter budget execution from unexpected shortfalls in budgetary resources. Accordingly, in the 2002 budget, CFAF 12 billion of nonwage, nonpriority sector expenditure has been set aside, which will be authorized only in the fourth quarter and only after its financing has been secured; (iv) following the recommendations of the World Bank, a medium-term expenditure program will be initiated in the first quarter of 2002; (v) the government will discontinue the use of cash payments for suppliers and will study the conditions for bank deposit payments for the civil service to be started in 2003; and (vi) starting in the third quarter of 2002, the quarterly budget execution will also include a functional classification of expenditure. The ongoing reorganization of the Ministry of Finance is expected to improve its implementation capacity.

Governance

30. The focus in the governance area will be on consolidating the progress made thus far by reinforcing existing rules and regulations and further strengthening the domestic institutions that are critical for internal checks and balances. The government will follow up on the recommendations of the audit on the use of the oil bonus by the General Auditor's Office and is expected to publish its results in an appropriate form. Moreover, the program's governance measures should have a direct positive impact on the fiscal area. First, the completion of the international audit of customs before end-April 2002 and the implementation of its recommendations should lead to a major reform of the customs administration, and a correspondingly large revenue yield. Second, lessons from the audit of the five largest procurement contracts, to be finalized by end-May 2002, will feed into the ongoing reform of the procurement system. The results of these audits will also be made public. As an important step, the government has specifically committed itself to using only transparent and competitive procedures to award public contracts (MEFP, para. 19); this practice should safeguard against pressures to circumvent existing regulations governing the sale of government assets and the awarding of public contracts—particularly in the energy sector where most temptations occur. In other areas covered by the World Bank's conditionality, Chad's national governance strategy is expected to be adopted by end-March 2002, after which date its implementation will begin. Also, a new procurement code will be published in 2002, and an independent procurement appeals system will be set up.

Regional integration and external trade regime

31. While regional integration, measured as trade intensification with CEMAC and neighboring non-CEMAC countries, has advanced, **macroeconomic policy convergence with the CEMAC zone has not progressed in recent years** (Box 6). At end-2000, Chad complied with only one of the four convergence indicators established by the Ministers of Finance of CEMAC. The trend has not been favorable either, with a weakening compliance record since 1999. The Chadian authorities fully subscribe to the objective of macroeconomic policy convergence by end-2004 as a way of strengthening the monetary zone, and plan to

comply with the decision of the zone's Ministers of Finance to develop a time-bound schedule for convergence in the near future.

32. **Chad has opened up its trade regime during the past years**, and now rates a 4 on the Fund's overall 10-point trade restrictiveness index. Trade integration will be fostered by the planned further reduction to a maximum rate of 20 percent of the common external tariff on imports from non-CEMAC countries scheduled to be adopted in 2002. Trade intensification is expected to get a major boost from the construction of the Chad-Cameroon pipeline.

Box 6. Chad: Convergence of Macroeconomic Policies in the CEMAC

In March 1993, the six CEMAC member countries set up a Committee on Multilateral Surveillance (Conseil de Surveillance), with a view to ensuring that the national macroeconomic policies are compatible with the objectives of stability of the common currency and sustained economic growth. The CEMAC treaty on the convergence of macroeconomic policies was signed in 1994, shortly after the devaluation of the CFA franc, and ratified by all member countries by March 1999.

According to the last report on multilateral convergence, prepared at end-2000, Chad compared relatively unfavorably to the other member countries, having complied with only one—the foreign reserve cover ratio—of the four convergence indicators.^{1/}^{2/} Moreover, the report revealed a worsening trend, as Chad had met all criteria in 1998, and two in 1999. Some of this deterioration was due to the slowdown of overall economic activity in 1999–2000, but fiscal and governance slippages in 2000 played a major role.

Chad has subscribed to the decision of the Council of Ministers of the CEMAC in August 2001 to strengthen macroeconomic surveillance and reinforce policy convergence. It is, therefore, now committed to complying with all the four newly adopted convergence criteria^{3/} by end-2004; the government has started to work on a three-year program to meet these criteria.

^{1/} These indicators included (i) a foreign reserve cover ratio (defined as gross official reserves over the monetary base) of at least 20 percent; (ii) a positive primary fiscal balance; (iii) a rate of increase in the wage bill not exceeding that in budgetary revenue; and (iv) the nonaccumulation of net domestic and external payments arrears.

^{2/} Only Gabon complied with all four criteria.

^{3/} These include (i) a fiscal primary base balance positive or zero; (ii) an annual inflation rate less than 3 percent; (iii) a ratio of outstanding public debt GDP to be lower than 70 percent; and (iv) the nonaccumulation of payments arrears.

IV. PRSP PREPARATION

33. The preparation of the fully participatory PRSP is well under way. However, the original deadline of the fall 2001 could not be met, as the exemplarily inclusive participatory process has taken considerably more time than earlier envisaged by both the authorities and the international community. Building a consensus in the drafting of the document has also proved to be more time-consuming than initially assumed. The progress made since the completion of the interim PRSP in May 2000¹⁸ and the road map to finalize the full PRSP by the spring of 2002 are discussed in the authorities' PRSP preparation status report, which is to be submitted with a joint staff assessment by the Fund and the World Bank to the two Executive Boards in December 2001.

V. PRIOR ACTIONS, FUND CONDITIONALITY, AND PROGRAM MONITORING

34. Four prior actions have been set with the objective of ensuring that conditions conducive to the program's success are in place at the time of the Executive Board's consideration of the third program review: (i) submission of the 2002 budget law, on which understandings were reached with the staff, to parliament (this prior action was fulfilled on November 29); (ii) adoption of the guidelines for the pricing and taxation of the Sédigi field's oil and gas products (thus making up for the nonobservance of a structural benchmark at end-September); (iii) submission of a report to the Council of Ministers on the findings of a four-week-long series of random inspection visits to the two main customs entry points (MEFP, para. 26) (this prior action was fulfilled on December 12)¹⁹; and (iv) clearing all outstanding external arrears (this prior action was fulfilled on December 18).

35. The program conditionality, covering only the areas that are directly relevant, and often critical, to the program's success, has been retained. The quantitative performance criteria have been updated and modified to take account of (i) the new schedule of external financing; and (ii) the downward revision of the revenue target at end-December. **The focus of conditionality in the structural area is proposed to shift, after good progress, from governance issues to the problem area— revenue collection.** Expenditure management will also need to be strengthened. It is, therefore, proposed that structural performance criteria be set on the adoption by the Council of Ministers of procedures for ex post verification of all tax-exempt products under the Doba project, and on the implementation of the streamlined expenditure circuit. Structural benchmarks are proposed to cover areas that are important for

¹⁸ This was considered by the Executive Boards of the Fund and the World Bank in July 2000.

¹⁹ The report confirms widespread undervaluation of imports, as well as corruption, the latter sustained in part by threats against customs officers. The government is evaluating the implications of the report.

the success of the program (in revenue collection, adoption of an action plan on the basis of the recommendations of the customs audit; in fiscal auditing, cross-checking of fiscal income tax returns with declaration on bidding for procurement contracts). The updated quantitative and structural performance criteria for end-December 2001, and the new criteria for end-March 2002, as well as indicative targets for end-June 2002 and accompanying structural benchmarks, are summarized in Tables 1 and 2 of the authorities' MEFP. The next, fourth, program review will take place after end-March 2002 and will focus on budget implementation and fiscal structural measures.

VI. CAPACITY BUILDING NEEDS AND STATISTICAL ISSUES

36. **The overall administrative capacity of the authorities remains severely limited**, despite recent improvements and assistance provided by resident experts (of whom two were from FAD). The staff and the authorities agree that **a concerted plan of action is needed to build up administrative capacity rapidly**. As a first step, a draft "mini" technical assistance action plan (TAAP) has been put together, and is being discussed with main donors. The mini TAAP identifies the following key areas where urgent assistance is needed: tax collection, budget elaboration and control, liaisons between the treasury and key line ministries, and statistics, the latter by involving relevant regional institutions of the CEMAC. Chad could also be a prime candidate to benefit from the planned regional assistance centers under the Fund's Africa Capacity Building Initiative. President Déby personally welcomed this Fund initiative during a meeting with the IMF mission.

37. Chad continues to suffer from major weaknesses in its statistical system (Appendix VI). A multisectoral STA mission in May 2000 proposed wide-ranging improvements to strengthen the statistical database, particularly in the area of national income accounts, balance of payments, and government finance. The government has started to implement these recommendations; however, overall progress has been limited. Improvements nevertheless occurred, following the revision of monetary accounts and the commitment not to engage in off-budget activities. With a delay—for reasons outside the authorities' control—the government will launch a household survey on income and expenditure in January 2002, with assistance from the World Bank. The results of the survey—the definition of a poverty line and main poverty indicators (incidence, depth, and severity)—will be continuously fed into the national poverty-reduction strategy.

VII. STAFF APPRAISAL

38. **Chad's satisfactory economic performance in 2001 signals a clear break with the policy slippages in 2000**. This performance, together with the acceleration of the Doba oil project, has set the stage for a sustained growth path with measurable poverty reduction. To realize this potential, the authorities must now focus on several short-term problems, as well as on challenges posed by the nearing petroleum era.

39. **A primary short-term challenge is strengthening fiscal revenues.** While some of the factors behind the weak revenue collection have been outside the government's control, the staff is convinced that an unwavering high-level political backing of the well-designed revenue measures included in the 2002 budget will be critical to achieving the program's revenue objectives. In this regard, President Déby's personal commitment to the international audit of customs and a strict follow-up on its recommendation is reassuring. It is clear that a continued faltering revenue performance may seriously endanger implementation of the government's PRGF-supported program.

40. **The staff welcomes recent improvements in expenditure management and urges the authorities to build on this momentum by pressing ahead with additional measures.** The introduction of the simplified and computerized expenditure circuit will provide the necessary tool for the Ministry of Finance to monitor and control expenditure effectively. Contingency spending mechanisms incorporated in the 2002 budget will provide a much-needed flexible instrument for cases when the budget's resource assumptions do not materialize. Other important measures will prepare the groundwork for moving away from the inherently inefficient and costly cash payments system toward the use of bank transfers to pay suppliers and, starting in 2003, the civil servants; this measure will also foster the development of personal banking services. Finally, the authorities will need to follow up on the recently prepared public expenditure reviews in the education and health sectors.

41. **The authorities are to be commended for their improved governance record, including the audit of the oil bonus, which has largely helped reestablish the government's credibility.** The focus now must be on consolidating progress and resisting pressures for circumventing existing rules and regulations. Following up on the recommendations in the audit on the use of the oil bonus (together with the audit's eventual publication in an appropriate form) will be crucial for creating a fully rules-based economic system with accountability by government officials at all levels; other governance measures should also have a direct positive impact on revenue collection and fiscal control.

42. The authorities face two major longer-term challenges in the petroleum era. They fully recognize the first one, which is to avoid the perils of developing a dual economy, in which the oil sector's rapid advancement does not benefit the rest of the economy. The staff is reassured by the authorities' apparent determination to implement the discussed actions in this regard. However, in the staff's view, **it will be equally important for the authorities to fully face up to the second main challenge of the petroleum era, which is to rapidly develop the domestic institutions and administrative capacity to enable them to absorb oil revenues effectively and to distribute them equitably.** Ongoing structural fiscal reforms and further improvements will be key in this regard. An indispensable element of this effort will be an improvement in the statistical system, so as to improve both the quality and the timeliness of macroeconomic statistical data. In these areas, the staff strongly supports the Chadian authorities' urgent request for additional technical assistance, including the possibility of benefiting early on from the Fund's new Africa Capacity Building Initiative.

43. In view of the progress made to date, including the authorities' actions in building a track record, and the appropriate policies envisaged for 2002, **the staff recommends the completion of the third review under the PRGF arrangement, with waivers granted for the nonobservance of performance criteria. In light of the worldwide cotton sector crisis and its sharp and unexpected negative impact on farmers' income, and taking into account the authorities' ongoing cotton sector reform program, the staff also recommends the approval of Chad's request for an augmentation of the PRGF arrangement amounting to 10 percent of quota** (equivalent to SDR 5.6 million), to be disbursed in two equal tranches upon the completion by the Executive Board of the third and fourth PRGF reviews.

Table 1. Chad: Quantitative Performance Criteria and Benchmarks for the Second Annual Program
Under the Poverty Reduction and Growth Facility Arrangement, End-September 2001
(Cumulative Changes from January 1, 2001, in billions of CFA francs)

	Crit.	Adjust. Crit.	Est.	Crit. Met
Quantitative performance criteria				
Ceiling on the increase in net credit of the banking system to the central government (excluding IMF resources) 1/	7.4	15.7	6.0	Yes
Floor on current primary fiscal balance 2/	-6.4		-5.6	Yes
Floor on total government revenue, excluding grants 3/	69.0		62.8	No
Nonaccumulation of external payments arrears of the central government (cumulative since Jan. 1, 2001) 4/ 5/	0.0		0.6	No
Ceiling on new nonconcessional external debt with maturities of more than one year contracted or guaranteed by the central government (cumulative) 6/	0.0		0.0	Yes
Ceiling on net change in external debt with a maturity of up to and including one year, except normal trade financing (cumulative)	0.0		0.0	Yes
Indicative benchmarks 7/				
Floor on current expenditure on health 8/	7.1		5.5	
Floor on current expenditure on education 8/	14.4		13.3	
Ceiling on total wage spending by the central government (including military)	42.5		41.5	
Adjusters				
Net reduction of domestic payments arrears of the government	6.7		-8.7	
Privatization revenue	0.0		0.0	
Balance of payments assistance 9/	45.4		13.8	
Adjustment lending (excl. IMF)	21.4		0.0	
Adjustment grants	21.3		5.2	
Debt relief excluding HIPC Initiative	2.7		8.6	

Sources: Chadian authorities; Bank of Central African States (BEAC); and staff estimates.

1/ The targets will be adjusted (i) upward for a shortfall in balance of payments assistance (as identified in the adjusters and excluding projected lending and grants) up to an amount equivalent to 75 percent of the shortfall; (ii) downward to take account of a lower repayment of domestic arrears than foreseen under the program for the corresponding period; and (iii) upward for a shortfall in sales of assets revenue up to an amount equivalent to 75 percent of the shortfall.

2/ Defined as total revenue less grants, minus current primary spending (current spending, less electoral and famine-related outlays and less interest payments).

3/ Net of reimbursements under the system of treasury checks.

4/ Monitored on a continuous basis.

5/ Excluding external payments arrears incurred pending debt rescheduling.

6/ Nonconcessional loans defined as loans with a grant element of less than 35 percent, using discount rates based on the commercial interest reference rates (CIRRs). An exception will be made for a nonconcessional IBRD loan in an amount of US\$35 million contracted by the government of Chad in the context of the Chad-Cameroon Pipeline Project.

7/ These indicators will not constitute performance criteria of the program.

8/ Including wages.

9/ Including the possible financing recorded in the financing gap.

Table 2. Chad: Structural Performance Criterion and Benchmarks for the
Second Annual Program Under the Poverty Reduction and Growth Facility Arrangement

	Test Date	Status
Structural performance criteria		
Completion of the audit on the use of the oil bonus as of December 31, 2000	September 30, 2001	Not done; measure satisfied with a delay 1/
Structural benchmarks		
Agreement with commercial banks on the payment of interest on government accounts	June 30, 2001	Not done; measure satisfied with a delay 2/
Launching of the bidding procedures to recruit a reputable international firm to carry out the functional and financial audit of customs administration	July 31, 2001	Done
Adoption by the government of the principles guiding the pricing and taxation mechanisms of the Sedigi oil and gas field	September 30, 2001	Not done

1/ Completed on November 12, 2001.

2/ Agreement reached on September 1 2001.

Table 3. Chad: Selected Economic and Financial Indicators, 2000-03

	2000	2001		2002	2003
		Prog.	Rev. Prog.	Rev. Prog.	Rev. Prog.
(Annual percentage change, unless otherwise specified)					
National income					
GDP at current prices	4.1	13.6	17.2	15.2	13.8
GDP at constant prices	0.6	8.2	8.9	10.8	9.4
Consumer price index (average)	3.8	7.3	12.4	4.0	4.0
Consumer price index (December on December)	13.0	-0.6	-0.1	12.1	1.8
Money and credit					
Net foreign assets 1/	-2.3	4.1	4.6	3.8	...
Net domestic assets 1/	21.1	15.3	13.3	10.0	...
<i>Of which: domestic credit 1/</i>	24.5	15.4	13.1	9.8	...
Net claims on central government	18.7	13.3	7.6	3.9	...
Credit to nongovernment sector	5.8	2.1	5.5	5.9	...
Broad money	18.5	19.0	17.8	13.9	...
Income velocity of money (M2) 2/	8.2	7.8	8.1	8.2	...
External sector (valued in CFA francs)					
Exports, f.o.b.	11.8	7.7	8.0	-9.4	10.8
Imports, f.o.b.	15.6	123.9	136.6	21.3	17.8
Export volumes	13.4	-2.4	-0.2	1.4	4.9
Import volumes	8.1	151.3	166.9	19.9	16.6
Terms of trade	-2.5	19.2	12.0	-8.7	0.7
(In percent of GDP)					
Basic ratios					
Gross investment	17.0	40.7	42.5	51.5	54.0
Central government	10.3	18.5	10.7	16.8	14.6
Private sector	6.7	22.2	31.7	34.7	39.4
<i>Of which: oil sector</i>	2.5	17.1	25.5	28.5	31.9
Gross domestic savings	1.6	0.5	0.6	3.5	4.3
Central government	-2.0	-2.3	-2.2	-2.4	-0.1
Private sector	3.5	2.8	2.8	5.9	4.4
Gross national savings	3.3	1.3	1.3	3.3	4.7
Central government	0.3	-0.9	-1.0	-1.8	0.7
Private sector	3.0	2.1	2.3	5.1	4.0
Central government finance					
Revenue	8.0	8.4	7.8	7.9	8.2
Total expenditure	20.3	29.2	20.8	27.2	22.9
Current primary balance (- =deficit) 3/	-0.9	-1.3	-1.3	-1.5	0.6
Overall fiscal deficit (commitment basis) 3/	-12.3	-20.8	-12.9	-19.3	-14.7
Overall fiscal deficit (cash basis) 3/	-12.4	-21.5	-13.6	-19.6	-14.9
Domestic financing	2.6	0.5	-0.4	0.3	-0.2
External financing (already obtained)	9.8	20.6	14.0	18.4	13.7
Financing gap (-)	0.0	-0.4	0.0	-0.9	-1.5
External sector					
Current account (- deficit)					
Including official transfers	-13.7	-39.3	-41.2	-48.2	-49.3
Excluding official transfers	-16.0	-40.7	-42.4	-48.8	-50.1
Excluding official transfers and oil-related imports	-13.5	-23.6	-16.9	-20.3	-18.2
Overall balance of payments (- deficit)	-0.9	-4.8	-5.0	-4.9	-1.9
(In millions of U.S. dollars, unless otherwise specified)					
Overall balance of payments deficit/surplus	-13.2	-78.0	-80.1	-91.6	-40.5
Nominal GDP	1,405.8	1,631.3	1,612.2	1,884.4	2,153.8
Nominal GDP (in billions of CFA francs)	1,002.4	1,138.4	1,175.3	1,354.1	1,541.0
CFA francs per U.S. dollar (period average)	713.0	697.8	729.0	718.6	715.5
CFA francs per U.S. dollar (end of period)	731.4	703.6	718.8	717.1	714.4
Population (midyear, in millions)	7.5	7.7	7.7	7.9	8.1
Nominal GDP per capita	188.0	212.8	210.3	239.8	267.4

Sources: Chadian authorities; and staff estimates and projections.

1/ Changes as percent of broad money stock at beginning of period.

2/ Ratio of GDP to average broad money.

3/ Excluding grants.

Table 4. Chad: Consolidated Government Operations, 2000-03 1/
(In billions of CFA francs)

	2000	2001				2002			2003 Rev. Proj.
		Sep.		Dec.		March	June	Dec.	
		Prog.	Est.	Prog.	Rev. Prog.	Rev. Prog.	Rev. Prog.	Rev. Prog.	
Total revenue and grants	128.2	136.6	80.0	188.5	137.4	40.0	90.1	203.9	228.4
Total revenue	80.2	69.0	62.8	96.0	92.2	23.7	50.9	107.3	126.3
Tax revenue	68.3	59.0	53.0	81.7	78.1	20.4	44.2	94.0	111.7
Tax on revenue	24.3	21.6	19.8	29.2	29.8	7.1	15.8	33.3	39.2
Tax on goods and services	18.8	16.0	13.6	21.8	20.5	5.9	12.4	25.1	29.5
Tax on international trade	21.8	20.8	18.7	29.7	26.8	7.2	15.5	34.3	41.5
Other	3.4	0.6	0.9	0.9	1.0	0.2	0.6	1.3	1.5
Oil revenue	...	...	...	...	...	0.0	0.0	0.0	0.0
Nontax revenue	11.9	10.0	9.8	14.3	14.1	3.3	6.6	13.2	14.6
Total grants	48.0	67.6	17.2	92.5	45.2	16.3	39.3	96.6	102.1
HIPC Initiative assistance	0.0	2.6	1.2	6.4	5.0	2.0	4.1	8.1	12.9
Project grants	48.0	65.0	16.0	86.1	40.2	14.3	35.2	88.5	89.2
Total expenditure	203.2	241.8	139.9	332.5	244.1	72.7	155.9	368.0	352.7
Current expenditure	99.9	94.8	79.0	122.0	117.9	32.1	62.0	139.9	128.0
Current primary expenditure	89.6	87.3	72.6	111.2	107.4	29.7	56.1	127.8	116.6
Wages and salaries	40.0	33.9	32.9	45.8	44.9	12.9	25.7	51.5	53.2
Materials and supply	20.8	20.6	15.1	27.1	24.7	6.3	13.3	27.3	31.2
Transfers	12.0	6.2	5.4	8.2	7.7	4.1	6.3	20.7	5.9
Defense	15.2	14.8	15.0	18.2	18.2	4.4	8.7	19.3	20.1
Salaries	10.2	8.6	8.6	11.5	11.5	3.1	6.3	12.6	13.1
Materials and supply	5.0	6.2	6.4	6.8	6.8	1.3	2.5	6.8	7.0
Famine	0.0	7.2	0.0	7.2	7.2	0.0	0.0	0.0	0.0
Elections	0.4	4.7	4.2	4.7	4.7	2.0	2.0	3.0	0.0
Summits	1.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest	10.3	7.5	6.4	10.8	10.4	2.4	5.9	12.1	11.4
Domestic	1.4	1.1	0.6	1.7	1.7	0.3	0.9	1.8	1.8
External	8.9	6.3	5.9	9.1	8.8	2.1	5.0	10.3	9.6
Current primary balance, perf. criterion definition 2/	-7.8	-6.4	-5.6	-3.3	-3.3	-3.9	-3.2	-17.6	9.7
Current balance	-19.7	-25.8	-16.2	-26.0	-25.7	-8.4	-11.1	-32.7	-1.8
Investment expenditure	103.3	147.0	61.0	210.5	126.3	40.6	93.9	228.1	224.7
Domestically financed	10.7	15.7	6.1	23.8	17.1	5.2	8.8	31.9	27.1
Foreign financed	92.6	131.3	54.9	186.7	109.2	35.5	85.1	196.3	197.6
Overall deficit (commitment basis)									
Excluding grants	-123.0	-172.8	-77.2	-236.5	-151.9	-49.0	-105.0	-260.8	-226.5
Including grants	-75.0	-105.2	-59.9	-144.0	-106.7	-32.7	-65.7	-164.1	-124.4
Change in payments arrears	-2.6	-7.8	7.8	-8.1	-7.8	-0.3	-0.3	-4.8	-3.5
External (interest)	1.2	-1.2	-0.9	-1.2	-1.2	0.0	0.0	0.0	0.0
Domestic	-3.7	-6.7	8.7	-7.0	-6.7	-0.3	-0.3	-4.8	-3.5
Float, errors, and omissions	1.7	0.0	-1.6	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (cash basis, excluding grants)	-123.8	-180.6	-70.9	-244.6	-159.8	-49.3	-105.3	-265.6	-230.0
Overall balance (cash basis, including grants)	-75.8	-113.0	-53.7	-152.1	-114.5	-33.0	-66.0	-168.9	-127.9
Total financing	75.8	109.0	53.7	148.1	114.5	30.4	61.4	156.5	105.1
External financing, excl. exceptional financing (net)	32.8	56.1	34.8	86.3	61.8	16.5	42.1	92.0	93.2
Loans	44.6	66.3	38.9	100.6	69.0	21.2	49.9	107.7	108.4
Amortization due	-14.1	-10.6	-10.8	-15.7	-16.3	-5.4	-9.4	-18.9	-17.1
Change in external arrears (principal)	2.3	-2.3	-1.9	-2.3	-2.5	0.0	0.0	0.0	0.0
Rescheduling / debt relief	0.0	2.7	8.6	3.6	11.7	0.8	1.6	3.2	2.0
Domestic financing (net)	25.7	1.0	3.3	6.2	-4.4	0.8	3.2	4.3	-3.6
Banking system	19.3	5.9	5.1	9.0	-1.6	1.4	7.1	6.5	0.0
Nonbanking system	3.7	-4.9	-1.8	-5.7	-4.2	-0.6	-3.9	-7.4	-3.6
Sale of assets	2.8	0.0	0.0	3.0	1.4	0.0	0.0	5.2	...
Expected additional financing	17.4	39.6	5.2	41.0	44.3	10.7	11.4	50.5	10.7
World Bank	0.0	17.4	0.0	17.4	28.7	0.0	0.0	21.6	10.7
European Union	7.2	14.3	4.1	14.3	10.4	3.9	3.9	15.7	0.0
African Development Bank	0.0	4.0	0.0	4.0	0.0	3.7	3.7	8.0	0.0
Bilateral donors	0.0	0.0	0.0	0.0	4.0	0.0	0.0	0.0	0.0
HIPC Initiative exceptional financing	...	0.9	0.0	2.3	0.0	3.0	3.8	5.2	0.0
Other 3/	10.2	3.0	1.2	3.0	1.2	0.0	0.0	0.0	0.0
Fund disbursement	0.0	12.2	10.4	14.6	12.8	2.4	4.8	9.6	4.8
Financing gap	0.0	4.0	0.0	4.0	0.0	2.6	4.6	12.5	22.7

Sources: Chadian authorities; and staff estimates and projections.

1/ Excluding accounting of public contract taxation.

2/ Defined as primary current expenditure minus spending related to summits (in 2000), elections, and famine.

3/ In 2000, includes the oil bonus; in 2001, includes the expected foreign financing for the elections.

Table 5. Chad: Consolidated Government Operations, 2000-03 1/

	2000	2001		2002	2003	2000	2001		2002	2003
	Est.	Prog.	Rev. Prog.	Rev. Prog.	Rev. Proj.	Est.	Prog.	Rev. Prog.	Rev. Prog.	Rev. Proj.
	(In percent of GDP, unless otherwise specified)					(In percent of non-oil GDP, unless otherwise specified)				
Total revenue and grants	12.8	16.6	11.7	15.1	14.8	12.8	17.5	12.4	16.9	17.2
Total revenue	8.0	8.4	7.8	7.9	8.2	8.0	8.9	8.3	8.9	9.5
Tax revenue	6.8	7.2	6.65	6.9	7.2	6.8	7.6	7.1	7.8	8.4
Oil revenue	...	...	...	0.0	0.0	...	...	...	0.0	0.0
Nontax revenue	1.2	1.3	1.2	1.0	0.9	1.2	1.3	1.3	1.1	1.1
Total grants	4.8	8.1	3.8	7.1	6.6	4.8	8.6	4.1	8.0	7.7
Of which: HIPC Initiative assistance	0.0	0.6	0.4	0.6	0.8	0.0	0.6	0.5	0.7	1.0
Total expenditure	20.3	29.2	20.8	27.2	22.9	20.3	30.8	22.1	30.6	26.6
Current expenditure	10.0	10.7	10.0	10.3	8.3	10.0	11.3	10.7	11.6	9.7
Of which: current primary expenditure	8.9	9.8	9.1	9.4	7.6	8.9	10.3	9.7	10.6	8.8
Baseline 2/	8.8	8.2	7.9	7.6	7.0	8.8	8.7	8.4	8.6	8.2
Exceptional 3/	0.2	1.0	1.0	1.3	0.0	0.2	1.1	1.1	1.5	0.0
Poverty Fund financed	0.0	0.5	0.2	0.5	0.5	0.0	0.5	0.3	0.6	0.6
Current primary balance										
Underlying position 2/	-0.8	0.2	0.0	0.3	1.2	-0.8	0.2	0.0	0.3	1.4
Total	-0.9	-1.3	-1.3	-1.5	0.6	-0.9	-1.4	-1.4	-1.7	0.7
Total investment expenditure	10.3	18.5	10.7	16.8	14.6	10.3	19.5	11.4	19.0	16.9
Baseline	10.3	17.7	10.5	15.9	14.1	10.3	18.7	11.2	17.9	16.4
Domestically financed	1.1	1.3	1.2	1.4	1.3	1.1	1.4	1.3	1.6	1.5
Foreign financed	9.2	16.4	9.3	14.5	12.8	9.2	17.3	9.9	16.3	14.9
Poverty Fund financed	0.0	0.8	0.2	0.9	0.5	0.0	0.8	0.2	1.0	0.5
Overall balance (commitment basis, excl. grants)	-12.3	-20.8	-12.9	-19.3	-14.7	-12.3	-21.9	-13.7	-21.7	-17.1
Overall balance (cash basis, incl. grants)	-7.6	-13.4	-9.7	-12.5	-8.3	-7.6	-14.1	-10.3	-14.0	-9.6
Total financing	7.6	13.0	9.7	11.6	6.8	7.6	13.7	10.3	13.0	7.9
External financing (net)	3.3	7.6	5.3	6.8	6.0	3.3	8.0	5.6	7.7	7.0
Domestic financing (net)	2.6	0.5	-0.4	0.3	-0.2	2.6	0.6	-0.4	0.4	-0.3
Expected additional financing	1.7	3.6	3.8	3.7	0.7	1.7	3.8	4.0	4.2	0.8
Fund disbursement	0.0	1.3	1.1	0.7	0.3	0.0	1.4	1.2	0.8	0.4
Financing gap	0.0	0.4	0.0	0.9	1.5	0.0	0.4	0.0	1.0	1.7
Memorandum items:										
HIPC Initiative assistance	0.0	0.8	0.4	1.0	1.0	...	...	...	...	...
Poverty-reducing spending	10.6	16.7	11.2	15.8	14.3	10.6	17.7	11.9	17.8	16.6
HIPC Initiative assistance (billions of CFA francs)	0.0	8.7	5.0	13.3	15.6	...	...	...	...	...
Total GDP (billions of CFA francs)	1,002.4	1,138.4	1,175.3	1,354.1	1,541.0	...	...	...	...	...

Sources: Chadian authorities; and staff estimates and projections.

1/ Excluding accounting of public contract taxation.

2/ Current primary expenditure, excluding exceptional expenditure and expenditure financed by Poverty Fund resources.

3/ Includes outlays related to famine and elections and, in 2002, exceptional subsidies to the cotton and energy sectors.

Table 6. Chad: Consolidated Government Operations
(Baseline Scenario, Excluding Poverty Fund), 2000-03 1/
(In billions of CFA francs)

	2000	2001		2002	2003
		Prog.	Rev. Prog.			Rev. Prog.	Rev. Proj.
Total revenue and grants	128.2	182.1	132.4	195.8	215.4
Total revenue	80.2	96.0	92.2	107.3	126.3
Tax revenue	68.3	81.7	78.1	94.0	111.7
Income tax	24.3	29.2	29.8	33.3	39.2
Tax on goods and services	18.8	21.8	20.5	25.1	29.5
Tax on international trade	21.8	29.7	26.8	34.3	41.5
Other taxes	3.4	0.9	1.0	1.3	1.5
Oil revenue	...	...	...	0.0	0.0
Nontax revenue	11.9	14.3	14.1	13.2	14.6
Total grants	48.0	86.1	40.2	88.5	89.2
HIPC Initiative assistance	...	...	...	...	...
Project grants	48.0	86.1	40.2	88.5	89.2
Total expenditure	203.2	317.6	238.8	348.8	338.7
Current expenditure	99.9	116.2	115.0	133.3	121.2
Current primary expenditure	89.6	105.5	104.6	121.2	108.2
Wages and salaries	41.5	43.8	44.1	49.1	51.1
Materials	20.8	23.3	22.6	23.0	24.9
Transfers	10.6	6.7	6.3	19.2	4.5
Defense	15.2	18.2	18.2	19.3	20.1
Salaries	10.2	11.5	11.5	12.6	13.1
Materials and supplies	5.0	6.8	6.8	6.8	7.0
Famine	0.0	7.2	7.2	0.0	0.0
Elections	0.4	4.7	4.7	3.0	0.0
Other	1.3	0.0	0.0	0.0	0.0
Contingent current expenditure	...	...	...	6.0	6.2
Interest	10.3	10.8	10.4	12.1	13.0
Domestic	1.4	1.7	1.7	1.8	1.8
External	8.9	9.1	8.8	10.3	11.2
Current primary balance, perf. criterion definition 2/	-7.8	2.5	-0.5	-10.9	18.1
Current balance	-19.7	-20.2	-22.8	-26.0	5.1
Investment expenditure	103.3	201.3	123.8	215.5	217.5
Domestically financed	10.7	14.6	14.6	19.3	19.9
Of which: contingent investment	...	...	...	6.0	6.3
Foreign financed	92.6	186.7	109.2	196.3	197.6
Overall deficit (commitment basis)					
Excluding grants	-123.0	-221.6	-146.6	-241.5	-212.4
Including grants	-75.0	-135.4	-106.4	-153.0	-123.2
Change in payments arrears	-2.6	-8.1	-8.1	-4.5	-3.5
External (interest)	1.2	-1.2	-1.2	0.0	0.0
Domestic	-3.7	-7.0	-7.0	-4.5	-3.5
Float, errors, and omissions	1.7	0.0	0.0	0.0	0.0
Overall deficit (cash basis; excl. grants)	-123.8	-229.7	-154.8	-246.0	-215.9
Overall deficit (cash basis; incl. grants)	-75.8	-143.6	-114.5	-157.5	-126.7
Total financing	75.8	139.6	114.5	145.0	104.0
External financing (net)	32.8	86.3	61.8	92.0	92.1
Loans	44.6	100.6	69.0	107.7	108.4
Amortization	-14.1	-15.7	-16.3	-18.9	-18.3
Change in external arrears (principal)	2.3	-2.3	-2.5	0.0	0.0
Debt relief/rescheduling obtained	0.0	3.6	11.7	3.2	2.0
Domestic (net)	25.7	0.0	-4.4	-1.9	-3.6
Banking system	19.3	2.7	-1.6	0.3	0.0
Nonbank sector	3.7	-5.7	-4.2	-7.4	-3.6
Sale of assets	2.8	3.0	1.4	5.2	...
Expected additional financing	17.4	38.7	44.3	45.3	10.7
World Bank	0.0	17.4	28.7	21.6	10.7
European Union	7.2	14.3	10.4	15.7	...
African Development Bank	0.0	4.0	0.0	8.0	...
Bilateral donors	0.0	0.0	4.0	0.0	...
HIPC Initiative exceptional financing	...	...	...	...	...
Other 3/	10.2	3.0	1.2	0.0	...
Fund disbursement	0.0	14.6	12.8	9.6	4.8
Financing gap	0.0	4.0	0.0	12.5	22.7

Sources: Chadian authorities; and staff estimates and projections.

1/ Excluding accounting of public contract taxation.

2/ Defined as primary current expenditure minus spending related to summits (in 2000), elections, and famine.

3/ In 2000, includes the oil bonus; in 2001, includes the expected foreign financing for the elections.

Table 7. Chad: Poverty-Reducing Spending, 2000-03 1/

	2000	2001	2002	2003
		Est.	Rev. Prog.	Proj.
	(In billion of CFA francs)			
Baseline budget	106.2	126.6	194.8	206.7
Current	34.8	41.3	46.3	50.4
Investment	71.4	85.3	148.4	156.3
Additional budget	0.0	5.3	19.2	14.1
Current	0.0	2.9	6.6	6.9
Investment	0.0	2.5	12.6	7.2
Total poverty-reducing spending	106.2	131.9	214.0	220.8
Current	34.8	44.2	53.0	57.2
Investment	71.4	87.7	161.0	163.5
	(In percent of GDP)			
Total poverty-reducing spending	10.6	11.2	15.8	14.3
Current	3.5	3.8	3.9	3.7
Investment	7.1	7.5	11.9	10.6
	(In percent of total spending)			
Total poverty-reducing spending	52.3	54.0	58.2	62.6
Current	17.1	18.1	14.4	16.2
Investment	35.1	35.9	43.8	46.4
	(In billion of CFA francs)			
Memorandum items:				
GDP	1,002.4	1,175.3	1,354.1	1,541.0
Total spending	203.2	244.1	368.0	352.7

Sources: Chadian authorities; and staff estimates and projections.

1/ Defined as spending on health, education, rural development, infrastructure, and governance.

Table 8. Chad: Balance of Payments, 2000-03

	2000	2001		2002		2003	
		Prog.	Rev. Prog.	Prog.	Rev. Prog.	Proj.	Rev. Proj.
	(In billions of CFA francs)						
Current account, incl. off. current transfers	-137.8	-447.7	-483.6	-566.7	-652.7	-670.8	-759.3
Current account, excl. off. current transfers	-160.5	-463.4	-497.9	-574.9	-660.8	-683.7	-772.2
Current account, excl. pipeline imports	-112.7	-253.0	-184.3	-221.6	-266.5	-227.5	-267.2
Trade balance, incl. oil sector	-44.0	-248.7	-270.4	-319.7	-370.9	-386.2	-445.6
Trade balance, excl. oil sector	-26.8	-119.8	-72.3	-91.3	-115.4	-93.0	-120.0
Exports, f.o.b.	129.4	139.4	139.7	152.2	126.5	169.3	140.1
Imports, f.o.b.	173.3	388.0	410.0	471.8	497.4	555.5	585.7
Formal imports	136.3	326.7	351.4	405.7	435.1	484.8	518.3
Of which: pipeline-related imports	17.1	128.8	198.1	228.3	255.5	293.3	325.5
emergency cereal imports 1/	...	16.5	16.5	...	...	...	...
Informal	37.0	61.3	58.6	66.1	62.3	70.8	67.4
Services, incl. oil sector (net)	-110.9	-208.4	-221.7	-248.6	-279.1	-292.0	-319.6
Services, excl. oil sector (net)	-103.0	-142.5	-120.4	-131.8	-148.4	-142.0	-153.1
Credit	36.8	36.9	36.9	38.7	38.7	40.5	40.6
Debit	147.7	245.3	258.6	287.3	317.7	332.5	360.3
Of which: pipeline related	7.9	65.9	101.3	116.8	130.7	150.0	166.5
Factor income (net)	-6.7	-6.6	-6.2	-7.6	-7.3	-6.4	-6.3
Of which: oil-related credit	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current transfers (net)	23.8	16.0	14.6	9.1	4.5	13.9	12.2
Official (net)	22.7	15.7	14.3	8.1	8.1	12.9	12.9
Of which: HIPC Initiative grants	...	6.4	5.0	8.1	8.1	12.9	12.9
Private (net)	1.1	0.3	0.3	1.0	-3.6	1.0	-0.8
Capital and financial account	127.3	393.3	425.4	530.8	587.3	650.7	730.9
Long- and medium-term capital	130.8	390.2	423.2	526.8	586.1	647.4	719.1
Public	78.5	171.0	92.9	152.2	177.4	153.1	180.4
Project grants	48.0	86.1	40.2	60.5	88.5	61.2	89.2
Projects loans	30.5	84.9	52.6	91.7	88.8	91.9	91.3
Drawings	44.6	100.6	69.0	107.7	107.7	108.4	108.4
Repayments	-14.1	-15.7	-16.3	-16.0	-18.9	-16.3	-17.1
Private	52.3	219.1	330.4	374.6	408.8	494.3	538.6
Direct investment	51.3	219.2	328.4	375.0	415.0	488.4	532.6
Of which: direct oil project investment	26.4	198.2	304.7	351.3	393.1	451.2	500.8
Other investments	2.0	-0.4	-6.2	6.0	6.0	6.1	9.5
Of which: banking sector	3.0	1.0	1.0	1.0	1.0	3.0	3.0
Short-term capital	-3.5	3.1	2.2	4.0	1.2	3.3	11.8
Private sector	2.8	1.1	1.2	1.8	0.9	1.2	5.4
Banking sector	-6.3	2.0	1.0	2.2	0.3	2.1	6.4
Net errors and omissions	1.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-9.4	-54.4	-58.2	-35.9	-65.4	-20.1	-28.4
Financing	9.4	9.4	13.9	3.9	2.4	-5.3	-5.0
Change in official net reserves	-3.4	-3.1	-4.6	-3.5	-5.2	-5.0	-5.0
Change in arrears	3.5	-3.5	-3.6	0.0	0.0	0.0	0.0
Rescheduling of public debt and arrears	...	3.6	11.7	3.2	3.2	2.0	2.0
Use of Fund resources (net)	9.3	12.3	10.5	4.2	4.4	-2.2	-2.0
Of which: additional support for emergency food imports	...	5.1	5.2	...	...	...	...
Financing need	0.0	45.0	44.3	32.1	63.0	25.4	33.5
Identified financing	...	41.0	44.3	29.3	50.5	10.9	10.7
European Union	...	14.3	10.4	11.8	15.7	0.0	0.0
World Bank	...	17.4	28.7	10.6	21.6	10.9	10.7
African Development Bank	...	4.0	0.0	4.0	8.0	0.0	0.0
HIPC Initiative assistance	...	2.3	0.0	2.9	5.2	...	...
Other donors 2/	...	3.0	5.2	...	0.0	...	...
Financing gap	0.0	4.0	0.0	2.7	12.5	14.5	22.7
Memorandum items:	(In percent, unless otherwise indicated)						
Nominal GDP (in billions of CFA francs)	1,002.4	1,138.4	1,175.3	1,300.3	1,354.1	1,460.0	1,541.0
Current account balance (incl. official transfers)/GDP	-13.7	-39.3	-41.2	-43.6	-48.2	-45.9	-49.3
Current account balance (excl. official transfers)/GDP	-16.0	-40.7	-42.4	-44.2	-48.8	-46.8	-50.1
Current account balance (excl. off. transfers and oil sector)/GDP	-13.5	-23.6	-16.9	-17.7	-20.3	-16.5	-18.2
Gross official reserves (in billions of CFA francs)	80.2	92.7	92.7	96.2	97.9	101.2	102.9
Gross official reserves in months of imports (incl. pipeline) 3/	3.4	1.9	1.8	1.7	1.6	1.5	1.4
Gross official reserves in months of imports (excl. pipeline) 3/	3.7	2.9	3.6	3.3	3.2	3.2	3.2
Debt outstanding (in billions of CFA francs)	731.8	860.2	898.6	971.6	989.8	1,107.0	1,086.7
Debt outstanding/GDP	73.0	75.6	76.5	74.7	73.1	75.8	70.5
Debt service/exports of goods and nonfactor services 4/	13.9	...	14.2	...	17.7	...	14.8

Sources: Chadian authorities; and staff estimates and projections.

1/ Imports of 66,000 tons of cereal to meet the food shortage.

2/ External assistance for elections.

3/ In months of imports of goods and nonfactor services.

4/ Debt service due, before HIPC Initiative assistance.

Table 9. Chad: External Financing Requirements and Sources, 2001-02
(In millions of U.S. dollars)

	2001 Revised Projection	2002 Revised Program
Gross financing requirements	719.9	960.3
External current account deficit (excluding official transfers)	683.1	919.6
Debt amortization	22.4	26.3
Medium- and long-term debt	22.4	26.3
Public sector	22.4	26.3
Multilateral 1/	13.1	13.1
Bilateral	9.3	13.2
Other	...	...
Short-term debt 2/	...	...
Repayment of arrears	5.0	0.0
Gross reserves accumulation	6.3	7.2
IMF repurchases and repayments	3.1	7.2
Available financing	719.9	943.0
Foreign direct investment (net)	453.2	568.8
Debt financing from private creditors	3.0	1.6
Medium- and long-term financing	...	...
Short-term financing	3.0	1.6
<i>Of which:</i> balance of payments financing 3/	...	...
Official creditors 4/	210.5	336.2
Multilateral 1/	148.2	265.1
<i>Of which:</i> balance of payments financing 3/	55.3	63.1
Bilateral	62.4	71.1
To public sector	62.4	71.1
<i>Of which:</i> balance of payments financing 3/	5.5	...
To private sector	...	...
IMF	17.5	13.4
Accumulation of arrears (exceptional)	...	...
Other flows 5/	35.6	23.0
Financing gap	0.0	17.3
Memorandum item:		
Total balance of payments financing 3/	60.8	63.1

Sources: Chadian authorities; and staff estimates and projections.

1/ Excluding the IMF.

2/ Original maturity of less than one year. Stock at the end of the previous period.

3/ Includes those transactions that are undertaken for the purpose of financing a balance of payments deficit or an increase in reserves.

4/ Includes both loans and grants.

5/ Includes all other net financial flows, and errors and omissions.

Table 10. Chad: Monetary Survey, 2000-02

	2000	2001						2002	
	Dec.	March	June	Sep.		Dec.		March	Dec.
	Est.	Est.	Prog.	Est.	Prog.	Rev. Prog.	Rev. Prog.	Rev. Prog.	
	(In billions of CFA francs)								
Net foreign assets	35.9	27.1	10.4	49.6	26.8	39.6	41.5	41.6	47.0
Central bank	22.2	17.8	10.3	25.3	17.8	25.3	26.8	26.8	32.0
Commercial banks	13.7	9.3	0.1	24.3	9.0	14.4	14.7	14.8	15.0
Medium- and long-term liabilities	-2.3	-2.9	-2.2	-2.2	-2.4	-2.7	-2.4	-2.4	-2.2
Net domestic assets	89.7	108.5	131.8	107.8	113.7	109.9	106.2	116.1	120.7
Domestic credit	132.3	157.2	177.3	149.9	156.7	152.0	148.4	161.9	162.7
Claims on the government (net) 1/	61.9	62.7	83.8	89.0	78.6	83.4	71.2	73.5	76.9
Treasury (net)	71.4	71.9	84.8	99.4	90.6	104.9	81.2	83.5	86.9
Banking sector 2/	16.3	16.5	18.1	29.0	26.0	32.8	14.8	15.5	16.2
Central bank	28.6	32.1	32.8	30.7	31.0	32.4	22.5	...	...
Commercial banks	-12.7	-16.1	-15.2	-2.2	-5.5	-0.1	-8.2	...	...
CCP	0.5	0.5	0.5	0.5	0.5	0.5	0.5	...	...
Fund position	55.1	55.4	66.7	70.5	64.7	72.1	66.3	68.0	70.7
Other nontreasury	-9.6	-9.2	-1.0	-10.5	-12.0	-21.4	-10.0	-10.0	-10.0
Credit to the economy	70.4	94.5	93.5	60.9	78.1	68.5	77.2	88.4	85.8
Other items (net)	-42.5	-48.6	-45.6	-42.0	-43.0	-42.1	-42.2	-45.8	-42.0
Money and quasi money	123.3	132.7	140.0	155.2	138.1	146.8	145.3	155.3	165.5
Currency outside banks	80.7	86.5	90.3	104.3	85.6	102.7	86.8	90.1	91.3
Demand deposits	34.3	37.3	40.1	39.9	42.3	36.7	42.2	49.1	51.4
Time and savings deposits	8.3	8.8	9.5	11.1	10.2	7.3	16.2	16.2	22.8
	(Changes in percent of beginning-of-period money stock, unless otherwise specified)								
Net foreign assets	-2.7	-7.1	-20.7	11.1	-7.3	3.1	4.6	0.1	3.8
Net domestic assets	21.3	15.2	34.1	14.7	19.4	16.3	13.3	6.8	10.0
Domestic credit	24.7	20.2	36.6	17.9	19.8	19.6	13.1	9.3	9.8
Claims on the government (net) 1/	18.1	0.7	17.8	22.0	13.6	17.5	7.6	1.6	3.9
Treasury (net)	20.1	0.4	10.9	22.7	15.6	27.1	7.9	1.6	3.9
Credit to the economy	6.6	19.5	18.7	-4.1	6.2	2.1	5.5	7.7	5.9
Credit to the economy (annual change)	11.6	...	...	...	...	4.0	9.7	...	11.1
Money and quasi money 3/	18.3	7.6	13.5	25.8	12.0	19.0	17.8	6.9	13.9
Currency outside banks	12.0	4.7	7.8	19.1	4.0	17.9	5.0	2.2	3.1
Demand deposits	4.4	2.4	4.7	4.5	6.4	1.9	6.4	4.7	6.3
Time and savings deposits	1.9	0.4	1.0	2.2	1.6	-0.8	6.4	0.0	4.6
Memorandum items:									
Nominal GDP (in billions of CFA francs)	1,002.3	...	...	...	...	1,138.4	1,175.3	...	1,354.1
Money multiplier (M2 as a fraction of base money)	1.3	...	...	...	...	1.3	1.4	...	1.4
Money velocity (GDP relative to M2)	8.1	...	...	...	...	7.8	8.1	...	8.2
Gross reserves (in percent of M2)	65.0	...	...	...	...	66.5	64.8	...	60.1

Source: Bank of Central African States (BEAC); and staff estimates and projections.

1/ Including net use of Fund resources.

2/ Data reflects the definition used by BEAC headquarters.

3/ Changes in percentage. For the quarterly data, changes are cumulative.

Table 11. Chad: Social Indicators, 1999 1/

	Chad	Sub-Saharan Africa
Total population, midyear (millions)	7.5	642.8
Growth rate (percent; annual average)	3.0	2.6
Urban population (percent of population)	23.5	33.8
Life expectancy at birth (years)	48.5	46.8
Male	46.9	45.9
Female	50.2	47.7
Total fertility rate (births per woman)	6.3	5.3
Mortality		
Infant (per thousand live births)	101	92
Under 5 (per thousand live births)	189	161
Child malnutrition (percent under 5 years)	39	40
Access to safe water (percent of population)	24 (1996)	...
Urban	48 (1996)	83 (1996)
Rural	17 (1996)	75 (1996)
Immunization rate (percent under 12 months)		
Measles	49	57
DPT	33	59
Gross primary enrollment (percent of school-age population)	58 (1997)	78 (1997)
Male	76 (1997)	74 (1997)
Female	40 (1997)	67 (1997)
Gross secondary enrollment (percent of school-age population)	10 (1997)	27 (1997)
Male	15 (1997)	27 (1997)
Female	4 (1997)	23 (1997)
Illiteracy (percent of population age 15+)		
Male	50	31
Female	68	47
Daily newspapers (per thousand people)	0.3 (1996)	...
GNP per capita (U.S. dollars)	215	513

Source: World Bank, *World Development Indicators*, 2001.

1/ Unless another year specified.

N'Djaména, December 20, 2001

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington D.C., USA

Dear Mr. Köhler:

1. On behalf of the government of Chad, we are pleased to transmit to you the attached memorandum of economic and financial policies (MEFP). It describes developments during the first three quarters of 2001 and the outlook for the rest of the year in the context of the second annual program supported by a Poverty Reduction and Growth Facility (PRGF) arrangement. It also outlines the government's economic, financial, and poverty-reducing objectives and policies for 2002.
2. As explained in the MEFP, Chad met all quantitative performance criteria at end-September 2001, except those for government revenue and the nonaccumulation of external arrears. The main reason for the nonobservance of the revenue target was weak administrative capacity, while –small amounts of– external arrears reoccurred against the backdrop of some CFAF 30 billion (equivalent to 3 ½ percent of GDP) in shortfalls in external financing. Progress was made on the reform agenda. The audit of the use of the oil bonus was completed, thus the associated structural performance criterion at end-September satisfied, with a few weeks delay. At the same time, the structural benchmark at end-September to adopt the guidelines for the taxation and pricing of the Sédigi oil and gas field could not be observed, as discussions over this plan took longer than earlier envisaged.
3. Against this background, the government of Chad has introduced a policy package aiming at strengthening both revenue collection and expenditure control. External arrears were also eliminated following the receipt of part of the expected external financing; Chad will remain current on its external obligations over the program period. In addition, steps have been taken to ensure a full catch-up in the structural areas. These are described in detail in the MEFP; two of them constitute prior actions for the completion of the program review. On the basis of these actions, the government of Chad requests waivers for nonobservance of the above-described performance criteria. The government of Chad believes that these measures and policies for 2002, including the submission to parliament at end-November 2001 of the 2002 budget along the lines of the understandings reached with the IMF, provide a basis for the completion of the third review under the second annual program under the PRGF arrangement.
4. The government of Chad expresses its deep appreciation for the IMF's prompt help in addressing emergency food needs in the face of famine in the form of an augmentation of the access to quota under the second annual PRGF-supported program (equivalent to 10 percent

of quota). As part of an international effort, this assistance was important in averting famine in Chad through the autumn of 2001. There is a remainder of the assistance of CFAF 3 billion, which the Chadian government wishes to use to build up food security stocks that have been depleted during 2001.

5. The decline in the world market price of cotton (Chad's main export commodity), has created an additional financing need of US\$24 million in 2002. While the gap will be reduced by an additional fiscal adjustment effort and additional financing from the World Bank, a balance of payments need of US\$7.3 million will remain to be covered, for which Chad hereby requests an increase of the arrangement of SDR 5.6 million (corresponding to 10 percent of quota). This increase would be equally distributed upon the approval of the third review under the PRGF, and that of the third annual program, around May 2002. This additional support is crucial for the implementation of the ongoing cotton sector reform, as described in the MEFP.

6. Despite the progress in recent years, not least thanks to assistance from the Fund, Chad's administrative capacity remains below what our government needs to implement its ambitious poverty-reducing program and prepare for the petroleum era. Therefore, in the context of the Fund's new Africa Capacity Building Initiative, the government of Chad hereby requests a substantial increase in Fund technical assistance over the program period in the areas described in the MEFP.

7. The preparation of Chad's poverty reduction strategy paper (PRSP), in a fully participatory manner and involving development partners, is expected to be finalized by the end of the first quarter of 2002. A PRSP preparation status report has been completed for a joint staff assessment by the Fund and the World Bank.

8. The fourth review under the PRGF arrangement will be completed by end-June 2002 and will consider, inter alia, budget implementation in 2002, and actions in the revenue and expenditure management areas. The government of Chad will continue to provide the Fund with all information that the Fund requests in connection with the implementation of the MEFP, and it will consult with the Fund regarding the implementation of any major policy initiatives not considered during the program discussions. During the arrangement period, the government of Chad stands ready to take any additional measures that may become appropriate to ensure the achievement of the program's goals.

Very truly yours,

Idriss Ahmed Idriss
Minister of Finance

Nagoum Yamassoum
Prime Minister

Attachments: Memorandum of Economic and Financial Policies
Addendum to the Technical Memorandum of Understanding

MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

N'Djaména, December 20, 2001

I. DEVELOPMENTS IN 2001 UNDER THE PRGF-SUPPORTED PROGRAM

1. During 2001, the government of Chad has aimed at implementing a comprehensive program of economic, structural, and poverty-reducing reforms. This program received support from the International Monetary Fund (IMF) under a Poverty Reduction and Growth Facility (PRGF) arrangement, approved on January 7, 2000. The second review of the arrangement was completed on May 16, 2001. On that occasion, the Executive Directors of the IMF also decided that Chad had reached the decision point under the enhanced Initiative for Heavily Indebted Poor Countries (HIPC). In June, the Paris Club provided a flow debt rescheduling of Chad's external debt on Cologne terms. On September 28, 2001, the Executive Board of the IMF evaluated Chad's economic performance at end-June 2001 and approved the disbursement of the fourth loan.
2. Program implementation has been broadly satisfactory, despite often difficult circumstances. These included weak food production in 2000/2001, which raised the threat of famine, and recurrent rebel fighting in the northern part of the country. Program implementation has been further complicated by a substantial shortfall in external financing, including from the European Union, as well as continued weaknesses in administrative capacity. At the same time, the medium-term economic outlook has improved considerably, following the acceleration of the Doba oil project. As a result, real GDP is now expected to grow by 8.9 percent in 2001, compared with 8.2 percent, as originally programmed. The current account deficit, excluding official transfers, is projected to widen to 42.4 percent of GDP, compared with 40.7 percent under the program, reflecting primarily higher imports associated with the Doba project. Much of the deficit is financed by foreign direct investment. Consumer prices are expected to increase by 12.4 percent, mainly owing to the food shortages.

A. Performance Through End-September 2001

3. Despite the above-mentioned difficulties, overall economic performance through the first three quarters of 2001 was broadly satisfactory. Chad met all quantitative criteria at end-September 2001, except for fiscal revenue and the continuous criterion for the nonaccumulation of external arrears. A CFAF 6.2 billion shortfall in revenue was more than offset by cuts in expenditure, so that the performance criterion on the primary current balance was observed. However, the structure of expenditure was unfavorable, as defense spending (related to the above-mentioned rebellion in the north and to the fight against organized crime) was somewhat above projection, while spending on social sectors was below the program target. The latter reflected the fact that spending from the virtual Poverty Fund—which combines resources from HIPC Initiative interim assistance and the remainder of the

oil bonus—reached only CFAF 1 billion, considerably lower than programmed, owing to administrative start-up difficulties.¹ Net bank credit to government was limited to CFAF 6.0 billion, against the target of CFAF 15.7 billion, thus the associated performance criterion was met. At the same time, the government had accumulated CFAF 8.7 billion of domestic arrears. In the face of the continued shortfall in external financing, some external arrears also accumulated, reaching CFAF 0.9 billion by end-October, thus the associated continuous performance criterion was not met.²

4. Progress was made in structural reforms, albeit slower than programmed. In the fiscal area, the value-added tax (VAT) administration has been strengthened and the SYDONIA computer system has been installed at N'Djaména airport and at the custom's entry point of N'guéli. The assignment of tax identification numbers (TINs) to all identified economic agents has progressed as scheduled. The 12-month treasury cash plan has regularly been updated twice a month. The new, streamlined expenditure circuit has been prepared for adoption, and the related procedures handbook has also been compiled. Moreover, 27 inactive government accounts in the banking system have been closed. In the governance area, the audit of the use of the oil bonus as of end-December 2000 has been completed in conformity with its terms of reference, albeit later than expected; thus the associated structural performance criterion has been satisfied with a few weeks delay. The bidding procedures to recruit an internationally reputable firm for the functional and financial audit of the customs and the bidding procedures for the audit of the five biggest procurement contracts signed in 2001 have both been launched as scheduled. The first procurement bulletin has been published, albeit with some delay. Moreover, the government has requested technical assistance from the World Bank to reconsider its planned contract with the consortium IECI to exploit the gas of the Sédigi field. In addition, the soundness of the banking system has been strengthened, owing to the increase in capital of a private bank in a difficult financial situation. In contrast, the principles guiding the pricing and taxation mechanisms of the oil and gas of the Sédigi field could not be adopted by end-September, as discussions within the government took more time than earlier envisaged; thus the associated structural benchmark was not observed. Progress in areas covered by World Bank conditionality—reforms of the civil service, the procurement system, and the cotton sector, and the government's privatization program—has been good. Moreover, an action plan in the area of governance was prepared and transmitted to the High Interministerial Committee.³

¹ These were mainly related to the fact that the Oil Revenues Control and Monitoring Board (CCSRP), in charge of approving the use of oil revenues, was not yet operational.

² All external arrears have been cleared as of December 18, 2001.

³ This progress provided a basis for an agreement with the World Bank on the Fourth Structural Adjustment Credit facility (SAC IV), which was discussed by the Bank's Executive Board on December 18, 2001.

5. Further progress has been made toward preparing a fully participatory poverty reduction strategy paper (PRSP), as described in the government's PRSP preparation status report. An updated macroeconomic framework is being prepared, and the costing of the identified priority measures has been broadly completed. Some progress has already been made toward achieving the completion point conditions under the enhanced HIPC Initiative, such as the completion of the budget cycle, and improvements in selected health, education, and transportation indicators.

B. Outlook for the Rest of 2001

6. The government of Chad is committed to making every effort to keep the PRGF-supported program on track, and it is taking additional measures to ensure a catch-up in areas where recently program implementation has suffered some delays. Against the backdrop of the shortfall in **fiscal revenue**, the government has taken the following measures: (i) acceleration of the collection of tax arrears, including VAT arrears; (ii) intensification of customs control including, inter alia, daily inspection visits to the N'Djaména airport and weekly random inspection at the N'guéli import entry post; the submission to the Council of Ministers of a report on the findings of a four-week implementation of such inspections was a prior action for the completion of the review;⁴ (iii) restructuring and strengthening of the joint tax-customs brigade's controls, with technical assistance from the Fund; (iv) establishment of a procedure to verify ex post all exempted imports under the Doba project, so as to ensure that non eligible transactions do not benefit from the project's tax exempt status; (v) continued update of the distribution of the tax identification numbers (TINs) and strict reinforcement of the policy of not granting public contracts to firms without a TINs; (vi) acceleration of the computerization of the large-taxpayer unit; (vii) centralization of tax control by merging the two agencies in charge; and (viii) broadening of the tax base through coverage of the large informal sector, including by following up on the census of companies in greater N'Djaména through the assignment of TINs to newly identified economic agents. Nevertheless, in the short run, these measures are not expected to allow for a full catch-up in fiscal revenue, so that the revenue target for end-December has been revised downward from CFAF 96 billion to CFAF 92 billion.

7. The government will continue to **reinforce further expenditure control**, although the scope for cutting or postponing spending commitments is limited, in view of the government's objective of protecting social sector outlays. To this ends, the Prime Minister will continue to be regularly informed on the cash-flow situation, so as to ensure that the revised decisions reflect the government's objective of protecting social sector outlays. However, owing to the above-mentioned administrative difficulties, the structure of expenditures will be affected by the postponement to 2002 of a large part of Poverty Fund-financed spending. The government will clear its domestic arrears accumulated in the course of 2001, including those to the National Water and Electricity Company (STEE).

⁴ This prior action was fulfilled on December 12, 2001.

8. **Public expenditure management** will be further strengthened. The full implementation of the new, streamlined, and computerized expenditure circuit will start on December 1, 2001. Beginning that date, no expenditure commitment will be made or executed outside the computerized expenditure circuit. In order to fully integrate the investment budget into the fiscal accounts, as well as with the use of the new expenditure circuit, the monitoring of all —both domestically and foreign-financed— investment will be strengthened. To this ends, all project managers, including of projects financed by foreign funds, will report monthly to the Budget Department, as well as to the Treasury Department, and the monthly treasury cash plan will include the execution of investment projects, starting on January 1, 2002.

9. In the structural area, the adoption of the principles guiding the pricing and taxation of the gas and oil of the Sédigi field constitutes a prior action. In other structural areas covered by World Bank conditionality, the national road maintenance company (SNER) will be privatized before end-December 2001; and the tender for the bids for the privatization of DHS will be launched by end-December 2001.

II. ECONOMIC AND FINANCIAL POLICIES IN 2002

A. Macroeconomic Framework

10. The economic outlook for 2002 is being reshaped by the acceleration of investment linked to the Doba oil field project and its spillover effects on the rest of the economy. Real GDP is now projected to increase by about 11 percent in 2002. Oil is expected to come onstream by the beginning of 2004, as compared to the earlier projection of 2005. Investment is also being carried out to exploit the Sédigi oil and gas field, with oil expected to start flowing by late 2003. As a share of GDP, investment is projected to increase from 43 percent in 2001 to 52 percent in 2002, with two-third of this representing private investment. The external current account deficit in 2002 is expected to be higher than earlier envisaged —49 percent of GDP, compared with 44 percent under the original program, owing to both higher imports associated with the acceleration of the Doba project and lower exports stemming from the decline in the world market prices for cotton. The deficit is expected to be covered by foreign direct investment (US\$ 578 million, or 30.6 percent of GDP); official transfers (6.5 percent of GDP); and exceptional budget support and balance of payments financing (4.6 percent of GDP).

11. Consumer prices are projected to increase by an average of 4 percent in 2002, following a return to normal food production in the 2001/02 agricultural campaign.

B. Fiscal Policies

12. The government's fiscal policy aims at containing the primary current deficit⁵ (excluding elections and famine-related spending) at CFAF 17.2 billion in 2002 (1.3 percent of GDP), after CFAF 3.3 billion (0.3 percent of GDP) in 2001, reflecting the adverse impact of the cotton crisis on public finances. Achieving this target will require both a continuous revenue effort and expenditure restraint, given the available budget resources. The overall balance, on a commitment basis and excluding grants, is expected to widen from CFAF 152 billion (13 percent of GDP) in 2001 to CFAF 261 billion (19 percent of GDP) in 2002, mainly reflecting a significant increase in foreign-financed public investment.

13. Total government revenue, excluding grants, is targeted to increase from CFAF 92.2 billion (7.8 percent of GDP) in 2001 to CFAF 107.3 billion (7.9 percent of GDP) in 2002, as a result of efforts to strengthen tax administration.⁶ In addition to the above-described measures taken in the last quarter of 2001, tax collection will be further strengthened through the following measures: (i) implementation of an action plan, which will be prepared and adopted by end-May 2002 on the basis of the audit of the customs administration; (ii) adoption of above-described identified ex post verification procedures for the Doba oil project imports by March 15, 2002 (a structural performance criterion under the program); (iii) a study on the reform of the general lump-sum tax (IGL—small taxpayer taxation) will be prepared by end-June 2002, with technical assistance from the Fund, with a view to introducing the reform in the context of the 2003 budget; (iv) the launching of the linking up of the computer networks of the customs administration, the large-taxpayer unit, and the expenditure circuit; (v) improving fiscal control via the following mechanism: the Public Procurement Department will transmit to the Tax Department by January 15, 2002 the list of all companies that were granted in 2000 or 2001 public contracts for an amount exceeding the ceiling for the IGL. On the basis of this information, the Tax Department will check the fiscal status of these companies and notify the tax adjustment when necessary. Reports on the findings will be published in the Public Procurement Bulletin by March 31, 2002 for the contracts awarded in 2000 and by June 30, 2002 for the contracts awarded in 2001; and (vi) the reinforcement of the collection of the tax on cattle sale.

14. Expenditure policies will aim at making decisive progress toward achieving the HIPC Initiative completion point conditions for the priority sectors. Overall expenditure will rise from CFAF 244 billion (21 percent of GDP) in 2001 to CFAF 368 billion (27 percent of

⁵ It is envisaged that, for the third annual program under the PRGF arrangement, which is expected to start on April 1, 2002, the program's fiscal target will be redefined as the base primary fiscal balance (which is the current primary fiscal balance minus domestically financed investment), i.e., the convergence indicator in the CEMAC zone.

⁶ As a share of non-oil GDP, total revenue, excluding grants, would increase from 8.3 percent to 8.9 percent over this period.

GDP) in 2002, mainly reflecting an increase in public sector investment, including those financed from the virtual Poverty Fund. The total wage bill will rise by 13.6 percent, on account of statutory promotions, a 10 percent wage increase in the health sector, and an increase in employment, concentrated in priority sectors (health, education, basic infrastructure, rural development, and governance). Goods and services spending in nonpriority sectors will be broadly frozen at their 2001 level, whereas that in the priority sectors will increase by 34 percent in real terms, as a result of the spending deferred from 2001, as explained below. Transfers will increase significantly on account of an exceptional financial support to the cotton sector and efforts to rehabilitate STEE. Public sector investment will concentrate in priority sector areas. As a result, overall priority sector spending will rise from 11.2 percent of GDP in 2001 to 15.8 percent in 2002, and the share of priority-sector spending in overall expenditure will increase from 54 percent to 58.2 percent respectively. The government will continue to clear its stock of domestic arrears by repaying CFAF 4.8 billion in 2002.

15. Chad will continue to benefit from interim assistance under the enhanced HIPC Initiative. This assistance will be effected through the virtual Poverty Fund, whose use is explicitly identified in a separate column of the 2002 budget. Procedures to transfer resources to the virtual Poverty Fund will be strengthened: starting on January 1, 2002, the government will transfer to the Bank of Central African States (BEAC) the full amount of debt service due, and the BEAC will be in charge of transferring to the Poverty Fund the corresponding amount of resources available as a result of the interim HIPC Initiative assistance. The total expected interim assistance in 2002 amounts to CFAF 11 billion (0.8 percent of GDP). Planned expenditures are as follows: (i) health and social affairs, CFAF 2.7 billion; (ii) education, CFAF 1.9 billion, chiefly on primary education; (iii) governance, CFAF 1.8 billion; (iv) infrastructure, CFAF 1.5 billion; and (v) rural development, CFAF 3.1 billion. The unused remainder of the virtual Poverty Fund resources at end-December 2001, a projected CFAF 8.2 billion, will also be spent in the context of the 2002 budget. As a result, the total available resources of the Poverty Fund will amount to CFAF 19.2 billion in 2002. As mentioned, the 2002 budget is tailored toward meeting the quantitative conditions for the completion point under the enhanced HIPC Initiative. The government of Chad aims at meeting all those conditions by the beginning of 2003, except for the requirement of a yearlong implementation of the full PRSP (see below).

16. The government will take major steps to **strengthen public expenditure management**. First, a close monitoring of budget implementation through the biweekly updating of the treasury cash plan and the new tables to monitor the expenditure circuit will help avert the recurrence of payments arrears. These new monitoring tables, which will track spending through the four stages of the streamlined expenditure chain (commitment, validation, payments order, and actual payment), will start on January 1, 2002, and their compilation for a full month will be a structural performance criterion for February 15, 2002. Second, as mentioned, starting on January 1, 2002, the monthly implementation of the investment budget will be included in the treasury cash plan. Third, the government has established an explicit contingency spending plan for an amount of CFAF 12 billion. This spending will be authorized only in the fourth quarter of 2002, and only after its financing

has been fully secured. The government will agree on the composition of this spending with the Fund. Fourth, following the recommendations of the World Bank, medium-term public expenditure programming will be initiated in the first quarter of 2002. Fifth, the government will discontinue its practice of paying its suppliers in cash. Also, a committee will be set up to define the modalities under which the payment of civil servant wages can also be made by electronic bank transfer, with a view to starting the implementation of this reform in 2003. These measures will also have a positive impact on the deepening of the monetization of Chad's economy thus the development of the banking sector. Finally, starting in the third quarter of 2002, the quarterly report on budget execution will include also a functional classification of expenditure.

17. The above-described measures are reflected in the 2002 budget, whose submission to parliament was a prior action for the completion of the third PRGF review. This prior action was met on November 29. As mentioned, the budget included, in a fully integrated manner, the government's program regarding the use of the interim assistance under the enhanced HIPC Initiative.

18. It is envisaged that the first biannual report on poverty-reducing spending as of end-December 2001 (specifically tracking spending financed by the HIPC Initiative resources), prepared by a committee headed by the Minister of Finance, will be completed by end-March 2002, and the second report as of end-June 2002 by end-September 2002. These reports will also describe progress made toward achieving the HIPC Initiative completion point conditions.

C. Governance

19. The government reiterates its strong commitment to strengthening transparency and good governance. To this end, in the areas covered by Fund conditionality, the government is committed to follow the recommendations made by the Accountant General's Office of the Supreme Court in the context of the audit of the use of the oil bonus as of end-December 2000. In addition, another action plan will be adopted by end-June 2002 as a follow-up to the findings of the audit of the five biggest public contracts awarded in 2001; the completion of this audit is expected by end-April 2002. On the basis of this audit, a methodology will be adopted to conduct regular audits of public contracts, as well as the public procurement system. Furthermore, the government reiterates its commitment not to award any procurement contract or sale of a national assets contract, without following transparent and competitive procedures. The report on the exploitation of the gold mine of Pala will be published by January 15, 2002. Additional areas covered by World Bank conditionality include: the audit of major public contracts awarded in 2002 according to the above-mentioned methodology; the adoption of the government's national governance strategy by the end of the first quarter of 2002 and its implementation throughout the rest of the year; the adoption of a new Public Procurement Code; and the creation of an independent procurement appeals system.

D. Monetary Prospects

20. Monetary policy is being conducted at the regional level by the BEAC. The bank's key objective is to maintain price stability over the medium term by maintaining the peg between the CFA franc and the euro, and to build up the monetary zone's official reserves. After a peak in 2001, mainly owing to food shortages, consumer price inflation is expected to return to sustainably low levels; consumer prices are projected to increase by about 4 percent on average in 2002.

21. Banking supervision will continue to be strengthened by the regional Central African Banking Commission (COBAC). An additional increase in capital of the above-mentioned private bank is envisaged by its private stakeholder. Banks will be encouraged to diversify their deposit base, which have so far relied heavily on public deposits, as well as their lending activities, in particular in the context of the Doba oil project. Strengthening most banks' management and accelerating their computerization will also be necessary. The government, together with the COBAC and with help from its development partners, will design and adopt by end-June 2002 the policy and legal framework for microfinance in Chad, in line with the guidelines of the Central African Economic and Monetary Community (CEMAC).

E. Balance of Payments Financing Needs

22. In 2002, the sharp decline in world market prices for cotton is projected to result in an additional balance of payments financing need of US\$24 million. The government of Chad will make an additional fiscal adjustment to absorb part of this gap in the form of cuts in nonpriority sectors nonwage spending; nevertheless, a substantial balance of payments need remains to be covered, for which the government is seeking additional financing from the World Bank, and requests an SDR 5.6 million augmentation of the PRGF arrangement (equivalent to 10 percent of quota) from the Fund. Half of this amount would be distributed upon the completion the third review under the PRGF arrangement, and the second half at the time of the fourth review.

F. Structural Reforms

23. In addition to the above-described measures in the fiscal and governance and transparency areas, the government will continue to implement its ambitious structural reform agenda in the areas covered by World Bank conditionality. The privatization agenda in 2002 is expected to include the following: (i) DHS, the oil and soap unit of Cotontchad; (ii) the reduction of the government's share in Sotexho, a hotel management company; (iii) the awarding of the third mobile phone license; and (iv) the sale of air traffic rights. Cotton sector reform, which aims at durably increasing producers' income and productivity, will continue as scheduled. In particular, a study will be launched in 2002 to identify possible scenarios for the privatization of Cotontchad. The final scenario will be adopted by end-2002 following a forum of investors and cotton producers, and a bidding process to find private stakeholders. The ultimate objective is the privatization of Cotontchad in 2003. Civil service

reform will continue, with a view to completing it by 2003. After the adoption of the new civil service statutes by parliament, the merit-based advancement and competitive recruitment will start to be implemented. The harmonized and computerized payroll and civil service files will be concluded by mid-2002, and an organizational, procedural, and human resources audit will be conducted for seven pilot ministries by end-2002.

G. PRSP Process

24. The preparation of the PRSP in a fully participatory process and involving development partners is well under way. After updating the macroeconomic framework and costing all identified measures, the steering committee in charge of overseeing the preparation of the PRSP will organize a series of seminars to discuss the work in progress and help strengthen the quality of the document. The authorities' PRSP preparation status report describes this process. It is expected that the PRSP will be finalized by the end of the first quarter of 2002.

H. Pressing Technical Assistance and Capacity-Building Needs

25. Despite progress made in selected areas with technical assistance from development partners, including the Fund, Chad's administrative capacity remains below what is required for the fully effective implementation of the government's poverty-reducing policies. The government welcomes the Fund's new Africa Capacity Building Initiative and requests that the Fund increase its technical assistance to Chad substantially over the PRGF arrangement period. The areas of immediate assistance needs include (i) macroeconomic forecasting, including a concentrated macroeconomic forecasting seminar in N'Djaména for the staff of the main government institutions; (ii) budget preparation and budget execution monitoring; and (iii) the statistical database. In the latter respect, the government requests additional Fund assistance to help implement the recommendations of the 2000 May multisectoral statistical mission.

III. PRIOR ACTIONS FOR THE REVIEW AND PROGRAM MONITORING

A. Prior Actions for the Third Review

26. The following measures constitute prior actions for the staff to recommend the completion of the third review under the PRGF arrangement:

- adoption of the guidelines for the pricing and taxation of the Sédigi field's oil and gas;
- submission to the Council of Ministers of a report on the findings of a four-week implementation of daily inspection visits to the N'Djaména airport and weekly random inspection at the N'guéli import entry post (this prior action was fulfilled on December 12);

- submission to parliament of the 2002 budget in accordance with the above-described measure (this measure was fulfilled on November 29); and
- clearing of all outstanding external arrears (this prior action was fulfilled on December 18).

B. Program Monitoring

27. Program implementation will continue to be monitored in reviews that are scheduled on a semiannual basis, while performance criteria will continue to be set on a quarterly basis, with associated quarterly disbursements. The fourth review and the negotiation of the third annual program under the PRGF-supported three-year arrangement will take place before end-June 2002. Quantitative and structural performance criteria and structural benchmarks are established for end-December 2001 and end-March 2002, while indicative targets are set for end-June 2002 (Appendix I, Table 1). The proposed quantitative performance criteria will continue to be the following: (i) a ceiling on the increase in net credit from the banking system to the central government; (ii) a floor on the current primary fiscal balance; (iii) a floor on total fiscal revenue (excluding grants); (iv) the nonaccumulation of central government external payments arrears; (v) a ceiling on new medium- and long-term nonconcessional external debt contracted or guaranteed by the central government; (vi) a ceiling on net change in external debt with a maturity of up to and including one year. Indicative benchmarks are set for (i) a floor on current expenditure on health; (ii) a floor on current expenditure on education; and (iii) a ceiling on the total wage bill (including the military sector). In addition, the measures indicated in Table 2 of this appendix will serve as performance criteria and structural benchmarks.

Table I. Chad: Quantitative Performance Criteria and Benchmarks for the Second Annual Program
Under the Poverty Reduction and Growth Facility Arrangement, 2001-02

(In billions of CFA francs)

	Cumulative Changes from January 1, 2001		Cumulative Change from January 1, 2002	
	End-Dec. 2001		End-March 2002	End-June 2002
	Ind. Bench.	Crit.	Crit.	Ind. Bench.
Quantitative performance criteria				
Ceiling on the increase in net credit of the banking system to the central government (excluding IMF resources) 1/	11.2	0.7	2.1	9.3
Floor on current primary fiscal balance 2/	-3.3	-3.3	-3.9	-3.2
Floor on total government revenue, excluding grants 3/	96.0	92.2	23.7	50.9
Nonaccumulation of external payments arrears of the central government (cumulative since Jan. 1, 2001) 4/ 5/	0.0	0.0	0.0	0.0
Ceiling on new nonconcessional external debt with maturities of more than one year contracted or guaranteed by the central government (cumulative) 6/	0.0	0.0	0.0	0.0
Ceiling on net change in external debt with a maturity of up to and including one year, except normal trade financing (cumulative)	0.0	0.0	0.0	0.0
Indicative benchmarks 7/				
Floor on current expenditure on health 8/	9.4	8.7	2.6	5.3
Floor on current expenditure on education 8/	19.6	18.3	5.6	11.2
Ceiling on total wage spending by the central government (including military)	57.3	56.3	16.0	32.0
Adjusters				
Net reduction of domestic payments arrears of the government	7.0	6.7	0.3	0.3
Privatization revenue	3.0	1.4	0.0	0.0
Balance of payments assistance 9/	46.4	55.9	8.4	11.2
Adjustment lending (excl. IMF)	21.4	28.7	3.7	3.7
Adjustment grants	21.3	15.5	3.9	5.9
Debt relief excluding HIPC Initiative	3.6	11.7	0.8	1.6

Sources: Chadian authorities; Bank of Central African States (BEAC); and staff estimates and projections.

1/ The targets will be adjusted (i) upward for a shortfall in balance of payments assistance (as identified in the adjusters and excluding projected lending and grants) up to an amount equivalent to 75 percent of the shortfall; (ii) downward (respectively upward) to take account of a lower (higher) repayment of domestic arrears than foreseen under the program for the corresponding period; and (iii) upward for a shortfall in sales of assets revenue up to an amount equivalent to 75 percent of the shortfall.

2/ Defined as total revenue less grants, minus current primary spending (current spending, less electoral and famine-related outlays and less interest payments).

3/ Net of reimbursements under the system of treasury checks.

4/ Monitored on a continuous basis.

5/ Excluding external payments arrears incurred pending debt rescheduling.

6/ Nonconcessional loans defined as loans with a grant element of less than 35 percent, using discount rates based on the commercial interest reference rates (CIRRs). An exception will be made for a nonconcessional IBRD loan in an amount of US\$35 million contracted by the government of Chad in the context of the Chad-Cameroon Pipeline Project.

7/ These indicators will not constitute performance criteria of the program.

8/ Including wages.

9/ Including the possible financing recorded in the financing gap.

Table 2. Chad: Structural Performance Criteria and Benchmarks for the Second Annual Program Under the Poverty Reduction and Growth Facility Arrangement

Criteria and Benchmarks	Test Date
Structural performance criteria	
Finalization of the first full set of the biweekly expenditure sheets with the four stages of the new, streamlined expenditure circuit (commitment, validation, payments order, and actual payment)	February 15, 2002
Adoption by the Council of Ministers of procedures for ex post verification of all tax-exempted products under the Doba project	March 15, 2002
Structural benchmarks	
Publication in the <i>Public Procurement Bulletin</i> of a report on the results of the inspection of companies that were awarded in 2000 public contracts for an amount exceeding the ceiling for the general lump-sum tax (IGL)	March 31, 2002
Adoption of an action plan by the Council of Ministers on the basis of the recommendations of the international audit of the customs	May 31, 2002

INTERNATIONAL MONETARY FUND

CHAD

**Addendum
to the Technical Memorandum of Understanding
Relative to the Second Annual Program under
the Poverty Reduction and Growth Facility Arrangement**

N'Djaména, 20 December 2001.

The technical memorandum of understanding relative to the second annual program under the arrangement supported by the Poverty Reduction and Growth Facility and attached to the letter of intent signed on April 28, 2001 and considered by the Executive Board of the International Monetary Fund on May 16, 2001 still applies for the remainder of the arrangement. However, starting December 1, 2001, paragraph 7 is modified and now reads as follows:

7. The ceiling on the cumulative change, from the beginning of the calendar year, on net credit of the banking system to the government will be adjusted downward by any shortfall in the actual net reduction of domestic payments arrears relative to the programmed amounts as shown in Table 1 attached to the memorandum of economic and financial policies, or upward for any repayment in excess of the target numbers. Arrears variations are calculated as the total amount of committed expenditures (data provided by the Department of Budget of the Ministry of Finance) minus the total amount of paid expenditures (data provided by the Department of Treasury of the Ministry of Finance).⁷

⁷ With the exception of arrears to the National Pension Fund (CNRT), which are subject to a specific convention and treated as internal debt.

Chad: Relations with the Fund
(As of November 30, 2001)

I. Membership Status: Joined 7/10/63; Article VIII

II. General Resources Account:	SDR Million	% Quota
Quota	56.00	100.00
Fund holdings of currency	55.72	99.50
Reserve position in Fund	0.28	0.50

III. SDR Department:	SDR Million	% Allocation
Net cumulative allocation	9.41	100.0
Holdings	0.00	0.03

IV. Outstanding Purchases and Loans:	SDR Million	% Quota
ESAF and PRGF Arrangements	71.00	126.79

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Poverty Reduction and Growth Facility (PRGF)	01/07/2000	01/06/2003	42.00	23.80
Enhanced Structural Adjustment Facility (ESAF)	09/01/1995	04/30/1999	49.56	49.56
Stand-By Arrangement	03/23/1994	03/22/1995	16.52	10.33

VI. Projected Obligations to Fund (SDR Million; based on existing use of resources and present holdings of SDRs):

	Overdue	Forthcoming				
	11/30/01	2001	2002	2003	2004	2005
Principal	0.1		5.8	7.4	9.1	10.4
Charges/interest		0.2	0.6	0.5	0.5	0.4
Total	0.1	0.2	6.4	7.9	9.6	10.8

VII. Implementation of HIPC Initiative:

	<u>Enhanced framework</u>
Commitment of HIPC assistance	
Decision point date	05/16/2001
Assistance committed (NPV terms)	
Total assistance (US\$ million)	170.00
<i>Of which:</i> Fund assistance (SDR million)	14.25
Completion point date	Floating
 Delivery of Fund assistance (SDR million)	
Amount disbursed	2.85
Interim assistance	2.85
Completion point	0.00
Amount applied against member's obligations (cumulative)	1.42

VIII. Safeguards Assessments:

Introduction

The Bank of the Central African States (BEAC) is the common central bank of the central African states, which includes Cameroon. A Stage Two (on site) safeguards assessment of the BEAC proposed specific remedies to alleviate vulnerabilities that were identified by staff. The authorities have committed themselves to implementing most of the proposed remedies, as described in the following sections.

Safeguards Areas and Main Remedies

The External Audit mechanism: The auditing function and the quality control procedures of the external auditor are adequate. The safeguards assessment proposed that (i) the external auditor refer explicitly to the international standards of auditing (ISA) in its opinion; (ii) the external auditor become more cognizant of the accounting rules applicable to the recording of Fund's balances; and (iii) the BEAC should include the audit opinion in the annual publication of the financial statements. The management of the BEAC has agreed to implement these actions for the FY 2002 accounts.

Legal Structure and Independence: The legislation governing BEAC is adequate.

Financial Reporting: The monthly statements of the bank's financial position are not published in any form, and the December 31, 2000 audited financial statements were not published in a timely manner. The staff recommended that the BEAC (i) enhance the readability and the credibility of the published annual accounts by including detailed explanatory notes on the accounting methods followed, and if these methods referred explicitly to a generally accepted accounting framework; (ii) adopt International Accounting Standards; and (iii) change the accounting of some of its operations with the Fund, especially with regard to the revaluation of the IMF accounts. The management of the BEAC has agreed to implement these recommendations by FY 2002.

Internal Audit Mechanism: The quality of the personnel, the rigorous methods followed for the audit of branches, the training program in place, and the risk assessment methods in place are satisfactory. However, certain weaknesses remain and staff recommended that the BEAC (i) establish a charter for the Internal Audit Department (IAD); (ii) expand the audit scope and coverage of IAD to include activities at headquarters; (iii) prepare an annual rolling multiyear audit program describing risk assessment, activities scheduled, staffing, and financial resources required; and (iv) increase the number of qualified staff.

In its response to the Stage Two report, the management of the BEAC has specifically agreed to expand the scope and coverage of the audit department, and to increase the number of qualified staff. A charter for the audit department will also be prepared, with the assistance of Fund staff, which will provide the BEAC with the relevant documentation. A gradual implementation of these recommendations should be completed by end-2002. The management of the BEAC did not specifically cover in its answer to the report the recommendation related to the risk-based rolling multiyear audit program.

The System of Internal Controls: On the whole, the risks are relatively well captured, although uncertainties exist because of insufficient a posteriori controls exercised on some activities at headquarters. The bank has a codified system of rules, selects its personnel carefully, maintains segregation of duties in the branches, and has recently increased resources for control purposes. Nevertheless, the staff recommended that the BEAC (i) strengthen the coordination among the audit bodies; (ii) examine in depth the segregation of duties at headquarters; and (iii) put in place a more systematic follow-up on all recommendations made by the external auditor to allow the Governor and the Board of Directors to better exercise their oversight responsibilities.

In its response to the Stage Two report, the management of the BEAC has agreed to establish an audit committee by 2002. Regarding the proposed segregation of duties, management noted that an internal assessment was under way, but that for budgetary reasons a formal audit could not be undertaken before end-2001.

Regarding late payments of Fund obligations, which had been an issue for all of the BEAC's member countries at some time in the last three years, the staff concluded that, while the BEAC's own payment procedures and related management controls in this area were functioning adequately, procedures should be modified with respect to BEAC's relations

with member countries. The staff recommended that the BEAC should repay the Fund directly, using its own resources for those countries with borrowing capacity with the central bank; for countries facing fiscal difficulties, the staff recommended that they at least maintain sufficient borrowing capacity with the BEAC to repay IMF obligations falling due within the next year. In its answer to the Stage Two Report, the management of the BEAC did not follow the mission's recommendation that the BEAC should repay the Fund directly. The management also commented that apart from direct statutory advances to treasuries, the BEAC could not grant loans to member countries.

IX. Exchange Rate Arrangement

Chad is a member of the Bank of Central African States (BEAC). The exchange system common to all members of the BEAC has been free of restrictions on payments and transfers for current international transactions. Repurchase of the CFA franc banknotes exported outside the BEAC was suspended on August 2, 1993. The BEAC common currency is the CFA franc, which was formerly pegged to the French franc. Effective January 12, 1994, the CFA franc was devalued by 50 percent in foreign currency terms, and the exchange rate was adjusted from F 1 = CFAF 50 to F 1 = CFAF 100. Starting on January 1, 1999, the CFA franc has been pegged to the euro at a the fixed rate of EUR 1 = CFAF 655.96. On December 10, 2001, the rate of the CFA franc, in terms of the SDR, was CFAF 936.01= SDR 1.

X. Article IV Consultations

Chad is on the standard 12-month consultation cycle.

The last discussions for the 2000 Article IV consultation were held in N'Djaména during the period May 5-21, 2000. The staff report (EBS/00/133; 7/10/00) was discussed by the Executive Board on July 25, 2000. The following documents were also distributed and discussed the same day by the Board: (i) a preliminary document on the enhanced Initiative for Heavily Indebted Poor Countries (EBS/00/125; 6/29/00) and (ii) an assessment of the interim poverty reduction strategy paper and interim poverty reduction strategy (EBD/00/55; 7/10/00).

XI. FSAP Participation, ROSCs, and OFC Assessments:

Not applicable for Chad

XII. Technical Assistance

1988: FAD mission to prepare a tax reform program.

1989: FAD mission to prepare a tax reform program.

1990: FAD mission to review implementation of the tax reform program.

1991: FAD mission to review implementation of the tax reform program.

1994: FAD mission to assess weaknesses in customs administration and recruit an expert responsible for strengthening customs administration.

October 1994-October 1995: FAD resident expert to strengthen customs administration.

1996: FAD mission to review the tax reform program (introduction of the turnover tax and strengthening of tax administration).

August 1997: FAD mission to follow up on the tax reform program initiated in 1996.

November-December 1997: FAD mission to assess weaknesses in customs administration and prepare a rehabilitation program for strengthening the customs directorate.

May-June 1998: FAD mission to assess the need for long-term assistance in tax and customs administration, treasury operations, and budget preparation and execution.

November 1998: FAD expert to begin a series of mission to strengthen customs administration.

March 1999: FAD expert started long-term assignment to assist the tax administration with, in particular, the introduction of a value-added tax.

October 1999: FAD mission to assess tax administration.

November 1999: FAD expert to start long-term assignment as public expenditure management advisor to the Minister of Finance.

May 2000: STA multisector statistics mission.

June 2001: FAD expert to start long term assignment to assist the tax administration with, in particular, the strengthening of tax collection and the implementation of the value-added tax.

X. Resident Representative

The post of Fund Resident Representative was opened in N'Djaména in 1998. Ms. Laurence M. Allain, the new IMF representative, took up her post on October 15, 2001.

Chad: Relations with the World Bank Group

1. The Bank's assistance program in Chad is laid out in its 1999-2001 Country Assistance Strategy and Addendum which was discussed by the Board in May 2000. This strategy focuses on three key objectives: (i) building capacity for improved governance, (ii) establishing the foundations for improved delivery of basic social services, and (iii) removing constraints to growth. This assistance program is consistent with the orientations of Chad's interim poverty reduction strategy paper discussed by the Boards of the IMF and of the World Bank on July 25, 2000.
2. The Bank's current portfolio of projects supports (i) capacity building for public financial management, management of the petroleum sector, and environmental management; (ii) investments in key sectors for poverty reduction (health, education, rural development, and transport); and (iii) support for the exploitation of Chad's petroleum resources. The current policy dialogue between Chad and the Bank focuses on improving transparency and accountability in Chad's public financial management system.
3. Support has been approved for key activities proposed by the Country Assistance Strategy over the last 12 months. A Management of the Petroleum Economy Project in the amount of US\$17.5 million aimed at building capacity for public financial management was approved in January 2000. A Health Sector Support Project in the amount of US\$41.5 million was approved in April 2000. On June 6, 2000, the Executive Board of the World Bank approved a Petroleum Development and Pipeline Project, for which it provided an IBRD loan in the amount of US\$39.5 million equivalent to the Republic of Chad, as well as US\$14.2 million in A-Loans and up to US\$42.7 million in B-Loans from the International Finance Corporation to the oil transportation company in Chad. A complementary IDA-funded Petroleum Sector Management Capacity-Building Project, aimed at promoting environmentally and socially sound management of the petroleum sector, was approved simultaneously for US\$23.7 million. A credit of US\$67 million in support of the National Transport Program was approved by IDA on October 26, 2000. Lastly, a second Population and Aids Project in the amount of \$24.6 million was approved by IDA on July 12, 2001.
4. Three quick-disbursing policy reform operations for a total of US\$85 million were successfully carried out from 1996 to 1999 in support of the government's structural adjustment program.

A. Statement of IDA Credits
(As of October 31, 2001)

(In millions of U.S. dollars)

Credit No.	Fiscal Year	Purpose	IDA	Undisbursed
Cr. 21840	1991	Engineering Project	11.0	2.0
Cr.26850	1995	Agricultural Services	24.5	2.2
Cr.26920	1995	Population and AIDS	20.4	1.3
Cr.30820	1999	Household Energy	5.3	2.9
Cr.32000	2000	Management of the Petroleum Econ.	17.5	14.6
Cr.30420	2000	Health Sector Support Project	41.5	37.4
L. 45580	2000	Oil Development and Pipeline Project	39.5	33.9
Cr. 33730	2000	Petroleum Sector Capacity Building Project	23.7	19.6
Cr. 34260	2001	National Transport Program Project	67.0	60.9
Cr. 35480	2001	Population and Aids	24.6	24.6
Total number of credits and loans = 10				
Total disbursed (IBRD and IDA)			603.8	
<i>Of which:</i> repaid			36.4	

B. Statement of IFC Investments

5. On June 6, 2000, the Executive Board of the World Bank approved US\$ 14.2 million in A-Loans and up to US\$ 42.7 million in B-Loans from the IFC to the oil transportation company in Chad in the context of the Petroleum Development and Pipeline Project. These loans became effective on July 27, 2001. IFC financing of small and medium-scale projects in the agricultural and financial sectors and IFC support for the participation of local enterprises in petroleum-related activities are currently under consideration.

C. Activities Under Preparation

6. A Fourth Structural Adjustment Credit (US\$40.0 million) will be presented to, and discussed by, the World Bank Board in December 2001. An Education Reform credit (US\$30.0 million) is also planned for June 2002. In addition, further investment in the energy, social, urban and agriculture sectors totaling approximately US\$140.0 is planned for the next fiscal year. Sector strategy work in education and rural development is ongoing.

7. In addition to these lending activities, the planned program of nonlending activities includes comprehensive public expenditure work and expenditure-tracking surveys in priority sectors. Institutional Development Grants have been approved to support capacity building for civil society groups and parliament. These grants are aimed, in particular, at strengthening the civil society's ability to play its role in the management future petroleum revenues.

Chad: Structural Reforms Supported by World Bank Programs

1. As discussed in the staff report, structural areas that lay outside of the Fund's core area of expertise are no longer covered by Fund conditionality. These areas—civil service, procurement and cotton sector reforms, and privatization— are fully covered under the World Bank's US\$17.5 million Management of the Petroleum Economy Project, which became effective in September 2000, and under the Fourth Structural Adjustment Credit (SAC IV), which was presented to the Executive Board for the World Bank on December 18, 2001. This annex includes detailed intermediate steps in all four areas for the period 2001-03, as described below.

Civil service reform

- Adoption by parliament of new civil service statutes introducing competitive recruitment and merit-based advancement December 2001 (done)
- Computerization of harmonized civil service and payroll records June 2002
- Adoption of application decrees of new civil service statutes July 2002
- Audit of seven pilot ministries June 2002
- Determination of post profiles and personal evaluation forms December 2002
- Test of the individual performance system in seven pilot ministries End- 2002
- Extension of individual performance system to whole civil service Second half 2003

Procurement Reform

- Issuance of decree on the simplification of approval circuit July 2001 (done)
- First issue of quarterly *Public Procurement Bulletin* October 2001 (done)
- Recruitment of consultant for assistance in drafting new *Procurement Code* November 2001 (done)

- Drafting of new Public Procurement Code and application Decrees March 2002
- Forum on draft Public Procurement code April 2002
- Adoption of new procurement code October 2002
- Adoption of application decrees December 2002

Cotton sector reform

- Recruitment of Controller General responsible for the implementation of Cotontchad's restructuring plan April 2001 (done)
- Legal separation of DHS (Oil and Soap Division) from Cotontchad November 2001 (done)
- Launching of tender for bids for privatizing the DHS December 2001
- Privatization of the DHS June 2002
- Launching of tender for bids for study on alternative scenarios for the privatization of Cotontchad September 2001 (done)
- Start of study on alternative scenarios for the privatization of Cotontchad February 2002
- Organization of investors' forum August 2002
- Organization of farmers' forum August 2002
- Finalization of study on alternative scenarios for privatization Cotontchad September 2002

- Adoption of privatization scenario by government October 2002
- Launching of tender for bids for the privatization of Cotontchad November 2002
- Privatization of Cotontchad June 2003

Privatization

- Privatization of the DHS, the oil and soap unit of Cotonchad June 2002
- Awarding the third mobile phone license September 2002
- Reduction in the government's share in Sotexho, owner of Novotel hotel End-2002
- Sale of air traffic rights End-2002
- Cotontchad (as per the previous point) June 2003

2. In addition, as discussed in the text, two areas—public expenditure management and governance—are jointly followed by the Fund and the World Bank. **In the area of governance**, beyond the financial support provided by the World Bank to carry out the audits of customs administration and large public procurement contracts, the World Bank's involvement focuses on public procurement and civil service reform, as described above. **In the area of public expenditure management**, the World Bank has conducted the first annual public expenditure reviews (in health and education) in 2001, to be extended to basic infrastructure and rural development in 2002, and will support the elaboration of medium-term expenditure programs (in health and education in 2002, to be extended to basic infrastructure and rural development in 2003), and continue to work on the simplification and computerization of the expenditure circuit.

Chad: Progress Toward Achieving the HIPC Initiative Completion Point Conditions

This matrix indicates progress that has been made thus far toward reaching the floating completion point conditions for the HIPC Initiative completion point, highlighting, where available, the expected date of the completion of a given condition.

Action	Status
Poverty reduction strategy paper	
<ul style="list-style-type: none"> Ensure that a fully participatory PRSP has been prepared and satisfactorily implemented for at least one year, as evidenced by the joint staff assessment of the country's annual progress report. 	<i>PRSP is expected to be completed by end-March 2002.</i>
Macroeconomic stability	
<ul style="list-style-type: none"> Continue maintenance of macroeconomic stability and satisfactory implementation of the PRGF-supported program. 	<i>Ongoing.</i>
Governance	
<ul style="list-style-type: none"> Make satisfactory progress in strengthening public expenditure management to facilitate the identification and tracking of poverty-related spending, as evidenced by the implementation for at least six months of the simplified and computerized expenditure circuit, and a functional expenditure-tracing system for primary education services. 	<i>Expected to be completed by mid-2002.</i>
<ul style="list-style-type: none"> Adopt a new law on public procurement and its application decrees; publish a quarterly bulletin on public procurement; complete audits by internationally reputed firms for the five largest public procurement contracts granted in 2001; adopt the Budget Settlement Law for year 2000 before the adoption of the Budget Law for year 2002, and, similarly, adopt the Budget Settlement Law for year 2001 before the adoption of the Budget Law for year 2003; and nominate the judges for the commercial courts in the five largest cities. 	<i>Drafting of new procurement legislation launched.</i> <i>First issue of quarterly bulletin published.</i> <i>Budget Settlement Law for 2000 submitted to Parliament and expected to be adopted before the 2002 Budget Law.</i>
<ul style="list-style-type: none"> Adopt a governance strategy and action plan in consultation with IDA and the IMF and implement it for at least one year. 	<i>Governance strategy and action plan expected to be adopted by March 2002.</i>
Priority sectors¹	
Health	
<ul style="list-style-type: none"> Ensure that at least 75 percent of all health districts and health centers across the country are operational, up from 68 percent in 1999. 	<i>79 percent of all health districts and 64 percent of all health centers operational in 2000.</i>
<ul style="list-style-type: none"> Achieve a DPT3 vaccination rate of at least 40 percent up from 35 percent in 1999, and an assisted delivery rate of at least 20 percent, up from 15 percent in 1998. 	<i>DPT3 vaccination rate 44 percent in 2000.</i>

Action	Status
HIV/AIDS and sexually transmitté diseases	
<ul style="list-style-type: none"> • Increase the sale of condoms through the social marketing project MASOCOT by at least 25 percent over the 2.239 million condoms sold in 2000. • Increase the treated cases of genital ulcers to at least 30,000 per year, up from 12,000 in 1998, and the treated cases of purulent urethritis to at least 40,000 per year, up from 21,000 in 1998. Decrease the prevalence of syphilis among pregnant women from 6 percent in 1998 to at most 4 percent. 	<i>Data not yet available.</i>
Education	
<ul style="list-style-type: none"> • Increase the gross enrollment rate to at least 61 percent for girls and 89 percent for boys, up from 50 percent and 85 percent, respectively, in 1998–99. • Reduce the repeater rate from 26 percent in 1998-99 to at most 22 percent. 	<i>Progress made: 1999–2000 gross enrollment rate is 55 percent for girls and 88 percent for boys. No progress made in repeater rate.</i>
Basic infrastructure	
<ul style="list-style-type: none"> • Ensure that at least 50 percent of the all-year road network can be used throughout the year (80 percent of the network can not be used for three to five months during the rainy season). 	<i>Progress made as of December 2001: 43.5 percent of the network can be used throughout the year.</i>
Rural development	
<ul style="list-style-type: none"> • Increase access to potable water to at least 32 percent, up from 27 percent in 2000. • Increase the share of agricultural families equipped with plows from 24 percent in 2000 to at least 26. • For livestock holders increase the number of water points by at least 10 percent, relative to 1138 water points in 2000. 	<p><i>Expected to be completed by end-2002.</i></p> <p><i>Expected to be completed by end-2002.</i></p> <p><i>Expected to be completed by end-2002.</i></p>

¹ For each indicator, agreement was reached on how to measure progress.

Chad: Statistical Issues

1. Chad's statistical system is weak and suffers from a shortage of financial and human resources. The compilation of national statistics is decentralized at various ministries, and at the national agency of the Bank of Central African States (BEAC). The statistics directorate at the Ministry of Planning (Direction des Statistiques et des Etudes Economiques et Démographiques, or DSEED) is in charge of the national accounts and the consumer price index (CPI), as well as the production and publishing of statistics on population. The Ministry of Finance is responsible for compiling fiscal data. The BEAC is responsible for monetary statistics and the balance of payments. The CPI is published biweekly, and other data are disseminated as they become available.
2. The authorities have expressed a strong interest in reforming the statistical system but lack the resources—both human and financial—to do so. An important step in this direction was the recent implementation of a new set of national accounts in line with the *System of National Accounts (SNA) 1993*. The adoption in 1999 by the government of a law to regulate and enhance statistical activity provides a new impetus to the collection and dissemination of statistical data.
3. Chad has adopted the General Data Dissemination System (GDDS) as its statistical development framework, and will participate in the forthcoming Economic and Monetary Community of Central Africa (CEMAC) workshop in Yaoundé (Cameroon) in January 2002. Following this workshop, Chad is expected to disseminate detailed standard documentation on its compilation practices in five areas (real, external, monetary statistics, fiscal, and sociodemographic data).
4. Overall, the quality of real sector data has improved since the national accounts were revised back to 1995. *However, weaknesses in balance of payments, government finance, and monetary statistics make program design and monitoring difficult.*

Real sector

5. In early 1998, the authorities started compiling a new set of national accounts, conforming with the methodological requirements of the *SNA 1993*, and retained 1995 as a base year. Particularly, main improvements include the compilation of an input-output table that incorporates nonmarket household production and provides a better coverage of the informal activities sector. However, there is a need to refine the data-updating process, notably to take into account structural changes in the economy. The only price index available is the CPI, which is based on outdated 1972 weights. It is essential that efforts aimed at producing a harmonized consumer price index for the CEMAC countries be continued with the assistance of the regional statistical office (AFRISTAT), and that financing be secured for the necessary household consumption survey.

Public finance

6. Chad has not yet been able to resume reporting of detailed data to for publication in the *Government Finance Statistics Yearbook (GFSY)*. Annual data to 1999 were reported and published in the *International Financial Statistics (IFS)*. The published data include a large discrepancy between the measures of financing and the deficit. The 2000 multisector mission noted that there was no comprehensive and systematic compilation of government finance statistics. The quarterly *Tableau des Opérations Financières de l'Etat (TOFE)*, compiled by a working group, mainly for the purpose of the Fund-supported program, is based on several disparate sources. The mission recommended that systematic procedures be established for the compilation of government finance statistics, based, to the extent possible, on a unified set of accounting and administrative records that would be implemented only after a comprehensive review of the public accounting system.

Monetary sector

7. Monthly data on monetary statistics for Chad, as well as for the other members of the CEMAC, are reported on a regular basis, although with some delays. The data are reported in electronic form by the regional central bank (BEAC) and published in *IFS*. The institutional coverage of monetary statistics is comprehensive, but accuracy is affected by large cross-border movements of currency among CEMAC member countries. About 40 percent of notes issued by Chad circulate in Cameroon. At the same time, currency circulation in Chad includes about 20 percent of notes from Cameroon and 10 percent of notes from the Central African Republic.

8. The monetary and financial statistics mission that visited the BEAC headquarters (May 2001) provided technical assistance in addressing the main shortcomings pertaining to the coverage, methodology, and timeliness of monetary statistics. The mission discussed an action plan for the implementation of the *Monetary and Financial Statistics Manual* and for the introduction of an area-wide page in *IFS* for the CEMAC. New proposals were discussed with the authorities for the provision of future technical assistance in monetary statistics to the region.

Balance of payments

9. As in other CEMAC countries, the agency responsible for the compilation of the balance of payments statistics is the Balance of Payments Unit (Service de la Balance des Paiements) of the national agency of the BEAC. The poor quality of the balance of payments statistics appears to be related to a lack of adequate staffing and adequate financial and physical resources dedicated to balance of payments compilation. The foreign trade data, compiled by the DSEED on the basis of customs declarations, are known to be unreliable, and to suffer from coverage problems; in addition, they are believed to be inconsistent with those used in the compilation of national accounts. Consequently, they are not fully used to compile the balance of payments data. Data on exports are estimated based on data provided by line ministers. Even considering the difficulty of collecting data on informal border trade

between Chad and its neighboring countries, many improvements could be made on such items as imports, cotton and cattle exports, freight, and public transfers. It is believed that a tighter coordination among the CEMAC, DSEED, and other agencies is desirable in order to improve the data coverage. In May 2000, a multisector technical assistance mission, the first STA mission in ten years, visited Chad to provide a thorough assessment of its needs in balance of payments statistics. It found that the compilation system and procedures for balance of payments statistics, recently revised to conform to the *Balance of Payments Manual* (fifth edition) (*BPM5*), to be conceptually sound but flawed in their use, owing to the absence of documented sources and methods, understaffing, and lack of training. In all of these areas, the mission made specific recommendations. This situation implies that the authorities' commitment to strengthen the human and technical resources needs to be confirmed.

10. The authorities have reported to STA balance of payments statistics for 1995, 1996 and 1997 in a comprehensive, detailed framework. The authorities have also committed themselves to describing the balance of payments compilation system during the forthcoming GDDS workshop.

Poverty indicators

11. With a delay for reasons outside the authorities' control, the government will launch a household survey on income and expenditure in January 2002, with assistance from the World Bank. The results of the survey will provide definitions of a poverty line and the main poverty indicators (incidence, depth, and severity).

Chad: Survey of Reporting of Main Statistical Indicators
(As of December 14, 2001)

	Exchange Rates 1/	International Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Current Government Balance	GDP/GNP	External Debt
Date of latest Observation	Nov. 01	Sep. 01	Sep. 01	Sep. 01	Sep. 01	Oct. 01	Oct. 01	Dec. 00	Dec. 00	Sep. 01	Dec. 00	Oct. 01
Date received	Nov. 01	Oct. 01	Sep. 01	Oct. 01	Oct. 01	Dec. 01	Nov. 01	Feb. 01	Feb. 01	Oct. 01	Feb. 01	Nov. 01
Frequency of data	Monthly	Monthly	Monthly	Monthly	Monthly	Irregular	Monthly	Annual	Annual	Monthly	Annual	Monthly
Frequency of reporting	Monthly	Quarterly	Quarterly	Quarterly	Quarterly	Quarterly	Monthly	Annual	Annual	Monthly	Annual	Monthly
Source of data	Central bank	Central bank	Central bank	Central bank	Central bank	Central bank	Ministry of Planning	Central bank	Central bank	Ministry of Finance	Ministry of Planning	Ministry of Finance
Mode of reporting	Cable	Mail	Mail	Mail	Mail	Mission in the field	Fax or mission in the field	Mission in the field	Mission in the field	Fax or mission in the field	Fax or mission in the field	Fax or mission in the field
Confidentiality	NO	YES	YES	YES	YES	NO	NO	YES	YES	YES	YES	YES

1/ From January 1, 1999 onward, the CFA franc has been pegged to the euro.

**Statement by Alexandre Barro Chambrier, Executive Director for Chad
January 16, 2002**

I. Introduction

Chad's economic performance improved in 2001, with measurable incidence on poverty. Despite a number of setbacks, including the decline in the world market cotton prices, adverse weather conditions and shortfalls in external financing, the positive developments enjoyed by the country were made possible by the sustained implementation of economic reforms and the acceleration of the Doba oil project. The authorities made substantial progress toward the HIPC Initiative completion point, including the preparation of a status report. They also met all quantitative and structural performance criteria, benchmarks and other indicators, except those for government revenue and the non-accumulation of external arrears for which they are requesting waivers. The shortfall in government revenue was partly due to the turnover of staff at all levels of administration and lower tax revenue from the state cotton company. Corrective actions have since been taken. As regards the external arrears, they were due to shortfall in external financing, but the arrears were all cleared before end-December. The authorities have also made good progress on governance issues. Overall, the program is being well implemented and is gradually gaining momentum.

Looking ahead, the medium-term outlook has improved markedly, following the acceleration of the Doba oil project. At this critical juncture, my Chadian authorities are committed to pursuing their adjustment efforts and taking other measures deemed necessary to maintain macroeconomic stability. However, they are cognizant that, they need to strengthen domestic institutions, in order to implement their ambitious poverty-reducing program with more chance to succeed and prepare for the petroleum era. Moreover, the authorities are convinced that preserving political and social stability is critical for the successful implementation of reforms and, in this context, a peace agreement has recently been signed with one of the main rebel movements.

II. Program Implementation and Recent Economic Developments in 2001

Notwithstanding a difficult environment, the economic and financial performance improved considerably in 2001, as program implementation proceeded satisfactorily, fiscal policy returned to a more prudent path, structural reforms advanced broadly as programmed and past slippages in transparency and governance have been corrected.

Macroeconomic developments in 2001 were marked by a surge in economic activity and higher inflationary pressures. Based on preliminary data, real GDP growth is estimated at 8.9 percent in 2001, from 0.6 percent in 2000, reflecting the acceleration of the construction of the Chad-Cameroon pipeline. Inflation is estimated at about 14 percent in 2001, reflecting the food shortage that resulted from last year's drought and strong oil sector demand. The current account deficit is projected to widen from 16 percent to 42 percent in 2001, owing mainly to higher imports related to the exploitation of Chad's two oil fields.

On the fiscal front, the primary current fiscal deficit (excluding spending on elections and food emergency) was lower than programmed, mainly due to lower-than-programmed expenditure. While on track through the first half of 2001, revenue collection weakened in the third quarter, due to weak administrative capacity at customs, a shortfall in taxes from the state cotton company and some abuses in the tax-exempt status of the Doha project that the authorities are determined to address. On the expenditure side, shortfall in external financing and security concerns in the North led to increased defense spending, lower-than-programmed expenditure in social sectors and the accumulation of domestic and external arrears.

On the structural front, as indicated in box 1 of the staff report, the authorities took a number of measures to strengthen the fiscal position, and to improve governance. In the revenue area, the value-added tax (VAT) administration was strengthened, the customs data base was installed in the N'djamena offices and tax administration numbers (TIN) were assigned to all identified economic agents. The authorities also made good progress in the area of expenditure management, with the release of the new procedural handbook on streamlined expenditure circuit, the publication of the first quarterly bulletin on public procurement, the completion of public expenditure reviews for health and education and, the closing of a number of inactive government accounts. Substantial progress was also made in the areas covered by World Bank conditionality, namely civil service reforms, procurement system, cotton sector and privatization. The structural performance criterion on the audit of the use of the oil bonus was satisfied. However, given the time needed to build consensus within the government, the structural benchmark on the principles governing the pricing and taxation mechanisms of the oil and gas of the Sedigi field could not be adopted as scheduled, and the performance criteria on total fiscal revenue and the non-accumulation of external arrears were not met, mainly due to weak administrative capacity and a shortfall in external financing.

The financial sector remains sound, with all but one bank complying with the main prudential ratios at end-June 2001. This bank has received a capital injection from its private owners, thus improving its solvency. Furthermore, the microfinance sector continues to experience a promising development.

In the area of governance, important progress has been made. The authorities prepared an action plan of governance and completed the audit of the use of the oil bonus as agreed. They also stepped-up the preparation of the international audit of the customs, as well as that of the five largest public procurement contracts. Finally, they requested the assistance of the World Bank to reconsider their planned contract concerning the exploitation of the Sedigi gas resources.

III. Policies for 2002 and medium-term

Although Chad is facing a challenging international environment, with uncertainty, particularly in the cotton sector, economic prospects for 2002 and beyond remain optimistic, mainly due to the upcoming exploitation of oil and gas resources. Real GDP is expected to

grow at around 10 percent per annum in 2001-2003 and to accelerate to 50 percent in 2004 when oil production starts. Inflation is expected to be reduced to an annual average of 4 percent, in line with inflation rate in the CEMAC zone. At the same time, the external account is expected to swing from a deficit of 50 percent of GDP into a surplus of 15 percent of GDP and debt sustainability will improve dramatically, with the external debt to exports ratio falling from 230 percent in 2003 to about 90 percent in 2004. At this critical juncture, the main objective of the authorities is to avoid the pitfalls of developing a dual economy by developing a vibrant domestic private sector.

Fiscal Policy

Despite the adverse impact of the cotton crisis on public finances, the authorities' priority in 2002 is to increase public spending in poverty-reducing areas, while containing the fiscal deficit (excluding elections and famine-related spending) at 1.3 percent of GDP in 2002 from 0.3 percent in 2001. Achieving this target will require continuous revenue effort and expenditure restraint. Fiscal revenue is expected to increase to 7.9 percent of GDP in 2002 from 7.8 percent in 2001, as a result of efforts to strengthen tax administration.

The authorities are committed to providing high level political support to enhance tax collection, especially in the customs area. In line with this commitment, the authorities will take a number of measures, including, completing an independent audit of customs and the setting-up procedures for verifying ex-post tax exemptions for imports under the Doba project. They will also take an additional set of measures to further enhance tax collection, including, inter alia, measures based on the findings of the customs audit, a reform of the system of taxing small taxpayers, and actions to reinforce cattle taxation, so as to bring part of the informal sector under the tax net.

On the expenditure side, the authorities intend to make decisive progress toward achieving the HIPC Initiative completion point conditions for the priority sectors, while mitigating the adverse impact of the cotton crisis. Consequently, current primary expenditure is expected to increase to 9.4 percent of GDP in 2002 from 9.1 percent in 2001. In this regard, the authorities have adopted a contingency spending plan, in order to reduce any risk of slippages in government expenditure. In the baseline scenario, the wage bill will increase slightly, reflecting additional spending in the priority social sectors and the impact of statutory promotion in the civil service and the ongoing regularization of military personnel. Transfers will also increase significantly, reflecting an exceptional financial support to the cotton sector and efforts to rehabilitate the water and electricity company (STEE). As regards the priority sectors, the authorities will step-up their efforts in health, education, governance, infrastructure and rural development and intend to concentrate public sector investment in these areas. The authorities will also take major steps to strengthen public expenditure management, including, inter alia, a close monitoring of budget implementation, in order to avert the recurrence of payment arrears; the launching of a medium-term public expenditure programming with the assistance of the World Bank and the discontinuance of cash payment to suppliers. In the context of the HIPC, the authorities will produce the first biannual report on poverty-reducing spending, so as to test the effectiveness of the HIPC tracking system for expenditure.

Monetary Policy and Financial Sector Reforms

Monetary policy which is conducted at the regional level by the BEAC, will be geared toward maintaining price stability over the medium-term and building-up the monetary zone's official reserves, so as to support the peg regime between the CFAF and the Euro. In the financial sector, the authorities will continue to strengthen banking supervision, while strengthening banks' management and accelerating their computerization. They also intend to encourage banks to diversify their deposit base, as well as their lending activities, in particular in the context of the Doba oil project. In the microfinance sector, the authorities, together with COBAC will design a new legal framework, in line with the guidelines of the Central African Economic and Monetary Community (CEMAC). As regards regional programs, the authorities support efforts aimed at adopting a unified banking licensing system within the CEMAC, and adopting a regional payments system, which enables settlements in real time and the development of electronic payment instruments.

Structural Reforms

In the structural area, the main objective of the authorities is to improve public sector management, while fostering governance. To this end, the authorities will continue to implement an ambitious reform agenda in the fiscal area, governance, and privatization. In the fiscal area, the authorities will press ahead with measures designed to strengthen revenue collection, as indicated in the section on fiscal policy. They will also accelerate the privatization of DHS, the oil and soap unit of Cotontchad; Sotexho, a hotel management company, and award a third mobile phone license. In the cotton sector, the authorities will launch a study to identify possible scenarios for the privatization of Cotontchad and adopt the final scenario for privatization by end-2002. As regards civil service reform, after the adoption of the new civil service statutes by parliament, the authorities intend to implement the merit-based advancement and competitive recruitment, finalize the harmonization and computerization of payroll and civil service files and conduct the organizational and human resources audit for seven pilot ministries.

The authorities are also committed to strengthening transparency and good governance. To this end, they will follow the recommendations of the audit of the use of the oil bonus as of end December 2000 and adopt an action plan as a follow-up of the audit of the five biggest public contracts awarded in 2001. On the basis of this action plan, they will adopt a methodology to conduct regular audits of public contracts, as well as the public procurement system. As regards the international audit of custom's administration and its follow-up, the authorities, at the highest level, have indicated their commitment to providing their support in this area. Finally, the authorities intend to adopt the national governance strategy, the new procurement code and set up an independent procurement appeals system with the assistance of the World Bank.

Poverty Alleviation and Preparation of the PRSP

Poverty reduction remains the government's key priority. The authorities are implementing the poverty reduction strategy in line with the I-PRSP priorities. The authorities have continued to make steady progress toward achieving the HIPC Initiative completion point triggers for education, health, rural development and basic infrastructure, and the fight against AIDS/HIV and other sexually transmitted infections. Important steps have also been taken to strengthen governance. Despite a number of difficulties associated with the absence of quantitative data in certain areas and the weak administrative capacity for organizing participatory consultations on a national scale, my Chadian authorities are steadily moving toward the completion of a fully participatory full PRSP by end March 2002. To this end, they intend to carry out the work needed to finalize the full PRSP, by among others, organizing regional validation workshops, incorporating the feedback and clarifying performance indicators. They will also strengthen human resources at the Permanent Secretariat of the PRSP Steering Committee and enhance the coordination between the PRSP Steering Committee and line ministries, so as to speed-up the completion of the full PRSP.

IV. Conclusion

My Chadian authorities have demonstrated their continued commitment to the adjustment program, despite facing a difficult environment. As a result, economic performance improved markedly in 2001, marking a clear break with the policy slippages in 2000. However, the situation remains fragile, as evidenced by the recent collapse of cotton prices, which contributed to a further weakening of the fiscal stance. At this critical juncture, my Chadian authorities reiterate their commitment to economic reforms and social stability and are hopeful that their efforts will be rewarded by additional and timely support from the international community. In view of Chad's good track record and the authorities' firm commitment to reforms, I would like to request the Board's support for waivers for the nonobservance of the performance criteria, an augmentation of quota to help cover the additional balance of payments financing need resulting from the decline in the world cotton price, and the completion of this review.



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 02/15
FOR IMMEDIATE RELEASE
February 25, 2002

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes 2001 Article IV Consultation with Chad

On January 16, 2002, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Chad.¹

Background

A three-year arrangement under the PRGF was approved for Chad on January 7, 2000 in an amount equivalent to SDR 36.4 million (65 percent of quota). At the time of the second review, on May 16, 2001, this amount was augmented by SDR 5.6 million (10 percent of quota) to address emergency food import needs. At the same time, Chad reached its decision point under the Enhanced HIPC Initiative, which entailed a debt relief of about US\$170 million in net present value (NPV) terms. In June 2001, the Paris Club provided a flow debt rescheduling of Chad's external debt on Cologne terms.

Overall, the Chadian economy had a reasonably good year in 2001. Fiscal policies followed a broadly prudent path, progress in structural reforms was close to programmed, and past slippages in transparency and governance were corrected. These achievements were made against the backdrop of a worsening environment, including weak agricultural production following extreme weather conditions, a shortfall in external financing, and a recent sharp decline in the world market price of cotton, Chad's main export commodity. Notwithstanding the overall progress, advances in certain areas have been slower than programmed. Revenue collection, in particular, weakened in the second half of the year.

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. 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.

Real GDP growth picked up significantly in 2001, reaching an estimated 8.9 percent, after only 0.6 percent in 2000, mainly because of the acceleration of the construction of the Chad-Cameroon pipeline. Consumer prices increased by 14 percent on average in the year ended October 2001, reflecting mainly the impact of food shortages, but prices started declining in the last quarter of the year as food supplies improved. Overall, Chad managed to maintain much of its gains in external competitiveness following the devaluation of the CFA franc in 1994. The external current account deficit (excluding official transfers) widened from 16 percent of GDP in 2000 to an estimated 42 percent in 2001, owing to higher imports related to the investment in the energy sector. A large part of the current account deficit was financed by foreign direct investment. Net official foreign exchange reserves increased in the third quarter to reach CFAF 18 billion, partially reversing a decline in the first half of the year. The financial sector's health remained good, with all but one bank complying with the main prudential ratios at end-June 2001.

The primary current fiscal deficit (excluding spending on elections and on food emergency) reached about 0.6 percent of GDP at end-September 2001, somewhat less than programmed, despite a shortfall in revenues. The structure of expenditure was somewhat unfavorable, with defense spending slightly higher than envisaged as a result of increased rebel activity in the North, and expenditure on social sectors lower than programmed. Against the backdrop of the shortfall in external financing, the government accumulated some payments arrears.

Structural reforms proceeded broadly as programmed. A series of fiscal structural measures were completed, aiming at enhancing revenue collection (such measures related to the value-added tax administration, the computerization of the customs database, and the assignment of tax identification numbers to all economic agents) and strengthening public expenditure management (this included the streamlining of the expenditure circuit, the preparation of public expenditure reviews for the health and education sectors, and the closure of a number of inactive government bank accounts). Privatization, as well as the reform of the civil service, the procurement system, and the cotton sector also advanced as scheduled. Governance improved considerably: in addition to the completion of the audit of the use of the oil bonus, the preparation of the international audit of the customs as well as that of the five largest public procurement contracts proceeded as scheduled.

Executive Board Assessment

Executive Directors noted that overall economic performance has improved considerably in 2001 against the backdrop of a worsening external environment, and economic growth has picked up significantly, boosted by the acceleration of the Doba oil field and pipeline project and ongoing structural reforms. Directors welcomed the prospect that growth will continue to be strong in 2002 and beyond, while stressing that this prospect highlights even more the critical importance of ensuring that policies will be tailored toward integrating the rapidly developing oil sector into the rest of the economy, and that broad-based structural reforms continue. They were encouraged that strong growth, combined with continued poverty reducing measures, would start to make a dent in poverty in the not too distant future. Directors observed, however,

that the growth prospects were somewhat dampened in the short term by a decline in the world market price of cotton, Chad's main export commodity.

Directors welcomed the authorities' commitment to prudent fiscal policies, while tailoring the 2002 budget toward poverty reduction. They highlighted, however, that the recent weakening in revenue performance could compromise the attainment of the poverty reducing objectives. While adverse price developments in the world cotton market and the tax-exempt status of the oil part of the economy have contributed to this disappointing performance, Directors agreed that administrative weaknesses have also played an important role. Accordingly, they urged the authorities to implement without delay the revenue measures included in the 2002 budget, in particular, the measures aimed at improving customs collection and at stemming tax evasion. A number of Directors also cautioned against the proliferation of tax exemptions and incentives. Directors agreed that, in addition to building on the recent improvements in expenditure management, the focus should now be on the initiation of a medium-term expenditure framework. They hoped that Chad would receive a more certain and better coordinated flow of bilateral financial assistance. Directors welcomed the authorities' decision to set up a contingency mechanism for the eventuality of a shortfall in budget resources. The authorities were also encouraged to make further progress toward creating an environment in which arrears are no longer permitted.

Directors commended the authorities on their improved transparency and governance record and saw the completion of the audit on the use of the oil bonus according to international standards as a major step in this regard. They urged the authorities to complete steadfastly the audits of the customs administration and of the five largest procurement contracts, and to follow up on the findings of the recent audit of the use of the oil bonus.

Directors encouraged the authorities to make the audits available to the public. They looked forward to an early adoption of the government's own national governance strategy.

Directors noted the early progress made toward achieving the completion point triggers under the enhanced HIPC Initiative, as evidenced by improvements in a number of social indicators. Looking ahead, they emphasized the need for continued structural reforms aimed at effectively managing the oil revenue flows, developing the non-oil sectors of the economy, and completing the reform and liberalization of the cotton sector. Some Directors suggested the authorities to consider the establishment of an oil stabilization fund.

Although Chad's trade integration has advanced well, Directors regretted that macroeconomic convergence with other members of the CEMAC monetary zone has not progressed in recent years. They welcomed in this regard the authorities' commitment to policy convergence by 2004 according to a predetermined schedule. Directors noted favorably that Chad's exchange system remains free from restrictions on payments and transfers for current transactions.

Directors were encouraged by the progress made in the preparation of the PRSP, and they particularly commended the authorities for the broad-based participatory process. To facilitate the timely finalization of the PRSP, they recommended that the collaboration between

government institutions and the steering committee overseeing the PRSP process be strengthened in areas where the former's specific technical expertise is required.

Directors expressed concern that, despite progress in recent years, Chad's statistical database continues to suffer from major weaknesses. They urged the authorities to implement the measures identified in the context of Fund technical assistance to improve the quality and timeliness of macroeconomic data. They agreed that Chad could benefit from increased technical assistance to substantially enhance its administrative capacity.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. The Staff Report for the 2001 Article IV Consultation with Chad is also available.

Chad: Selected Economic Indicators

	1997	1998	1999	2000	2001 Rev. Prog.
	(Annual percentage change, unless otherwise specified)				
National income					
GDP at current prices	7.1	12.4	-3.6	4.1	17.2
GDP at constant prices	4.3	6.6	1.0	0.6	8.9
Consumer price index (average)	5.9	4.4	-8.5	3.8	12.4
Money and credit					
Net foreign assets 1/	1.3	-11.6	-5.0	-2.3	4.6
Net domestic assets 1/	-12.4	3.3	5.7	21.1	13.3
Broad money	-11.2	-8.1	-1.3	18.5	17.8
Income velocity of money (M2) 2/	7.7	9.5	9.4	8.2	8.1
External sector (valued in CFA francs)					
Exports, f.o.b.	16.1	7.0	-23.6	11.8	8.0
Imports, f.o.b.	15.5	11.7	-6.6	15.6	136.6
Terms of trade	-4.9	8.7	-6.9	-2.5	12.0
	(In percent of GDP)				
Basic ratios					
Gross investment	16.3	17.5	12.6	17.0	42.5
Central government	6.6	7.8	9.4	10.3	10.7
Private sector	9.7	9.6	3.2	6.7	31.7
Of which: oil sector	1.8	2.0	0.1	2.5	25.5
Gross domestic savings	-1.5	4.1	-2.2	1.6	0.6
Central government finance					
Revenue	7.7	7.7	8.1	8.0	7.8
Total expenditure	17.9	15.6	18.6	20.3	20.8
Current primary balance (- =deficit) 3/	0.8	1.1	-0.1	-0.9	-1.3
Overall fiscal deficit (cash basis) 4/	-5.2	-3.1	-6.3	-12.4	-13.6
Domestic financing	-0.4	0.3	1.0	2.6	-0.4
External financing (already obtained)	5.6	2.8	5.3	9.8	14.0
External sector					
Current account (- deficit)					
Including official transfers	-9.1	-11.0	-14.0	-13.7	-41.2
Excluding official transfers	-13.0	-13.9	-15.3	-16.0	-42.4
Excl. official transfers and oil-related imports	...	...	-15.2	-13.5	-16.9
Overall balance of payments (- deficit)	-1.2	-1.3	-2.1	-0.9	-5.0
	(In millions of U.S. dollars, unless otherwise specified)				
Overall balance of payments deficit/surplus	-18.2	-22.4	-33.3	-13.2	-80.1
Nominal GDP	1,522.8	1,692.9	1,566.2	1,405.8	1,612.2
Nominal GDP (in billions of CFA francs)	888.8	998.7	962.9	1,002.4	1,175.3
CFA francs per U.S. dollar (period average)	583.7	590.0	614.8	713.0	729.0
Population (midyear, in millions)	6.9	7.1	7.3	7.5	7.7
Nominal GDP per capita (In U.S. dollars)	219.7	238.2	214.8	188.0	210.3

Sources: Chadian authorities; and IMF estimates and projections.

1/ Changes as percent of broad money stock at beginning of period.

2/ Ratio of GDP to average broad money.

3/ Excluding grants.

4/ Excluding grants.