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São Tomé and Príncipe: Request for a Three-Year Arrangement Under the Poverty Reduction and Growth Facility—Staff Report; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for São Tomé and Príncipe

In the context of the request for a three-year arrangement under the Poverty Reduction and Growth Facility, the following documents have been released and are included in this package:

- the staff report for the Request for a Three-Year Arrangement Under the Poverty Reduction and Growth Facility, prepared by a staff team of the IMF, following discussions that ended on November 19, 2005, with the officials of São Tomé and Príncipe on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 15, 2005. 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.

- a staff statement of August 1, 2005 updating information on recent developments.

- a Press Release summarizing the views of the Executive Board as expressed during its August 1, 2005 discussion of the staff report that completed the request.

- a statement by the Executive Director for São Tomé and Príncipe.

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

Joint Staff Advisory Note of the Poverty Reduction Strategy Paper
Letter of Intent sent to the IMF by the authorities of São Tomé and Príncipe*
Memorandum of Economic and Financial Policies by the authorities of
São Tomé and Príncipe*
Poverty Reduction Strategy Paper
Poverty Reduction Strategy Paper—Update
Technical Memorandum of Understanding*
*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.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

SÃO TOMÉ AND PRÍNCIPE

Request for a Three-Year Arrangement Under the Poverty Reduction and Growth Facility

Prepared by the African Department
(In consultation with other departments)

Approved by Jean A. P. Clément and Martin Fetherston

July 15, 2005

- Discussions on a new Poverty Reduction and Growth Facility (PRGF) arrangement were held in São Tomé and Príncipe during November 6–19, 2004 and continued in Washington, D.C. in December 2004, and January and May 2005. The staff team met with President de Menezes, the Prime Minister, the government economic team headed by the Minister of Planning and Finance and the Governor of the Central Bank of São Tomé and Príncipe (BCSTP), and with representatives of the donor community. The staff team comprised Messrs. Pastor (Head), Laporte, Segura, Tyaba (all AFR) and Erickson (EP, INS). Mr. Randriamaholy, the Fund resident representative, assisted the mission.

- The last PRGF arrangement with São Tomé and Príncipe was approved in April 2000, and went off track in early 2001. A staff-monitored program was put in place for 2002, under which the country established a broadly satisfactory track record. Preliminary discussions on a new PRGF arrangement were held in 2003, but the authorities could not commit to medium-term macroeconomic policies at that time in the wake of the July 2003 coup d'état and the difficult political environment that ensued. São Tomé and Príncipe reached the decision point under the enhanced HIPC Initiative in December 2000.

- São Tomé and Príncipe is requesting a three-year arrangement under the PRGF in an amount of SDR 2.96 million (40 percent of quota) to support the program described in the attached memorandum of economic and financial policies (MEFP).

- Data are adequate for the purposes of monitoring a Fund-supported program. A full safeguards assessment of the BCSTP was completed in August 2004, with the report's recommendations being currently implemented. Relations with the Fund are summarized in Appendix I. Relations with the World Bank Group are described in Appendix II. Statistical issues are discussed in Appendix III.

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Executive Summary

- During 1998–2003, government policies helped sustain output growth and lower inflation, although the fiscal position remained unsettled. Over this period, real GDP growth increased from 2.5 percent to 4 percent, while inflation declined from 21 percent to 10 percent. Policy performance deteriorated following a coup d'état in 2003, as the government raised social spending markedly against the background of social tensions. The external current account remained dependent on donor support throughout the period, while the country also accumulated external payments arrears.

- In 2004, the economy continued to grow at a moderate pace, but inflation increased to 15 percent by year-end, as bank credit to the private sector rose sharply and the government loosened fiscal policy. In particular, the government raised expenditures to an unsustainable level in anticipation of a large oil signature bonus, which in the event was not received in 2004 and is now expected for late-June 2005. External payments arrears continued to increase in 2004, although the country remained current in its debt to multilateral institutions.

- The authorities have taken steps to ensure a proper management of oil revenues, which are potentially very large, but still uncertain. Oil production is expected to start not earlier than 2012, but in the meantime the country is expected to receive signature bonuses from the sale of exploration licenses. In December 2004, the National Assembly approved the Oil Revenue Management law which seeks to ensure transparency and accountability in the management of oil revenue and establishes rules for the gradual use of these resources. São Tomé and Príncipe has announced that it will participate in the Extractive Industries Transparency Initiative (EITI).

- The proposed program for 2005–07 aims at correcting macroeconomic imbalances and sets the conditions for sustained strong growth. Real GDP growth is envisaged to slow down in 2005 in response to tight financial policies, but pick up thereafter, while inflation is projected to decline to single-digit levels by 2007. Gross international reserves would be kept at around 3½ months of imports of goods and services. The program includes a major fiscal consolidation effort over the next three years, and the implementation of key structural reforms embodied in the country's PRSP.

- The program for 2005 envisages a large fiscal adjustment, based on a strong revenue effort (with measures totaling 2.1 percent of GDP) and significant expenditure cuts, while safeguarding spending levels on education and health. It is assumed that a Fund-supported program would pave the way for a new debt rescheduling with Paris Club creditors. Monetary policy would be aimed at reducing inflation under a market-determined exchange rate regime. Structural conditionality would cover the areas of tax reform, transparency in the management of government revenue, the finances of the water and electricity company, the development of an effective AML/CFT regime, and business climate.

- Access under the three-year arrangement would be set at SDR 2.96 million (40 percent of quota), and would be disbursed in seven equal tranches. Prior actions include parliament approval of a budget for 2005 consistent with the fiscal program and the receipt of the oil signature bonus expected for late-June 2005.

I. Introduction

1. **In the attached letter of intent the Prime Minister and Minister of Planning and Finance requests a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF) in an amount of SDR 2.96 million, equivalent to 40 percent of quota.** The arrangement would help São Tomé and Príncipe meet its challenges of macroeconomic stabilization and structural reform as set out in the attached MEFP. The proposed access, together with additional external resources that a PRGF arrangement might help to catalyze, would help São Tomé and Príncipe keep the import coverage of gross international reserves at an adequate level during the program period.

2. **The government has also submitted to the IMF and the World Bank its full poverty reduction strategy paper (*Estratégia Nacional para Redução da Pobreza*; PRSP), that was promulgated by the President of the Republic in January 2003, as well as an update of the strategy.**[1] A joint staff advisory note (JSAN)[2] concluded that the PRSP represented a credible but highly ambitious poverty reduction strategy for São Tomé and Príncipe. Its main strengths are in: (i) providing a poverty diagnosis and a comprehensive private-sector-led development strategy for São Tomé and Príncipe; (ii) paying special attention to cross-cutting issues, notably governance, health and education; and (iii) identifying detailed indicators to monitor progress in poverty reduction. Looking forward, the staff's recommendation is to further prioritize sectoral strategies, while making them fully consistent with the annual fiscal budget and the attainment of the poverty reduction targets set in the strategy.

3. **The last Article IV consultation with São Tomé and Príncipe was completed by the Executive Board on March 17, 2004.** On that occasion, Executive Directors noted that São Tomé and Príncipe had maintained broadly satisfactory macroeconomic performance in 2002 and 2003, despite a short-lived coup d'état. Directors observed that in view of the impending significant expansion in oil sector activities and the expected receipt of large signature bonuses, the authorities faced the challenge of managing properly this oil wealth against the backdrop of widespread poverty and weak institutions. Directors welcomed the authorities' intention to preserve oil income for future generations by establishing a transparent and well-managed fund for oil revenues that would stabilize the effect of oil revenues on the economy. Directors supported the authorities' interest in pursuing another Paris Club debt rescheduling and resuming discussions on a PRGF arrangement, and underscored in this regard the importance of sustaining satisfactory macroeconomic

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[1] The PRSP was not submitted earlier to the Executive Boards of the IMF and the World Bank because the macro framework was insufficiently developed to put the poverty reduction strategy into full perspective (see www.imf.org of 03/16/05 and Update www.imf.org, Sup. 1 of 03/16/05). The World Bank Executive Board discussed the PRSP and the JSAN on April 21, 2005.

[2] www.imf.org

performance and sound financial policies, while preparing and implementing oil sector legislation. They looked forward to São Tomé and Príncipe reaching the HIPC Initiative completion point once all necessary conditions have been met.

4. **A new government was established on June 7, 2005.** The former Governor of the central bank, Ms. Maria do Carmo Trovoada, was named the country's new Prime Minister and Minister of Planning and Finance. President de Menezes, as well as the new government, have restated the authorities' commitment to the economic policies described in the attached Memorandum of Economic and Financial Policies (MEFP). The new Prime Minister has signed the Letter of Intent, the MEFP, and the Technical Memorandum of Understanding.

II. Background and Recent Developments

5. **São Tomé and Príncipe is a small economy greatly dependent on external financial assistance and heavily indebted.** The country's GDP is about US$60 million (US$375 GDP per capita). Exports of goods and services—primarily tourism and cocoa—are equivalent to a third of GDP, while imports of goods and services are equivalent to more than twice this amount. The large current account deficit is being financed almost entirely by foreign grants and concessional credits (Tables 1–6). The country reached the decision point under the enhanced HIPC Initiative in December 2000. The net present value of external debt, as of end-2004, is estimated at 450 percent of exports of goods and nonfactor services.

6. **In the early 1990s, oil and natural gas deposits were discovered off-shore from São Tomé and Príncipe, but revenues from these deposits—while potentially very high—are still uncertain** (Box 1). Oil production is expected to start not earlier than 2012. In the meantime, São Tomé and Príncipe is expected to receive signature bonuses from the sale of exploration licenses. Only one license has been sold so far, with a corresponding oil signature bonus payment, totaling US$49.2 million, expected in late-June 2005.

7. **During 1998–2003, government policies helped sustain output growth and lower inflation, although the fiscal position remained unsettled**. Over this period, real GDP growth increased from 2.5 percent to 4 percent, while inflation declined from 21 percent to 10 percent. Improved policy performance, a large inflow of foreign aid, government efforts to diversify agriculture away from cocoa, and initiatives to foster a nascent tourism industry, were critical in this regard. However, in 2003, the fiscal deficit increased following a coup d'état, as the government addressed social and political pressures by increasing social outlays.[3] The external current account remained dependent on donor support throughout the period, while the external debt burden continued to be very heavy.

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[3] Also, following a successful fiscal performance in 1998–2000, spending overruns forced the 2001 domestic primary fiscal balance into a large deficit and led the PRGF-supported program off track.

Box 1. São Tomé and Príncipe's Oil Sector

Geological analysis in the early 1990s identified large oil and natural gas deposits off-shore from the islands on São Tomé and Príncipe. In 1997, the government submitted São Tomé and Príncipe's maritime boundaries for approval by the U.N. and the Gulf of Guinea Commission. The proposed territorial boundaries were contested by neighboring countries, particularly Nigeria, and it was only in 2001 that the dispute was settled.

The territorial agreement with Nigeria resulted in the creation of a Joint Development Zone (JDZ) to be administered by the Joint Development Authority (JDA) headquartered in Abuja. It was agreed that São Tomé and Príncipe would receive 40 percent of all oil revenue from the JDZ. São Tomé and Príncipe also marked out an Exclusive Development Zone (EDZ) from which it would not have to share proceeds from oil production.

During 2003, the JDA conducted the first bidding round for licensing nine blocks located in the JDZ, but the auctions resulted in the sale of a license for only one block. A bidding round for five additional blocks in the JDZ was launched in late-2004, with the results being announced in May-2005. Geological analysis of the EDZ has not yet been conducted.

8. **In 2004, the economy continued to grow at a moderate pace, but inflation increased.** Initial expectations of an economic take-off driven by oil-related foreign direct investment did not materialize. Also, some growth in fishing and tourism was offset by a decline in traditional exports, especially cocoa. At the same time, inflation increased from 10.2 percent at end-2003 to 15.2 percent at end-2004, against the background of a relaxation of fiscal policy and rapid credit growth.

Text Table 1. São Tomé and Príncipe: Key Macroeconomic Indicators, 1998-04

	1998	1999	2000	2001	2002	2003 Est.	2004 Proj.
Real GDP (annual percentage change)	2.5	3.3	3.0	4.0	4.1	4.0	3.8
Consumer Price Index (end-of-period; annual percentage change)	20.9	12.6	9.6	9.4	8.9	10.2	15.2
Domestic primary fiscal balance (percent of GDP) 1/	0.7	1.3	2.1	-12.9	-4.3	-11.7	-20.6
External current account balance (percent of GDP)							
Including official transfers	…	-26.2	-20.5	-25.3	-24.6	-20.2	-27.3
Excluding official transfers	…	-51.1	-52.4	-63.2	-54.0	-54.5	-61.5
NPV of external debt (in percent of exports of goods and services)	1634.6	1394.6	920.8	489.2	512.7	499.2	449.0
Gross international reserves 2/	3.0	3.1	3.5	4.0	3.9	4.5	3.4

Source: Table 1.

1/ Including HIPC Initiative spending.
2/ In months of following year's non-oil imports of goods and nonfactor services.

9. **Fiscal imbalances widened significantly in 2004 as a result of expenditure pressures arising from the anticipation of very large oil signature bonuses that did not materialize.**[4] The domestic primary deficit increased from 11.7 percent of GDP in 2003 to 20.6 percent of GDP in 2004, mainly reflecting an increase in government current and capital expenditure, especially during the second half of the year, to an unsustainable level in anticipation of the oil sector receipts. The expenditure hikes included a large increase in the government wage bill and spending in goods and services, as well as higher transfers to finance the government's overseas technical scholarship program. Domestically-financed capital expenditure also increased significantly.

10. **The overall fiscal deficit (on a commitment basis) increased from 17.0 percent of GDP in 2003 to 26.3 percent in 2004.** The deficit was partly financed by net credit from the BCSTP and sizeable net foreign borrowing (including interest-free loans from Nigeria and the Central Bank of Angola). Domestic payment arrears arose on account of overdue payments of São Tomé and Príncipe's share in the net operational cost of the JDA,[5] while reschedulable external arrears (on interest and principal) largely to the Paris Club[6] also increased.

11. **The expansionary fiscal stance, combined with rapid growth of bank credit to the private sector and a lack of exchange rate flexibility, contributed to a fall in international reserves during 2004.** The BCSTP relied heavily on sales of foreign exchange to keep the nominal exchange broadly unchanged in the face of downward pressures on the dobra stemming from an expansion in central bank credit to the government and an aggressive lending policy by the leading domestic bank in anticipation of new banks entering the local market.[7] As a result, gross official reserves declined from US$23 million at end-2003 to US$18 million at end-2004 (that is, from 4.5 months to 3.4 months of imports of goods and services). During 2004, the dobra appreciated by around 4.3 percent in real terms vis-à-vis the U.S. dollar, although it depreciated slightly in real effective terms (Figure 1).

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[4] The 2004 budget of anticipated that oil signature bonus payments would be received in the first quarter of 2004 for about US$150 million (three times the level now expected).

[5] Under the financial arrangement with Nigeria, São Tomé and Príncipe could defer payments on its 2002–04 contributions to the JDA until after receipt of the first oil signature bonus, currently projected for end-June 2005.

[6] These are debt-service obligations that have not been paid, but would become eligible for rescheduling in the event the country obtains a financial arrangement with the Fund.

[7] The banking system is dominated by a large bank (*Banco Internacional de São Tomé e Príncipe, BISTP),* with a controlling stake by the government, but under private management. Following a very large increase in dollar-denominated deposits in 2003, the BISTP expanded credit to the private sector markedly in 2004.

12. **The banking sector underwent important institutional changes in 2004, although the sector's interest rate spreads, the degree of dollarization of the economy, and supervision of the banking sector remained a challenge to the authorities.** Notably, the number of deposit money banks increased from two to four in the wake of the prospective oil sector expansion. Most shareholders in the new banks are foreign investors from the region. The proliferation of new banks is expected to foster financing deepening, increase financial intermediation in the agricultural sector, and reduce interest rate spreads, which are currently very wide (Table 1). At the same time, the share of foreign currency deposits in broad money remained at around 42 percent, while foreign currency-denominated loans represent the bulk of the banks' loan portfolio. Banking supervision is hampered by the limited availability of skilled supervisory staff and reliable information. In this context, the BCSTP, in consultation with the Fund's Monetary and Financial Systems Department (MFD), is training its banking supervision staff on prudential regulation accounting procedures and recruiting new examiners for supervision. At the same time, new quarterly examination reports have been submitted to banks to collect basic data for offsite prudential regulation analysis.

13. **The external current account deficit (excluding grants) remained very large in 2004, at 61.5 percent of GDP.** Grants and capital inflows, mainly in the form of foreign direct investment to the tourist sector, as well as short- and long-term government borrowing from international financial institutions—mainly African Development Bank and the World Bank—and regional neighbors (Nigeria and Angola) financed most of the current account deficit. The overall external balance registered a deficit equivalent to 14.8 percent of GDP that was financed by a loss in reserves and an accumulation of external payment arrears.

14. **The government has made significant progress towards implementing the triggers for reaching the floating completion point under the HIPC Initiative** (MEFP, paras. 45–49). A full PRSP has been prepared through a participatory process and it is being implemented. Substantial progress has been made in strengthening public expenditure management and the use of HIPC Initiative assistance. Also, a capacity-building program to ensure transparency in the management of oil resources is being adopted in consultation with the World Bank, including the establishment of a petroleum revenue oversight and a control committee consistent with the Oil Revenue Management Law that was approved by the National Assembly in December 2004 (Box 2).

Box 2. Oil Revenue Management Law (ORML)

The ORML seeks to ensure transparency and accountability in the management of oil revenue stemming from operations in São Tomé and Príncipe's JDZ and the EDZ; and establishes rules for the use of oil revenue.

Transparency and Accountability: The ORML calls for the establishment of a single National Oil Account (CNP) with a custodian foreign bank to collect all oil revenue, regular auditing of oil revenue accounts by a reputable international accounting firm, and the dissemination of information through the internet. It also establishes an investment committee that would decide on the investment of the resources accumulated in the CNP, prohibits investing in São Tomé and Príncipe assets, and prohibits any borrowing by the Sãotomean state or the JDA using actual or prospective oil revenue as collateral.

Use of Oil Revenue: The ORML sets limits on the annual transfer of resources from the CNP to the budget. For the period before production starts, the limits aim at ensuring a gradual—but complete—use of revenue from signature bonuses. For the subsequent period, the limits allow for a gradual build up of a Permanent Fund. In broad terms, for this period the annual drawings from the CNP are limited to the sum of: (i) the "long term real rate of return" multiplied by the level of the Permanent Fund; and (ii) the "long term real rate of return" multiplied by the present value of future oil revenue from fields under production. To stress that these limits should not be considered targets, the law establishes that the transfers from the CNP should not be higher than the amounts determined by the Ministry of Planning and Finance, in consultation with the central bank, taking into account the economy's absorptive capacity and the government's inflation objectives. Transfers to the budget should be used to finance programs defined in the government's PRSP.

The "long term real rate of return" is defined as the real rate of return expected on a portfolio composed of assets proportionate to the assets held in the Permanent Fund during the same period. The "long term real rate of return" is capped at 5 percent. The inflation adjustment shall use the variation rates of the official price indices in the countries of the currencies in which the Permanent Fund asset portfolio is invested.

III. MEDIUM-TERM MACROECONOMIC ISSUES AND POLICY FRAMEWORK

15. **The PRSP provides the basis for the government's medium-term economic strategy.** The PRSP targets reductions in poverty and improvements in social indicators that are broadly in line with—and, as regards reducing poverty more ambitious than—the Millennium Development Goals (MDGs). In particular, the strategy aims at reducing the percentage of São Tomé and Príncipe's population living in poverty (54 percent) by one half by 2010 and by more than two-thirds by 2015 (Table 7). While the macro framework underpinning the PRSP for 2005–07 is consistent with the PRGF program that assumes an average real GDP growth rate of 4.4 percent per annum, preliminary analysis conducted by the authorities suggests that São Tomé and Príncipe would need to grow at an average rate higher than 8 percent per annum during the next decade to meet its ambitious poverty alleviation targets in the context of the MDGs. As noted in the JSAN, this high-growth objective would only appear attainable with a large increase in private investment, as well as donor support and concessional lending to finance the refurbishing of the economy's basic infrastructure.

16. **The PRSP sets an extensive structural reform agenda aimed at promoting private sector-led growth, while supporting macroeconomic stability.** In particular, the government's strategy targets: (i) reforming public institutions, including state enterprises; (ii) fostering good governance in the management of public resources; (iii) enacting a new investment code that provides equal treatment to domestic and foreign investors; and (iv) developing a sound banking system. The government's view is that the combination of these reforms would be critical in removing constraints for faster economic growth in São Tomé and Príncipe.

17. **The PRSP acknowledges that attainment of its growth and poverty reduction objectives will depend critically on the maintenance of macroeconomic stability** (Text Table 2). Starting from this premise, the medium-term policy framework targets fiscal consolidation while allowing for appropriate spending in priority sectors. Prudent monetary policy would also be critical in securing price stability and providing confidence to the market.

Text Table 2. São Tomé and Príncipe: Key Macroeconomic Indicators, 2003-07

	2003	2004	2005	2006	2007
	Est.		Proj.		
Real GDP (annual percentage change)	4.0	3.8	3.2	4.5	5.5
Consumer Price Index (end-of-period; annual percentage change)	10.2	15.2	15.0	12.0	9.4
Domestic primary fiscal balance (percent of GDP) 1/	-11.7	-20.6	-17.5	-11.9	-7.6
Pro-poor expenditure (percent of GDP)	26.7	22.2	29.3	…	…
External current account balance (percent of GDP)					
Including official transfers	-20.2	-27.3	-28.2	-23.5	-28.7
Excluding official transfers	-54.5	-61.5	-60.3	-60.3	-63.1
NPV of external debt (in percent of exports of goods and services) 2/	499.2	449.0	459.5	347.6	361.3
Gross international reserves 3/	4.5	3.4	3.4	3.5	3.5

Source: Table 1.

1/ Including HIPC Initiative spending.
2/ Assumes completion point under the Enhanced HIPC Initiative in 2006.
3/ In months of following year's non-oil imports of goods and nonfactor services.

18. **As regards medium-term fiscal consolidation, the program targets a reduction in the domestic primary deficit from 20.6 percent in 2004 to 7.6 percent in 2007.** The three key parameters in this area are the domestic revenue effort, the government's spending envelope in goods and services, and the gradual use of the oil signature bonus payment expected in late-June 2005. The 2005 budget addresses the first of these decisively, with durable measures that will significantly boost tax receipts. Large cuts in expenditure in goods and services are also envisaged for 2005 and beyond, by hardening the budget constraint of inefficient budgetary units. In addition, the government's use of the signature bonus would be calibrated so as to ensure that these resources are used gradually and efficiently, and are not exhausted before oil production starts the next decade; this policy is consistent with the thrust of the ORML.[8] No new domestic or external payment arrears will be accumulated during the program period.

19. **The government wage bill (as a share of GDP) is programmed to increase in 2005, but to decline gradually thereafter.** The increase in 2005 reflects an increase in the monthly minimum wage of civil servants from US$31 to US$40 to address social demands. The authorities are aware that continued wage increases of this magnitude in the future would be unsustainable. In this regard, they intend to launch a thorough reform of the public sector

[8] The program assumes that out of the US$49.2 million signature bonus receipt, some US$26.4 million are used in 2005 to repay outstanding short-term obligations to the JDA (US$9.3 million), finance the budget (US$14.3 million), and settle debt service payment arrears with bilateral creditors (US$2.8 million). The remaining US$22.8 million are to be deposited in the government's National Oil Account held with the New York Federal Reserve Bank.

compensation system (MEFP, para. 16) that would contain the growth of the wage bill in the medium term.

20. **Monetary policy will be aimed at reducing inflation to single-digit levels by end-2007, while the exchange rate would be market determined, to safeguard the foreign exchange reserves of the central bank.** A substantial reduction of the fiscal deficit would facilitate the coordination of fiscal and monetary policies and the adoption of tighter monetary and credit targets. To manage liquidity, the BCSTP will launch open market operations with central bank certificates of deposits and allow interest rates to be market determined, while continuing with its policy of auctioning foreign exchange.

21. **São Tomé and Príncipe's gross external financing requirements are projected to peak at US$76.4 million in 2005, before declining to around US$49.2 million in 2006–07** (Table 8). The resources are expected to come mainly from part of the oil bonus, official grants and concessional loans, and debt relief stemming from the attainment of HIPC completion point in the first half of 2006. In 2005, all financing requirements would be fully covered after a debt rescheduling on Cologne terms with Paris Club creditors.[9] Balance of payments projections, however, show small residual gaps for 2006 and beyond, which could be covered by additional donor support. These estimates of external financing requirements are consistent with the somewhat conservative assumption that no signature bonus payments—other than the US$49.2 million on the first oil license expected in late-June 2005—would be received by São Tomé and Príncipe during the program period.[10]

22. **São Tomé and Príncipe's public debt will remain high over the medium-term.** Even after assuming debt rescheduling from the Paris Club in 2005, and further debt relief at the enhanced HIPC Initiative completion point, the NPV of debt-to-export ratio is only projected to fall from 450 percent at end-2004 to 402 percent by end-2010 (Tables 9–10), compared with the threshold of 150 percent. Debt sustainability analysis (Appendix V) shows that São Tomé and Príncipe's debt outlook (public and external) is highly vulnerable

[9] On May 10, 2005, Paris Club creditors agreed to provide financing assurances to São Tomé and Príncipe in support of its request for a PRGF arrangement with the Fund. São Tomé and Príncipe will now request a retroactive debt rescheduling on Cologne terms from December 2000. The authorities have earmarked US$1.5 million to cover interest due and late interest once bilateral agreement with Paris Club creditors are signed. To ensure comparability of treatment, US$1.3 million will also be earmarked for non-Paris Club creditors. These funds will be placed in a escrow account with the New York Federal Reserve.

[10] While the licensing round for five additional blocks in the JDZ is ongoing, they are excluded from the projections, given the significant delays experienced with the finalization of the production sharing agreement on Block 1. It was agreed with the authorities, however, that the program's macroeconomic framework might need to be substantially revised if and when new oil signature bonuses arrive.

to external shocks, particularly an exchange rate depreciation, as well as declining foreign grants and FDI. The debt indicators would also worsen in the absence of fiscal consolidation.

IV. THE ECONOMIC AND FINANCIAL PROGRAM FOR 2005

23. **The macroeconomic framework for 2005 incorporates the following assumptions:** (i) real GDP growth of 3.2 percent, consistent with putting fiscal policy on a sustainable path; (ii) a reversal in the upward trend in inflation registered in 2004; and (iii) central bank's reserve coverage target equivalent to 3.4 months of imports of goods and services. Achieving the 2005 macroeconomic objectives will require concerted implementation of fiscal and monetary policies, and of key structural reforms embodied in the PRSP.

Fiscal policy

24. **The fiscal program for 2005 includes measures to increase tax revenue—mainly excise duties in the absence of a general consumption tax—and improve tax administration, as well as policies to control the growth of public expenditure while safeguarding pro-poor spending.** The effective implementation of these measures would reduce the domestic primary deficit from 20.6 percent of GDP in 2004 to 17.5 percent in 2005.

Revenue-raising measures (MEFP, para. 13)

25. **The main measures aimed at increasing revenue by 2.1 percent of GDP in 2005 include the following**:

- The (dobra-denominated) reference prices used to assess excise duties on a core group of nonfood imports were increased in January 2005 (with an estimated yield of 1.4 percent of GDP). Previous reference prices dated from the 1990s, and had become outdated due to the depreciation of the dobra.

- The excise tax levied on services was increased from 2 percent to 5 percent (estimated yield of 0.4 percent of GDP) effective July 15, 2005.

- The deduction on the excise duty on domestically-produced beer was terminated, with the new ad valorem rate set at 25 percent on July 15, 2005 (estimated yield of 0.2 percent of GDP).

- Revenue from urban property taxes will be boosted in 2005 by an increase in coverage and tighter enforcement of regulations governing the collection of these taxes. It is expected that the coverage could be tripled from the current level of 4,000 registered dwellings, yielding dobras 800 million (0.1 percent of GDP) in additional revenue in 2005.

26. **The fiscal program includes substantive reforms of the personal and corporate income tax systems that would set a more progressive income tax regime and seek to harmonize corporate taxation with international practices.** The draft new tax codes will be submitted to the National Assembly by end-July 2005, with the new tax regimes entering into effect in January 2006.

27. **In addition, the government will continue to keep retail petroleum prices in line with world market prices.** However, for 2005, any decline in world market prices will not be passed-through to consumers, and instead the margin would accrue to the treasury.

Enhanced tax administration (MEFP, para. 14)

28. **A new tax code and a new tax procedural code will be introduced by end-July 2005 to bolster taxpayers' rights and obligations.** Operationally, this translates into the establishment of: (i) tax tribunals at different levels of government to handle tax issues and disputes, (ii) stiff penalties for tax violations, and (iii) more adequate resources for tax collection and enforcement. Other policies to improve tax administration include the streamlining and simplification of taxes such as the urban property tax, inheritance taxes, taxes on grants, and taxes on asset transfers. In addition, the government will continue to enforce the use of taxpayer identification numbers throughout the territory.

Strengthening expenditure controls (MEFP, paras. 15–19)

29. **The wage bill** will increase in 2005 by 2 percent of GDP, following the increase in the minimum wage to US$40 per month. However, to correct distortions stemming from the current compensation system, including an obsolete wage grid, the 2005 fiscal program will seek to eliminate all selective salary increases and special wage regimes. The new policy framework will: (i) broaden the scope of wage negotiations to cover all government employees at the same time and (ii), for purposes of wage negotiations, introduce a broader concept of remuneration to include salaries, overtime fees, supplementary salary payments, and other subsidies. With these measures in place, the increase in the nominal wage bill will be contained below the annual inflation rate in 2006 and 2007.

30. **The 2005 fiscal program provides for significant cuts in current expenditure in goods and services, as well as in domestically-financed capital expenditure.** The core of the spending cuts in goods and services will fall on telecommunication spending of budgetary units, water and electricity consumption, and spending on official travel. Regarding domestically-financed capital expenditure, in implementing the cuts, the authorities would ensure a minimal level of disruption to the government's social expenditure program. Furthermore, part of the foreseen reduction reflects projects which had initially been earmarked for domestic funding, but which the government now intends to fund through foreign-financed counterpart funds, despite an estimated reduction in overall capital spending.

31. **Aggregate pro-poor spending, as defined in the government's Poverty Reduction Strategy is budgeted at 29.3 percent of GDP, from an estimated 22.2 percent of GDP in**

2004. Pro-poor spending on the health and education sectors—which includes the impact of a US$40 minimum wage paid to teachers, doctors, and other personnel working in these sectors—is projected to increase by a combined 3.1 percent of GDP. Pro-poor spending in other sectors, including social infrastructure and provision of potable water, will also increase. The bulk of the higher pro-poor spending will be in the form of capital outlays.

Monetary and exchange rate policy (MEFP, paras. 24–27)

32. The monetary program assumes broad money growth of 12.3 percent, which is consistent with the government's output and inflation objectives for 2005. The program assumes a broadly stable velocity of circulation of money. Based on the fiscal program described above and largely constant banking sector net foreign assets, the program implies an increase in credit to the private sector of 19 percent during the year.

33. **The exchange rate will be market determined, with foreign exchange market interventions aimed at meeting the international reserves target of the program.** While small interventions could be useful in smoothing short-term exchange rate fluctuations, persistent one-sided pressures should be allowed to be fully reflected in the exchange rate.[11]

34. **At the same time, the BCSTP will remain fully engaged in the development of indirect monetary instruments.** Following the introduction of foreign exchange auctions in late 2004, the next step includes the development of a market for central bank certificates of deposits to help manage liquidity in the economy, particularly in the period following the receipt of the oil signature bonus on Block 1.

External sector policies (MEFP, paras. 32–34)

35. **The program will seek to address the constraints impeding a diversified and expanded trade performance by São Tomé and Príncipe.** To this end, the government will continue to seek technical advice from the international community in the context of the Integrated Framework for Trade-Related Technical Assistance.

36. **The authorities put a high priority in São Tomé and Príncipe being part of the upcoming Economic Partnership Agreement (EPA) negotiations between the EU and Sub-Saharan countries.** The implications for São Tomé and Príncipe are twofold. First, as established in the Cotonou Agreement the EU is negotiating EPAs with trading blocks rather than with individual countries. São Tomé and Príncipe would in principle join CEMAC for EPA negotiation purposes, although discussions concerning the precise form of its association are still ongoing. Second, EPAs include a provision for reciprocity in preferential

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[11] São Tomé and Príncipe's exchange rate regime is currently classified by the Fund as managed floating. The spread between the official and the parallel rates of the dobra has been below 1 percent since 1999.

tariff reductions with the EU, which could imply significant reductions in duties on goods originating in the EU. The authorities are aware of these potential revenue losses and agreed to keep the staff fully-informed about their policy intentions and decisions in this area throughout the duration of the Fund-supported program.

37. **Regarding the trade regime, the government will conduct a survey of existing customs exemptions during 2005** with a view to their gradual elimination during the coming years, except for exemptions contemplated in international accords. At the same time, the existing non-tariff barrier related to the privately-managed (though partially state-owned) telecommunications company (CST) will be eliminated by end-December 2005. Existing regulations protecting CST from competition will expire on that date, thus opening the sector to new operators.

38. **The economic program for 2005 includes a number of structural policies geared to foster private sector investment and increase the growth potential of the economy (Box 3)**. In the case of the oil sector, these policies would be complemented by the implementation of expert advice from the World Bank on governance issues, including in the context of São Tomé and Príncipe's participation in the EITI, to ensure that the country avoids mistakes made by other resource rich countries.

Box 3. Structural Conditionality

Coverage under the proposed PRGF arrangement

Structural conditions in the first year of the proposed arrangement (MEFP, Table I.2) cover policy measures that are critical to the effective implementation of the PRSP's macroeconomic framework. Key areas include:

- **Strengthening the tax revenue base** (MEFP, paras. 13, 14)—Submit to the National Assembly: (i) new tax codes on personal income taxation and corporate taxation; (ii) a new tax procedural code; (iii) new guidelines on urban property taxation; and (iv) new legislation on inheritance taxes.

- **Governance and public expenditure management** (MEFP, paras. 20–23)—Establish a timetable for the implementation of an integrated budgetary classification and information system in line with the recommendations of the Fund's Fiscal Affairs department (FAD) and the World Bank.

- **AML/CFT regime** (MEFP, para. 31)—Submit to the National Assembly legislation criminalizing money laundering and the financing of terrorism.

- **State enterprise finances** (MEFP, paras. 36–38)—Develop a strategy to address the financial weaknesses of the water and electricity company (EMAE), including a timetable for the reduction of arrears. Conduct feasibility studies on the privatization of the port authority (ENAPORT) and the airport and air security state company (ENASA).

- **Business climate and agricultural sector development** (MEFP, paras. 39–41)—Submit to the National Assembly a new investment code that provides equal treatment for domestic and foreign investors and is consistent with the new code on corporate taxation. Launch a study to analyze the factors that may be obstructing the development and diversification of the agricultural sector, including the economic effects from a lack of complete property rights for land-holders.

Structural areas covered by World Bank lending and conditionality

Areas of ongoing World Bank lending (Appendix II) include social sector support projects and capacity building, including technical advice on good governance practices and other petroleum-sector related issues (MEFP, para. 35). A Country Assistance Strategy paper was discussed by the World Bank Executive Board on June 2, 2005. A Diagnostic Trade Integration Study is also being prepared under the Integrated Framework for Trade-Related Technical Assistance (MEFP, para. 32).

Statistical issues

39. **São Tomé and Príncipe's economic and financial statistics remain in need of improvement, although the core macroeconomic data remain adequate for the purposes of monitoring a Fund-supported program** (Appendix III). Work is ongoing to improve fiscal, monetary and national accounts statistics with assistance from the World Bank, as well as STA under the Fund's General Data Dissemination System (GDDS) Lusophone Project.

V. Access, Phasing, and Capacity to Repay the Fund

40. **Proposed access under the PRGF arrangement is SDR 2.96 million (40 percent of quota), to be disbursed in seven equal tranches** (Table 11). This level is marginally lower than the norm for second PRGF users, and seeks to strike a balance between the merits of the program and the need for financing mentioned above, and some risks of implementation. This access, together with additional external resources that a PRGF arrangement might help to catalyze, would help keep the import coverage of gross international reserves at around 3.5 months during the program period. By the end of the arrangement, São Tomé and Príncipe's use of fund resources would be equivalent to 49 percent of quota (Table 12); this estimate takes into account the country's profile of projected obligations to the Fund (totaling SDR 0.94 million) during 2005–07. Given the strong adjustment envisaged under the program, the country can be expected to meet its future obligations to the Fund. During the period of the arrangement, São Tomé and Príncipe's repayment of principal and interest to the Fund will not exceed 2 percent of exports of goods and services in any single year.

41. **The main risks to the program arise from the country's political cycle and its weak institutional capacity.** The prospect of oil revenue has raised popular expectations, and thus maintaining a sound fiscal stance in such an environment may be difficult, particularly in the period leading to the July 2006 presidential elections. However, the authorities have ratified their commitment to fiscal consolidation and price stability. They also consider that a Fund-supported program would play an important role in helping them withstand spending pressures under the circumstances. Program implementation may also be complicated by weak institutional capacity, particularly in regards to budgetary planning and monetary policy.

VI. Staff Appraisal

42. **After a favorable performance on disinflation and economic growth during 1998–2003, the conduct of financial policies came under pressure in 2004.** A relaxation of fiscal policy and rapid credit growth led to an increase in inflation. At the same time, economic activity slowed moderately, as initial expectations about the take-off of the economy in anticipation of the development of the oil sector did not materialize. Also, the official international reserve position also came under stress as the BCSTP relied heavily on intervention in the foreign exchange market to prevent a depreciation of the dobra.

43. **Despite the setbacks of 2004, the staff believes that upfront actions taken by the authorities to launch the program for 2005–07 will help regain the momentum needed**

to stabilize the economy and start delivering the ambitious medium-term goals set out in the government's PRSP. The strong revenue measures, the actions taken to control the growth of current and capital expenditure, along with a more flexible exchange rate policy supported by new indirect monetary instruments, are all directed towards improving policy implementation in those areas where problems were encountered in 2004.

44. **The tax measures incorporated in the 2005 budget represent an important effort to boost tax receipts and modernize the personal and corporate taxation systems.** Together with the anticipated external support, including in the form of debt relief under the enhanced HIPC Initiative, the strengthened revenue base should make possible an increase in pro-poor spending required under the growth and poverty reduction strategy. Envisaged reforms in tax administration are also critical for establishing a transparent and fairer tax system.

45. **The expenditure allocations in the 2005 budget are austere, but are closely aligned with the priorities established in the PRSP.** The authorities are aware that their fiscal consolidation goals and the government's tight budget constraint require controlling the growth of the wage bill and reforming the framework for civil service wage negotiations. To ensure fiscal sustainability, it is essential that the wage increases granted in 2005 be treated as exceptional, and that any other ad-hoc wage increases be avoided in the future. The staff is encouraged in this context by the government's decision to eliminate all selective salary increases and/or special wage regimes. The new policy framework will: (i) broaden the scope of wage negotiations to cover all government employees; and (ii) for purposes of wage negotiations, will redefine the concept of remuneration to include the basic salary, overtime fees, supplementary salary payments, and other subsidies. The latter policy should help the authorities in effectively assessing the overall budgetary impact of their wage negotiations with the unions.

46. **A strengthened fiscal position should facilitate the coordination of fiscal and monetary policies and the adoption of a monetary stance consistent with disinflation and a flexible exchange rate policy that would safeguard the NIR targets under the program.** Full compliance with the program limits on net domestic assets of the central bank would be critical towards reaching the government's inflation target. Active open market operations should provide an additional monetary tool to pursue the BCSTP's parallel need of managing liquidity and accumulating international reserves.

47. **The staff welcomes the authorities' commitment to strengthen the finances of the water and electricity company (EMAE) and fostering private investment in the sector.** Recurrent payment arrears on water and electricity bills have significantly impaired the finances of EMAE and, therefore, the government's actions to set a credible and lasting solution to this problem in the context of the program is encouraging. Also, the decision to engage large private investors with renowned technical qualifications in the production of hydroelectric and thermal electricity seems adequate given the size of the local market and the need to lower electricity production costs, while fostering private sector-led growth.

48. **The PRSP encompasses a broad range of institutional and structural reforms, the determined implementation of which would be fundamental for the success of the strategy.** Some of the reforms, notably in public expenditure management and anti-money laundering legislation will be monitored and supported under the proposed PRGF arrangement. But, in most areas, the authorities will need to draw on the technical and financial support of other development partners. In particular, the authorities have agreed to work expeditiously with the World Bank to prepare and begin action plans for reforms in these areas, including the energy sector, privatization of state enterprises, and governance. The passage of the oil revenue management law and the decision to participate in the EITI are important steps to secure transparency and accountability in the management of oil revenue.

49. **In view of the strength of the proposed program, including the prior actions already taken, the staff supports the authorities' request of a three-year PRGF arrangement in an amount of SDR 2.96 million equivalent to 40 percent of quota.** In the staff's view, the proposed access strikes an appropriate balance between the need to support São Tomé and Príncipe's efforts to achieve sustainable economic growth and poverty reduction, and the risks to the Fund.

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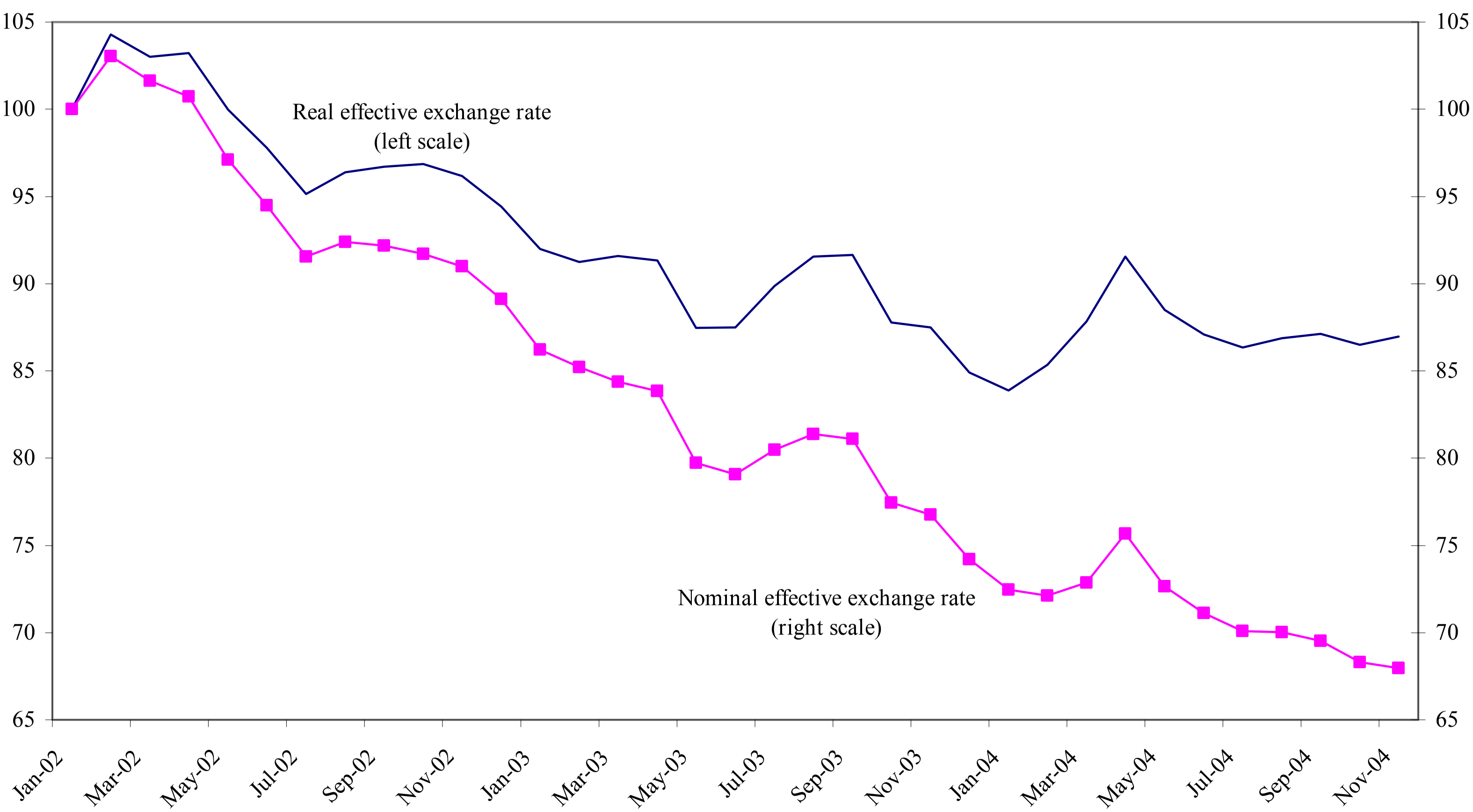
Figure 1 . São Tomé and Príncipe: Effective Exchange Rates, 2002–04
(Index, January 2002=100)



Source: Information Notice System.

Table 1. São Tomé and Príncipe: Selected Economic Indicators, 2001-10

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
					Prog.		Proj.			
	(Annual percentage changes, unless otherwise specified)									
National income and prices										
GDP at constant prices	4.0	4.1	4.0	3.8	3.2	4.5	5.5	6.5	7.0	7.5
Consumer prices (percentage change; end of period)	9.4	8.9	10.2	15.2	15.0	12.0	9.4	8.0	7.0	6.0
Consumer prices (percentage change; average)	9.5	9.2	9.6	12.8	15.1	13.4	10.6	8.7	7.5	6.5
External trade										
Exports, f.o.b. 1/	15.4	37.6	19.4	13.8	6.0	0.2	0.0	-17.4	1.7	4.8
Of which : cocoa	11.3	41.7	19.6	-4.5	7.9	0.0	-0.2	-0.2	-0.2	-0.5
Imports, c.i.f.	6.8	16.6	17.2	9.0	4.6	6.7	11.3	10.9	9.4	10.1
Of which : non-oil sector imports	6.8	16.6	17.2	9.0	1.0	4.5	7.6	8.2	7.4	11.5
Exchange rate (in dobras per U.S. dollar; end of period)	9,020	9,192	9,456	10,104	...	...	...	...	...	...
Real effective exchange rate (depreciation -)	-0.6	-5.2	-8.7	-2.7	…	…	…	…	…	…
Terms of trade	24.5	52.7	-11.6	-20.3	0.2	0.4	-0.2	-0.8	-0.5	-0.9
Money and credit (end of period)										
Net domestic assets 2/	-40.7	-0.2	11.0	17.1	3.6	9.0	14.0	16.3	19.4	18.6
Of which: credit to government (net) 2/	15.4	-0.2	15.3	6.0	1.8	-11.4	-15.9	-11.7	-14.7	-10.3
credit to the economy 2/	-2.7	12.1	20.6	34.4	11.3	15.1	14.1	13.1	13.0	13.0
Broad money	36.7	26.9	41.8	7.4	12.3	21.9	21.9	16.7	16.4	15.4
Velocity (ratio of non-oil GDP to average broad money)	3.2	2.8	2.3	2.2	2.4	2.4	2.3	2.3	2.3	2.3
Central bank reference interest rate (in percent; end of period)	15.5	15.5	14.5	14.5	…	…	…	…	…	…
Commercial bank lending rate (in percent; end of period)	38.0	38.0	30.0	30.0	…	…	…	…	…	…
Commercial bank deposit rate (in percent; end of period)	15.0	15.0	10.3	10.3	…	…	…	…	…	…
	(In percent of GDP, unless otherwise specified)									
National accounts										
Consumption	123.0	117.5	116.7	122.0	122.0	121.4	118.1	116.1	112.9	111.6
Gross investment	35.8	32.5	36.1	34.5	37.3	40.2	47.7	50.9	52.4	49.4
Public investment	21.6	14.5	20.1	19.4	16.4	16.0	15.5	14.8	13.8	13.0
Private investment	14.2	18.0	16.0	15.1	21.0	24.3	32.2	36.1	38.6	36.4
Of which: non-oil sector (in percent of non-oil GDP)	14.2	18.0	16.1	15.1	15.1	15.1	17.5	17.5	17.6	17.6
Gross domestic savings	14.8	-17.5	17.6	12.2	10.6	16.0	16.8	15.8	16.1	13.6
Public savings 3/	9.4	12.5	13.8	6.6	84.4	23.2	23.8	22.5	21.7	20.0
Gross national savings	10.5	8.0	15.9	7.1	9.2	16.7	18.9	17.6	17.7	15.6
Government finance										
Total revenue, grants and oil signature bonus	59.0	50.5	58.1	59.3	127.9	63.9	61.9	59.0	56.1	52.6
Of which : tax revenue	18.3	19.5	20.7	23.4	24.1	24.2	24.6	25.0	25.1	25.3
grants	37.8	27.2	32.5	30.9	28.2	33.2	31.2	30.0	27.2	23.7
oil signature bonus	…	…	…	…	71.0	…	…	…	…	…
unidentified revenue measures	…	…	…	…	…	2.0	1.9	1.8	1.7	1.6
Total expenditure and net lending	79.5	66.9	75.1	85.6	76.5	71.2	66.1	63.1	59.2	55.8
Of which: noninterest current expenditure	23.0	26.9	28.4	41.7	37.8	33.6	30.2	28.6	27.0	25.3
capital expenditure	46.0	28.8	35.8	35.8	29.3	28.9	28.1	27.2	25.4	24.2
Domestic primary balance (commitment basis; incl. HIPC Initiative spending) 4/	**-12.9**	**-4.3**	**-11.7**	**-20.6**	**-17.5**	**-11.9**	**-7.6**	**-5.5**	**-4.5**	**-3.9**
Overall balance (commitment basis; including grants)	-20.5	-16.4	-17.0	-26.3	51.4	-7.3	-4.1	-4.1	-3.1	-3.2
Overall balance (cash basis; including grants)	-19.6	-6.4	-11.9	-19.8	27.7	-7.3	-4.1	-4.1	-3.1	-3.2
External sector										
Current account balance (including official transfers)	-25.3	-24.6	-20.2	-27.3	-28.2	-23.5	-28.7	-33.3	-34.6	-33.9
Current account balance (excluding official transfers)	-63.2	-54.0	-54.5	-61.5	-60.3	-60.3	-63.1	-64.7	-63.1	-58.7
Non-oil current account balance (excl. official transfers) 5/	-63.2	-54.0	-54.7	-63.7	-56.6	-53.2	-50.4	-46.6	-42.6	-40.4
Net present value of total external debt 6/ 7/ 8/	489.2	512.7	499.2	449.0	465.3	358.1	375.6	390.8	398.5	401.9
Net present value of total external debt 6/ 7/ 9/	755.9	693.2	634.2	550.6	619.7	427.3	440.6	468.5	458.0	442.8
Scheduled external debt service before debt relief 8/	41.3	60.8	58.0	50.6	56.7	51.9	49.6	48.9	46.1	42.6
External debt service paid	23.9	20.0	25.4	…	...	...	...	...	...	...
Export earnings (in millions of U.S. dollars)	3.7	5.1	6.0	6.9	7.3	7.3	7.3	6.0	6.1	6.4
Overall balance (in millions of U.S. dollars)	0.5	-2.4	1.8	-9.5	19.2	-12.6	-11.8	-9.6	-7.6	-8.2
Gross foreign reserves (in months of following year's non-oil imports of goods and nonfactor services) 10/	4.0	3.9	4.5	3.4	3.4	3.5	3.5	3.5	3.5	3.5
Permanent oil fund (in millions of U.S. dollars) 11/	…	…	…	…	23.1	19.2	15.1	11.0	6.7	2.3

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

1/ During 2004-07, includes US$1.4 million per year in re-exports of oil arising from aid in kind received from Nigeria.
2/ In percent of broad money at beginning of period.
3/ Government revenue includes HIPC debt relief. In 2005, reflects receipt of US$49.2 million from oil signature bonus on Block 1.
4/ Excluding oil revenue, grants, interest earned and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2002-04, it also excludes transfers to the JDA, which are to be repaid with proceeds from the oil signature bonus from Block 1.
5/ Excluding oil exports, c.i.f. imports of oil sector-related goods and services, and oil sector profit remittances.
6/ Including arrears to Italy on a loan that remains in dispute.
7/ Assumes that the completion point under the enhanced HIPC Initiative is reached in 2006.
8/ In percent of exports of goods and nonfactor services, calculated as a three-year backward-looking average (e.g., average over 2001-03 for exports in 2003).
9/ In percent of government revenue.
10/ Excluding guarantee deposits placed at the central bank by prospective financial institutions pending operating licenses.
11/ Includes interest income earned on oil fund.

Table 2. São Tomé and Príncipe: Financial Operations of the Central Government, 2001-10

(In billions of dobras, unless otherwise indicated)

	2001	2002	2003	2004	2005				2006	2007	2008	2009	2010
					Prel.	Proj.	Prog.		Prog.		Proj.		
					Jan.-Mar.	Jan.-Jun.	Jan.-Sep.	Jan-Dec					
Total revenue and grants	**248.8**	**245.6**	**321.0**	**372.9**	**62.6**	**712.5**	**830.7**	**952.8**	**570.7**	**652.6**	**725.2**	**802.5**	**868.2**
Oil revenue 1/	0.0	0.0	1.1	13.7	3.5	7.1	10.9	15.1	16.6	17.8	0.0	0.0	0.0
Non-oil revenue	89.2	113.4	140.4	165.0	32.7	84.8	139.5	198.7	239.3	285.8	334.0	389.1	450.5
Tax revenue	77.2	95.0	114.2	147.3	29.6	72.3	121.2	179.4	216.0	259.8	307.2	359.0	416.9
Nontax revenue	12.0	18.4	26.2	17.6	3.1	12.6	18.3	19.4	23.3	26.0	26.8	30.1	33.6
Grants	159.5	132.2	179.4	194.3	26.4	91.6	151.4	210.1	296.7	329.0	369.3	389.5	392.0
Project grants	120.9	110.0	142.1	137.7	26.4	74.4	111.7	148.9	181.6	214.0	245.6	255.8	264.0
Nonproject grants	17.3	0.5	2.4	20.4	0.0	0.0	0.0	0.0	9.3	10.0	13.9	17.4	9.0
HIPC Initiative-related grants	21.4	21.8	35.0	36.1	0.0	17.2	39.7	61.3	105.8	105.0	109.8	116.3	119.1
Multilateral	21.4	21.8	35.0	36.1	0.0	17.2	25.9	33.7	37.1	39.8	41.9	43.7	45.0
Bilateral (before HIPC completion point)	0.0	0.0	0.0	0.0	0.0	0.0	13.8	27.6	56.0	26.8	31.0	35.5	36.9
Completion point debt relief 2/	…	….	….	…	…	…	…	…	12.7	38.4	36.9	37.2	37.1
Oil signature bonuses	…	….	….	…	…	528.9	528.9	528.9	0.0	0.0	0.0	0.0	0.0
Unidentified revenue measures	…	….	….	…	…	…	…	…	18.0	20.1	22.0	23.9	25.6
Total expenditure and net lending	**335.3**	**325.6**	**415.1**	**538.6**	**112.9**	**250.0**	**403.5**	**570.2**	**647.5**	**706.9**	**786.6**	**858.2**	**936.4**
Current expenditure	121.9	156.8	183.3	292.5	68.1	136.9	224.7	318.3	341.3	359.8	400.3	439.2	476.2
Personnel costs	40.5	43.6	55.0	75.7	19.7	41.5	73.5	103.3	113.6	125.0	135.7	145.6	154.7
Financed by Treasury	40.5	43.6	55.0	75.7	19.7	41.5	70.1	96.7	113.6	125.0	135.7	145.6	154.7
Financed by HIPC relief	…	…	…	…	…	…	3.3	6.7	0.0	0.0	0.0	0.0	0.0
Goods and services 3/	18.8	26.7	43.9	95.8	14.6	28.4	43.1	58.3	61.2	64.0	74.7	86.9	100.2
Interest on external debt due	23.6	25.9	26.1	30.1	8.2	17.0	25.2	34.0	38.7	39.2	46.1	51.0	55.4
Interest on internal debt due	1.1	0.0	0.0	0.0	0.6	1.3	1.9	2.5	2.5	2.5	2.5	2.5	2.5
Transfers	13.1	40.7	35.9	65.9	20.9	38.9	62.9	92.6	95.7	97.7	106.9	115.8	124.2
Of which: Regular transfers	13.1	9.4	13.4	39.9	12.3	25.7	39.2	56.0	57.5	58.7	63.8	68.6	73.0
Foreign-funded scholarship program	…	…	1.1	13.7	3.5	7.0	10.5	15.1	16.6	17.8	18.3	18.9	19.4
Domestically-funded scholarship program	…	…	…	12.0	5.4	10.8	16.2	21.6	21.6	21.6	21.6	21.6	21.6
Joint Development Agency 4/	…	31.3	22.6	26.0	8.6	13.3	23.7	36.6	38.3	39.0	43.2	47.2	51.1
Other	24.8	20.0	22.4	25.0	4.1	9.8	18.3	27.7	29.6	31.4	34.4	37.4	39.2
Capital expenditure	194.3	140.0	197.9	225.0	36.5	104.4	159.0	218.2	257.9	296.7	333.8	363.8	400.2
Financed by the treasury	29.4	12.3	38.0	50.5	0.0	9.8	17.0	28.9	31.8	34.9	38.0	55.5	82.1
Financed by external sources	164.9	127.7	160.0	174.5	36.5	94.7	142.0	189.3	226.1	261.7	295.9	308.2	318.0
HIPC Initiative-related social expenditure	17.2	22.5	33.6	30.1	3.6	8.6	19.8	33.7	48.3	50.4	52.5	55.2	60.0
Mulatilateral	17.2	22.5	33.6	30.1	3.6	8.6	19.8	33.7	37.1	39.8	41.9	43.7	45.0
Bilateral debt relief before completion point	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	11.2	10.6	10.6	11.6	15.0
Public service restructuring 5/	1.9	6.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net lending	0.0	0.0	0.3	-9.0	4.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (commitment basis)	**-86.5**	**-80.0**	**-94.1**	**-165.7**	**-50.3**	**462.5**	**427.2**	**382.7**	**-76.8**	**-54.3**	**-61.4**	**-55.6**	**-68.2**
Change in arrears (net; reduction -)	3.8	48.8	28.3	41.0	25.7	-174.8	-174.8	-176.0	0.0	0.0	0.0	0.0	0.0
External arrears 6/	3.8	14.9	9.4	13.8	8.2	-78.3	-78.3	-78.3	0.0	0.0	0.0	0.0	0.0
Domestic arrears	0.0	34.0	18.8	27.2	17.5	-96.5	-96.5	-97.7	0.0	0.0	0.0	0.0	0.0
Of which: Joint Development Agency 4/	…	31.3	22.6	26.0	8.6	-96.5	-96.5	-96.5	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-82.7**	**-31.1**	**-65.8**	**-124.7**	**-24.6**	**287.7**	**252.5**	**206.7**	**-76.8**	**-54.3**	**-61.4**	**-55.6**	**-68.2**

Table 2. São Tomé and Príncipe: Financial Operations of the Central Government, 2001-10 (concluded)

(In billions of dobras, unless otherwise indicated)

	2001	2002	2003	2004	2005				2006	2007	2008	2009	2010
					Prel.	Proj.	Prog.		Prog.		Proj.		
					Jan.-Mar.	Jan.-Jun.	Jan.-Sep.	Jan-Dec					
Overall fiscal balance (commitment basis)	**-86.5**	**-80.0**	**-94.1**	**-165.7**	**-50.3**	**462.5**	**427.2**	**382.7**	**-76.8**	**-54.3**	**-61.4**	**-55.6**	**-68.2**
Change in arrears (net; reduction -)	3.8	48.8	28.3	41.0	25.7	-174.8	-174.8	-176.0	0.0	0.0	0.0	0.0	0.0
External arrears 6/	3.8	14.9	9.4	13.8	8.2	-78.3	-78.3	-78.3	0.0	0.0	0.0	0.0	0.0
Domestic arrears	0.0	34.0	18.8	27.2	17.5	-96.5	-96.5	-97.7	0.0	0.0	0.0	0.0	0.0
Of which : Joint Development Agency 4/	…	31.3	22.6	26.0	8.6	-96.5	-96.5	-96.5	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-82.7**	**-31.1**	**-65.8**	**-124.7**	**-24.6**	**287.7**	**252.5**	**206.7**	**-76.8**	**-54.3**	**-61.4**	**-55.6**	**-68.2**
Financing	**82.7**	**31.1**	**65.8**	**124.7**	**24.6**	**-287.7**	**-252.5**	**-206.7**	**76.8**	**54.3**	**61.4**	**55.6**	**68.2**
External (net)	31.9	3.6	24.7	72.5	-21.2	-28.5	-43.2	-43.8	-8.8	-15.2	-21.5	-8.5	-15.7
Disbursements (projects)	42.9	17.7	17.9	36.8	10.1	20.2	30.3	40.4	44.5	47.8	50.3	52.4	54.1
Program financing (loans)	25.8	0.0	30.8	50.3	0.0	10.4	10.4	21.6	60.9	65.4	66.9	83.6	77.3
Short-term loans (Nigeria and Angola) (net) 7/	0.0	45.0	46.7	58.7	0.0	-10.4	-10.4	-10.4	0.0	0.0	0.0	0.0	0.0
Scheduled amortization (medium and long-term)	-36.7	-59.1	-70.8	-73.2	-31.3	-48.7	-73.5	-95.4	-114.2	-128.3	-138.7	-144.6	-147.1
Domestic (net)	35.6	-1.8	16.0	17.2	14.5	-63.6	-27.3	5.2	-37.9	-64.7	-57.9	-84.7	-69.2
Bank credit (net)	17.3	-0.3	29.7	16.6	27.5	-63.6	-27.3	5.2	-37.9	-64.7	-57.9	-84.7	-69.2
Of which : HIPC Initiative account	-4.3	0.7	-4.1	-6.0	3.6	-8.5	-6.2	0.0	0.0	0.0	0.0	0.0	0.0
Nonbank financing	18.3	-1.5	-13.7	0.7	-13.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Oil reserve fund flows (net) 8/	0.0	0.0	0.0	0.0		-245.0	-245.0	-245.0	53.9	57.9	61.0	63.5	65.6
Change in arrears (principal)	15.2	29.3	25.1	34.9	31.3	-145.6	-145.6	-145.6	0.0	0.0	0.0	0.0	0.0
Paris Club rescheduling	0.0	0.0	0.0	0.0	0.0	194.9	208.6	222.4	68.7	65.3	67.9	72.6	74.0
Reschedulable arrears 9/	0.0	0.0	0.0	0.0	0.0	194.9	194.9	194.9	0.0	0.0	0.0	0.0	0.0
Debt relief (bilateral-without completion point)	0.0	0.0	0.0	0.0	0.0	0.0	13.8	27.6	56.0	26.8	31.0	35.5	36.9
Completion point debt relief	…	…	…	…	…	…	…	…	12.7	38.4	36.9	37.2	37.1
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.8	11.0	11.9	12.7	13.5
Memorandum items:													
Domestic primary balance (commitment basis) 10/	-54.5	-21.1	-64.9	-129.3	-31.4	-45.2	-84.4	-130.6	-106.2	-79.8	-67.9	-64.5	-64.9
Overall balance (commitment basis, excluding Oil Signature Bonuses)	-86.5	-80.0	-94.1	-165.7	-50.3	-66.4	-101.7	-146.2	-76.8	-54.3	-61.4	-55.6	-68.2

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

1/ During 2004-07, includes US$1.4 million in re-exports of oil arising from aid in kind received from Nigeria.

2/ The projections assume that São Tomé and Príncipe reaches HIPC Completion point in the first half of 2006.

3/ In 2004, includes Db20.8 billion (i.e. 3.3 percent of GDP) for hosting the 2004 conference of the Community of Portuguese Language countries (CPLP).

4/ Under the arrangement with Nigeria, São Tomé and Príncipe could defer payments on its 2002-04 contributions to the Joint Development Agency until receipt of the first oil signature bonus.

5/ Severance packages totaling Db 8,000 million were financed by a Structural Adjustment Facility grant from the European Union in 2001-02.

6/ Interest arrears on Paris Club and non-Paris Club bilateral debt.

7/ For 2002-04, includes three US$5 million loans from Nigeria borrowed during 2002-04 and a US$1 million loan from Angola borrowed in 2004. Repayment of the Nigeria loans has been rescheduled until receipt of oil signature bonuses other than on Block 1. The US$1 million from Angola is due to be repaid in 2005.

8/ For 2006-10, drawings from the oil fund are equivalent to 20 percent of the oil permanent fund at end-2004 (in line with the Oil Revenue Management Law).

9/ For 2005, reflects impact of Paris Club rescheduling in the third quarter of 2005.

10/ Excluding the oil revenue including the Nigeria oil grant, non-oil grants, interest earned and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2002-04, it also excludes transfers to the JDA, which are to be repaid with proceeds from the oil signature bonus on Block 1. Includes HIPC Initiative-related social expenditure.

Table 3. São Tomé and Príncipe: Financial Operations of the Central Government, 2001-10

(In percent of GDP, unless otherwise indicated)

	2001	2002	2003	2004	2005				2006	2007	2008	2009	2010
					Prel.	Proj.	Prog.		Prog.		Proj.		
					Jan.-Mar.	Jan.-Jun.	Jan.-Sep.	Jan-Dec					
Total revenue and grants	**59.0**	**50.5**	**58.1**	**59.3**	**8.4**	**95.6**	**111.5**	**127.9**	**63.9**	**61.9**	**59.0**	**56.1**	**52.6**
Oil revenue 1/	0.0	0.0	0.2	2.2	0.5	1.0	1.5	2.0	1.9	1.7	0.0	0.0	0.0
Non-oil revenue	21.1	23.3	25.4	26.2	4.4	11.4	18.7	26.7	26.8	27.1	27.2	27.2	27.3
Tax revenue	18.3	19.5	20.7	23.4	4.0	9.7	16.3	24.1	24.2	24.6	25.0	25.1	25.3
Nontax revenue	2.9	3.8	4.7	2.8	0.4	1.7	2.5	2.6	2.6	2.5	2.2	2.1	2.0
Grants	37.8	27.2	32.5	30.9	3.5	12.3	20.3	28.2	33.2	31.2	30.0	27.2	23.7
Project grants	28.6	22.6	25.7	21.9	3.5	10.0	15.0	20.0	20.3	20.3	20.0	17.9	16.0
Nonproject grants	4.1	0.1	0.4	3.2	0.0	0.0	0.0	0.0	1.0	0.9	1.1	1.2	0.5
HIPC Initiative-related grants	5.1	4.5	6.3	5.7	0.0	2.3	5.3	8.2	11.8	10.0	8.9	8.1	7.2
Multilateral	5.1	4.5	6.3	5.7	0.0	2.3	3.5	4.5	4.1	3.8	3.4	3.1	2.7
Bilateral (before HIPC completion point)	0.0	0.0	0.0	0.0	0.0	0.0	1.9	3.7	6.3	2.5	2.5	2.5	2.2
Completion point debt relief 2/	…	…	…	…	…	…	…	…	1.4	3.6	3.0	2.6	2.2
Oil signature bonuses	…	…	…	…	…	71.0	71.0	71.0	0.0	0.0	0.0	0.0	0.0
Unidentified revenue measures	…	…	…	…	…	…	…	…	2.0	1.9	1.8	1.7	1.6
Total expenditure and net lending	**79.5**	**66.9**	**75.1**	**85.6**	**15.2**	**33.5**	**54.2**	**76.5**	**72.5**	**67.1**	**64.0**	**60.0**	**56.7**
Current expenditure	**28.9**	**32.2**	**33.2**	**46.5**	**9.1**	**18.4**	**30.2**	**42.7**	**38.2**	**34.1**	**32.6**	**30.7**	**28.8**
Personnel costs	9.6	9.0	9.9	12.0	2.6	5.6	9.9	13.9	12.7	11.9	11.0	10.2	9.4
Financed by Treasury	9.6	9.0	9.9	12.0	2.6	5.6	9.4	13.0	12.7	11.9	11.0	10.2	9.4
Financed by HIPC relief	…	…	…	…	…	…	0.4	0.9	0.0	0.0	0.0	0.0	0.0
Goods and services 3/	4.5	5.5	7.9	15.2	2.0	3.8	5.8	7.8	6.8	6.1	6.1	6.1	6.1
Interest on external debt due	5.6	5.3	4.7	4.8	1.1	2.3	3.4	4.6	4.3	3.7	3.8	3.6	3.4
Interest on internal debt due	0.3	0.0	0.0	0.0	0.1	0.2	0.3	0.3	0.3	0.2	0.2	0.2	0.2
Transfers	3.1	8.4	6.5	10.5	2.8	5.2	8.4	12.4	10.7	9.3	8.7	8.1	7.5
Of which: Regular transfers	3.1	1.9	2.4	6.3	1.7	3.4	5.3	7.5	6.4	5.6	5.2	4.8	4.4
Foreign-funded scholarship program	…	…	0.2	2.2	0.5	0.9	1.4	2.0	1.9	1.7	1.5	1.3	1.2
Domestically-funded scholarship program	…	…	…	1.9	0.7	1.4	2.2	2.9	2.4	2.0	1.8	1.5	1.3
Joint Development Agency 4/	…	6.4	4.1	4.1	1.2	1.8	3.2	4.9	4.3	3.7	3.5	3.3	3.1
Other	5.9	4.1	4.0	4.0	0.5	1.3	2.5	3.7	3.3	3.0	2.8	2.6	2.4
Capital expenditure	46.0	28.8	35.8	35.8	4.9	14.0	21.3	29.3	28.9	28.1	27.2	25.4	24.2
Financed by the treasury	7.0	2.5	6.9	8.0	0.0	1.3	2.3	3.9	3.6	3.3	3.1	3.9	5.0
Financed by external sources	39.1	26.2	29.0	27.7	4.9	12.7	19.1	25.4	25.3	24.8	24.1	21.5	19.3
HIPC Initiative-related social expenditure	4.1	4.6	6.1	4.8	0.5	1.2	2.7	4.5	5.4	4.8	4.3	3.9	3.6
Multilateral	4.1	4.6	6.1	4.8	0.5	1.2	2.7	4.5	4.1	3.8	3.4	3.1	2.7
Bilateral debt relief before completion point	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.3	1.0	0.9	0.8	0.9
Public service restructuring 5/	0.4	1.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net lending	0.0	0.0	0.1	-1.4	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (commitment basis)	**-20.5**	**-16.4**	**-17.0**	**-26.3**	**-6.8**	**62.1**	**57.3**	**51.4**	**-8.6**	**-5.1**	**-5.0**	**-3.9**	**-4.1**
Change in arrears (net; reduction -)	0.9	10.0	5.1	6.5	3.5	-23.5	-23.5	-23.6	0.0	0.0	0.0	0.0	0.0
External arrears 6/	0.9	3.1	1.7	2.2	1.1	-10.5	-10.5	-10.5	0.0	0.0	0.0	0.0	0.0
Domestic arrears	0.0	7.0	3.4	4.3	2.4	-13.0	-13.0	-13.1	0.0	0.0	0.0	0.0	0.0
Of which: Joint Development Agency 4/	…	6.4	4.1	4.1	1.2	-13.0	-13.0	-13.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-19.6**	**-6.4**	**-11.9**	**-19.8**	**-3.3**	**38.6**	**33.9**	**27.7**	**-8.6**	**-5.1**	**-5.0**	**-3.9**	**-4.1**

Table 3. São Tomé and Príncipe: Financial Operations of the Central Government, 2001-10 (concluded)
(In percent of GDP, unless otherwise indicated)

	2001	2002	2003	2004	2005				2006	2007	2008	2009	2010
					Prel.	Proj.	Prog.		Prog.		Proj.		
					Jan.-Mar.	Jan.-Jun.	Jan.-Sep.	Jan-Dec					
Overall fiscal balance (commitment basis)	**-20.5**	**-16.4**	**-17.0**	**-26.3**	**-6.8**	**62.1**	**57.3**	**51.4**	**-8.6**	**-5.1**	**-5.0**	**-3.9**	**-4.1**
Change in arrears (net; reduction -)	0.9	10.0	5.1	6.5	3.5	-23.5	-23.5	-23.6	0.0	0.0	0.0	0.0	0.0
External arrears 6/	0.9	3.1	1.7	2.2	1.1	-10.5	-10.5	-10.5	0.0	0.0	0.0	0.0	0.0
Domestic arrears	0.0	7.0	3.4	4.3	2.4	-13.0	-13.0	-13.1	0.0	0.0	0.0	0.0	0.0
Of which: Joint Development Agency 4/	…	6.4	4.1	4.1	1.2	-13.0	-13.0	-13.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-19.6**	**-6.4**	**-11.9**	**-19.8**	**-3.3**	**38.6**	**33.9**	**27.7**	**-8.6**	**-5.1**	**-5.0**	**-3.9**	**-4.1**
Financing	**19.6**	**6.4**	**11.9**	**19.8**	**3.3**	**-38.6**	**-33.9**	**-27.7**	**8.6**	**5.1**	**5.0**	**3.9**	**4.1**
External (net)	7.6	0.7	4.5	11.5	-2.9	-3.8	-5.8	-5.9	-1.0	-1.4	-1.8	-0.6	-0.9
Disbursements (projects)	10.2	3.6	3.2	5.8	1.4	2.7	4.1	5.4	5.0	4.5	4.1	3.7	3.3
Program financing (loans)	6.1	0.0	5.6	8.0	0.0	1.4	1.4	2.9	6.8	6.2	5.4	5.8	4.7
Short-term loans (Nigeria and Angola) (net) 7/	…	9.2	8.5	9.3	0.0	-1.4	-1.4	-1.4	0.0	0.0	0.0	0.0	0.0
Scheduled amortization (medium and long-term)	-8.7	-12.1	-12.8	-11.6	-4.2	-6.5	-9.9	-12.8	-12.8	-12.2	-11.3	-10.1	-8.9
Domestic (net)	8.4	-0.4	2.9	2.7	1.9	-8.5	-3.7	0.7	-4.2	-6.1	-4.7	-5.9	-4.2
Bank credit (net)	4.1	-0.1	5.4	2.6	3.7	-8.5	-3.7	0.7	-4.2	-6.1	-4.7	-5.9	-4.2
Of which: HIPC Initiative account	-1.0	0.1	-0.7	-1.0	0.5	-1.1	-0.8	0.0	0.0	0.0	0.0	0.0	0.0
Nonbank financing	4.3	-0.3	-2.5	0.1	-1.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Oil reserve fund flows (net) 8/	0.0	0.0	0.0	0.0	0.0	-32.9	-32.9	-32.9	6.0	5.5	5.0	4.4	4.0
Change in arrears (principal)	3.6	6.0	4.5	5.6	4.2	-19.5	-19.5	-19.5	0.0	0.0	0.0	0.0	0.0
Paris Club rescheduling	0.0	0.0	0.0	0.0	0.0	26.2	28.0	29.9	7.7	6.2	5.5	5.1	4.5
Reschedulable arrears 9/	0.0	0.0	0.0	0.0	0.0	26.2	26.2	26.2	0.0	0.0	0.0	0.0	0.0
Debt relief (bilateral-without completion point)	0.0	0.0	0.0	0.0	0.0	0.0	1.9	3.7	6.3	2.5	2.5	2.5	2.2
Completion point debt relief	…	…	…	…	…	…	…	…	1.4	3.6	3.0	2.6	2.2
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	1.0	1.0	0.9	0.8
Memorandum items:													
Pro-poor expenditure (in millions of U.S. dollars)	11.9	10.4	15.8	14.3	…	…	…	20.3	…	…	…	…	…
Pro-poor expenditure (in percent of GDP)	25.0	19.4	26.7	22.2	...	...	...	29.3	...	...	...	...	...
Education	8.6	2.7	6.2	6.1	...	...	...	7.9	...	...	...	...	...
Health	11.4	9.0	10.3	7.8	...	...	...	9.1	...	...	...	...	...
Others	5.0	7.6	10.2	8.2	...	...	...	12.2	...	...	...	...	...
Capital expenditure (in millions of U.S. dollars)	22.0	15.4	21.2	23.0	3.6	10.1	14.8	20.3	21.8	23.4	24.9	26.1	27.8
(Annual percentage changes)	…	-29.9	37.5	8.6	…	…	…	-11.8	7.4	7.2	6.8	4.6	6.6
Domestic primary balance (commitment basis) 10/	**-12.9**	**-4.3**	**-11.7**	**-20.6**	**-4.2**	**-6.1**	**-11.3**	**-17.5**	**-11.9**	**-7.6**	**-5.5**	**-4.5**	**-3.9**
Overall balance (commitment basis, excluding Oil Signature Bonuses)	**-20.5**	**-16.4**	**-17.0**	**-26.3**	**-6.8**	**-8.9**	**-13.6**	**-19.6**	**-8.6**	**-5.1**	**-5.0**	**-3.9**	**-4.1**
External debt service paid	9.8	8.4	11.3	3.1	…	…	…	…	…	…	…	…	…
Non-oil nominal GDP (in billions of dobras)	422.0	486.8	552.6	629.2	…	…	…	745.1	893.7	1,054.0	1,229.6	1,431.0	1,650.9

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.
1/ During 2004-07, includes US$1.4 million in re-exports of oil arising from aid in kind received from Nigeria.
2/ The projections assume that São Tomé and Príncipe reaches HIPC Completion point in the first half of 2006.
3/ In 2004, includes Db20.8 billion (i.e. 3.3 percent of GDP) for hosting the 2004 conference of the Community of Portuguese Language countries (CPLP).
4/ Under the arrangement with Nigeria, São Tomé and Príncipe could defer payments on its 2002-04 contributions to the Joint Development Agency until receipt of the first oil signature bonus.
5/ Severance packages totaling Db 8,000 million were financed by a Structural Adjustment Facility grant from the European Union in 2001-02.
6/ Interest arrears on Paris Club and non-Paris Club bilateral debt.
7/ For 2002-04, includes three US$5 million loans from Nigeria borrowed during 2002-04 and a US$1 million loan from Angola borrowed in 2004. Repayment of the Nigeria loans has been rescheduled until receipt of oil signature bonuses other than on Block 1. The US$1 million from Angola is due to be repaid in 2005.
8/ For 2006-10, drawings from the oil fund are equivalent to 20 percent of the oil permanent fund at end-2004 (in line with the Oil Revenue Management Law).
9/ For 2005, reflects impact of Paris Club rescheduling in the third quarter of 2005.
10/ Excluding the oil revenue including the Nigeria oil grant, non-oil grants, interest earned and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2002-04, it also excludes transfers to the JDA, which are to be repaid with proceeds from the oil signature bonus on Block 1. Includes HIPC Initiative-related social expenditure.

Table 4. São Tomé and Príncipe: Monetary Survey, 2002-05

	2002	2003	2004				2005			
			Mar.	June	Sep.	Dec.	Mar.	June	Sep.	Dec.
						Est.	Prel.	Proj.	Prog.	
	(In billions of dobras; end of period)									
Net foreign assets	264.7	324.7	278.6	289.6	309.6	297.7	249.5	375.7	348.7	323.4
Central bank	194.3	235.1	202.3	207.0	214.2	189.3	171.0	291.4	260.7	226.8
Commercial banks	70.5	89.6	76.2	82.6	95.4	108.5	78.5	84.3	88.0	96.6
Net domestic assets	-69.9	-48.6	-28.7	-20.5	-29.3	-1.2	44.9	-49.7	-19.0	9.6
Net domestic credit	31.1	101.0	124.8	162.5	164.4	212.6	249.1	167.9	210.2	251.4
Net credit to government	-10.5	19.2	32.9	26.3	13.2	35.8	63.3	-27.8	8.4	41.0
Claims	59.2	63.1	63.7	71.1	81.8	83.6	91.6	76.7	85.5	94.7
Deposits	-69.7	-43.9	-30.8	-44.8	-68.6	-47.8	-28.3	-104.5	-77.0	-53.7
Budgetary deposits	-8.1	-18.5	-15.7	-26.7	-25.5	-19.2	-11.6	-17.2	-25.3	-29.4
Of which: HIPC Initiative resources	-3.6	-10.3	-8.2	-9.8	-10.3	-4.2	-0.4	-12.6	-20.7	-25.0
Counterpart funds	-14.5	-13.6	-13.5	-16.2	-18.4	-18.4	-16.5	-16.5	-11.5	-9.0
Foreign currency deposits 1/	-47.1	-11.8	-1.5	-1.9	-24.8	-10.3	-0.3	-70.8	-40.3	-15.4
Credit to the economy	41.6	81.8	91.8	136.1	151.2	176.8	185.8	195.7	201.8	210.4
Other items (net)	-101.0	-149.6	-153.4	-183.0	-193.7	-213.8	-204.2	-217.6	-229.2	-241.8
Broad money (M3)	194.8	276.2	249.9	269.1	280.3	296.5	294.4	326.0	329.7	333.0
Local currency	116.2	158.3	138.9	143.2	159.8	175.8	171.2	191.9	190.3	187.0
Money	104.0	147.1	126.6	128.7	144.1	159.3	154.2	172.9	171.3	168.0
Currency outside banks	39.4	56.4	44.9	43.3	52.7	60.0	50.3	57.2	55.4	51.9
Demand deposits	64.6	90.7	81.7	85.3	91.4	99.3	103.9	115.7	115.9	116.2
Time deposits	12.2	11.2	12.3	14.6	15.6	16.5	17.0	18.9	19.0	19.0
Foreign currency deposits	78.5	117.9	111.0	125.8	120.6	120.7	123.1	134.2	139.5	145.9
	(Changes from the beginning of the year; in billions of dobras)									
Net foreign assets	44.6	60.0	-46.2	-35.1	-15.2	-27.0	-48.2	78.0	51.0	25.7
Net domestic assets	-0.3	21.4	19.9	28.0	19.3	47.4	46.1	-48.5	-17.7	10.8
Net domestic credit	19.0	69.9	23.7	61.4	63.4	111.5	36.5	-44.6	-2.3	38.9
Net credit to government	-0.3	29.7	13.7	7.1	-6.0	16.6	27.5	-63.6	-27.3	5.2
Net claims on other public institutions	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Credit to the economy	18.6	40.2	10.0	54.3	69.4	95.0	9.0	18.9	25.0	33.6
Other items (net)	-19.3	-48.6	-3.8	-33.4	-44.1	-64.2	9.6	-3.8	-15.4	-28.1
Broad money (M3)	41.3	81.4	-26.3	-7.1	4.2	20.3	-2.1	29.5	33.2	36.5
	(Changes in percent of beginning-of-period money stock, unless otherwise specified)									
Net foreign assets	29.1	30.8	-16.7	-12.7	-5.5	-9.8	-16.3	26.3	17.2	8.7
Net domestic assets	-0.2	11.0	7.2	10.2	7.0	17.1	15.5	-16.3	-6.0	3.6
Of which: net credit to government	-0.2	15.3	5.0	2.6	-2.2	6.0	9.3	-21.4	-9.2	1.8
credit to the economy	12.1	20.6	3.6	19.7	25.1	34.4	3.0	6.4	8.4	11.3
credit to the economy (percentage change from beginning of the year)	80.9	96.6	12.3	66.4	84.8	116.1	5.1	10.7	14.1	19.0
Broad money (M3)	26.9	41.8	-9.5	-2.6	1.5	7.4	-0.7	10.0	11.2	12.3
Memorandum items:										
Velocity (ratio of GDP to average broad money)	2.8	2.3	...	...	...	2.2	...	...	...	2.4

Sources: São Tomé and Príncipe authorities; and staff estimates and projections.
1/ Includes drawings from the oil signature bonuses to finance the budget and disbursements under expected PRGF arrangement.

Table 5. São Tomé and Príncipe: Summary Accounts of the Central Bank, 2002-05

(In billions of dobras, end of period)

	2002	2003	2004				2005			
			Mar.	June	Sep.	Dec.	Mar.	June	Sep.	Dec.
						Est.	Prel.	Proj.	Prog.	
Net foreign assets	194.3	235.1	202.3	207.0	214.2	189.3	171.0	291.4	260.7	226.8
Gross reserves 1/	159.5	240.6	232.1	206.7	221.0	197.1	190.1	301.0	277.8	252.0
of which: guarantee deposits	0.0	25.6	50.5	21.1	18.7	17.9	30.0	31.7	32.9	34.2
Short-term liabilities 1/	0.0	-25.6	-50.5	-21.1	-28.6	-27.9	-40.0	-31.7	-40.1	-49.0
Other foreign assets	58.3	46.5	47.6	48.9	49.8	49.5	49.6	52.4	54.5	56.5
Other liabilities	-23.5	-26.4	-26.9	-27.5	-28.0	-29.4	-28.7	-30.3	-31.5	-32.7
Net domestic assets	-82.4	-76.4	-61.3	-72.3	-88.7	-70.0	-33.7	-134.9	-107.1	-82.9
Net domestic credit	-5.4	29.4	44.0	38.7	26.6	54.7	79.8	-11.3	24.9	57.5
Net credit to government	-7.1	23.8	38.3	32.1	18.8	42.6	67.6	-23.5	12.7	45.3
Claims	59.2	63.1	63.7	71.1	81.8	83.6	91.6	76.7	85.5	94.7
Of which: use of SDRs/Poverty Reduction and Growth Facility	31.1	35.0	35.6	36.5	37.2	38.9	38.1	40.2	48.9	58.2
Deposits	-66.3	-39.2	-25.4	-39.0	-63.0	-41.0	-24.0	-100.2	-72.7	-49.4
Ordinary	-6.8	-16.0	-12.5	-23.1	-22.0	-14.5	-7.3	-12.9	-21.0	-25.1
Of which: HIPC Initiative resources	-3.6	-10.3	-8.2	-9.8	-10.3	-4.2	-0.4	-12.6	-20.7	-25.0
Bank liquidation (CNPC; net of claims)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Counterpart funds	-12.4	-11.5	-11.4	-14.1	-16.2	-16.2	-16.5	-16.5	-11.5	-9.0
Foreign currency 2/	-47.1	-11.8	-1.5	-1.9	-24.8	-10.3	-0.3	-70.8	-40.3	-15.4
Rediscount to commercial banks	1.7	1.1	1.1	1.2	1.2	5.2	5.2	5.2	5.2	5.2
Other claims	0.0	4.4	4.6	5.4	6.7	6.9	7.0	7.0	7.0	7.0
Other items (net)	-76.9	-105.8	-105.3	-111.0	-115.3	-124.7	-113.5	-123.6	-132.0	-140.3
Base money	111.9	158.7	141.0	134.7	125.5	119.2	137.3	156.5	153.6	143.9
Currency issued	45.7	63.1	51.6	49.4	56.6	67.2	54.2	61.1	59.3	56.9
Bank reserves	66.1	95.6	89.4	85.3	68.9	52.1	83.0	95.3	94.3	87.1
Memorandum Items:										
Gross reserves (in US$ millions) 1/	17.3	25.7	24.2	21.0	22.0	19.8	19.0	28.5	25.3	22.1
of which: excluding guarantee deposits	17.3	23.0	18.9	18.8	20.1	18.0	16.0	25.5	22.3	19.1
Permanent Oil Fund (in US$ millions) 3/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	22.8	23.0	23.1

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

1/ Includes guarantee deposits by prospective financial institutions pending operating licenses.

2/ Includes drawings from the oil signature bonuses to finance the budget and disbursements under expected PRGF arrangement.

3/ Not included in gross international reserves of BCSTP.

Table 6. São Tomé and Príncipe: Balance of Payments, 2001–10

(In millions of U.S. dollars, unless otherwise specified)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
				Est.		Prog.			Proj.	
Current account balance, excluding official transfers	-30.1	-28.9	-32.2	-39.6	-41.8	-45.5	-52.3	-59.4	-64.7	-67.4
Of which : non-oil current account balance 1/	-30.1	-28.9	-32.4	-41.0	-39.2	-40.2	-41.8	-42.8	-43.7	-46.4
Trade balance	-20.7	-23.4	-27.3	-29.5	-30.7	-33.3	-37.9	-44.0	-48.7	-53.9
Exports, f.o.b.	3.7	5.1	6.0	6.9	7.3	7.3	7.3	6.0	6.1	6.4
Non-oil exports	3.7	5.1	5.9	5.5	5.9	5.9	5.9	6.0	6.1	6.4
Of which : cocoa	3.3	4.6	5.5	5.3	5.7	5.7	5.7	5.7	5.7	5.6
Oil re-exports 2/	0.0	0.0	0.1	1.4	1.4	1.4	1.4	0.0	0.0	0.0
Imports, f.o.b.	-24.4	-28.5	-33.4	-36.4	-38.0	-40.6	-45.2	-50.1	-54.8	-60.3
Food	-7.7	-9.2	-12.0	-13.1	-13.4	-13.6	-13.9	-14.3	-14.2	-15.2
Investment goods	-11.4	-13.6	-14.1	-14.9	-13.6	-15.4	-16.5	-18.2	-21.4	-23.7
Oil sector-related investment goods	0.0	0.0	0.0	0.0	-1.3	-2.2	-3.8	-5.4	-6.8	-6.8
Petroleum products	-4.1	-4.3	-3.8	-5.1	-6.2	-5.4	-6.2	-6.9	-6.0	-7.2
Other	-1.2	-1.3	-3.5	-3.3	-3.6	-4.0	-4.7	-5.3	-6.3	-7.5
Services and income (net)	-10.0	-6.2	-6.7	-9.9	-12.6	-15.2	-18.4	-19.5	-20.8	-19.0
Exports of nonfactor services	11.9	14.5	16.5	18.2	20.0	21.9	24.4	27.1	29.4	32.5
Of which : travel and tourism	8.4	10.4	11.6	12.5	13.4	14.4	15.5	16.7	17.9	19.3
Imports of nonfactor services	-19.2	-17.9	-20.4	-25.0	-29.7	-34.4	-40.2	-43.6	-46.6	-47.5
Freight and insurance	-5.1	-6.1	-6.7	-7.3	-7.6	-8.1	-9.0	-10.0	-11.0	-12.1
Technical assistance	-9.9	-7.5	-8.2	-9.1	-9.8	-11.7	-11.7	-10.1	-9.8	-9.8
Oil sector-related services 3/	0.0	0.0	0.0	0.0	-2.4	-4.1	-7.2	-10.1	-12.7	-12.7
Other	-4.2	-4.3	-5.5	-8.7	-9.9	-10.5	-12.3	-13.4	-13.2	-12.9
Factor services (net)	-2.7	-2.8	-2.8	-3.1	-2.8	-2.6	-2.6	-3.1	-3.6	-4.0
Interest due	-2.7	-2.8	-2.8	-3.1	-3.2	-3.3	-3.1	-3.4	-3.9	-4.1
Permanent oil fund interest earnings	0.0	0.0	0.0	0.0	0.3	0.6	0.5	0.4	0.3	0.1
Private transfers (net)	0.6	0.8	1.8	-0.2	1.5	2.9	3.9	4.1	4.7	5.5
Official transfers (net)	18.0	15.7	20.3	22.0	22.2	27.8	28.5	28.8	29.2	28.5
Of which : Public investment projects	13.8	12.1	15.2	14.1	13.9	15.4	16.9	18.4	18.4	18.4
Nonproject grants	2.0	0.1	0.4	3.5	1.4	2.2	2.2	1.0	1.3	0.6
HIPC Initiative-related grants	2.3	2.3	3.4	3.1	5.7	8.9	8.2	8.2	8.3	8.3
Multilateral	2.3	2.3	3.4	3.1	3.1	3.1	3.1	3.1	3.1	3.1
Bilateral	0.0	0.0	0.0	0.0	2.6	5.8	5.0	5.0	5.2	5.1
Current account balance, including official transfers	-12.1	-13.2	-12.0	-17.6	-19.5	-17.8	-23.8	-30.6	-35.6	-38.9
Of which : non-oil current account balance 1/	-12.1	-13.2	-12.1	-19.0	-17.0	-12.4	-13.3	-14.0	-14.6	-17.9
Capital account balance	7.9	2.0	4.0	9.1	38.7	5.1	12.1	21.0	28.0	30.7
Medium- and long-term capital (net)	7.0	-1.0	1.1	4.9	53.5	10.5	17.5	23.8	31.6	32.0
Project loans	4.9	2.0	1.9	3.8	3.8	3.8	3.8	3.8	3.8	3.8
Program loans	2.9	0.0	3.3	5.1	2.0	5.2	5.2	5.0	6.0	5.4
Oil signature bonuses	0.0	0.0	0.0	0.0	49.2	0.0	0.0	0.0	0.0	0.0
Direct foreign investment	3.3	3.6	3.4	3.5	8.5	11.9	19.4	25.4	31.7	32.7
Of which : petroleum-related investment	0.0	0.0	0.0	0.0	4.5	6.8	12.0	16.8	21.2	21.2
Other investment	0.0	0.0	0.0	0.0	-1.1	-0.7	-0.7	-0.1	0.6	0.4
Of which : Use of Fund resources (PRGF)	0.0	0.0	0.0	0.0	-1.1	-0.7	-0.7	-0.1	0.6	0.4
Amortization	-4.1	-6.5	-7.6	-7.5	-8.9	-9.6	-10.1	-10.4	-10.4	-10.2
Short-term capital	0.9	3.0	3.0	4.1	-14.7	-5.3	-5.4	-2.8	-3.7	-1.3
Of which : Nigerian and Angola advances	0.0	5.0	5.0	6.0	0.0	0.0	0.0	0.0	0.0	0.0
Scheduled repayment of Nigeria and Angola advances	0.0	0.0	0.0	0.0	-16.0	0.0	0.0	0.0	0.0	0.0
Rescheduling of Nigeria advances			….	…	15.0	…	….	…	…	…
Transfers to Joint Development Agency			….	…	-12.7	-3.2	-3.1	-3.2	-3.4	-3.6
Errors and Ommissions	4.7	8.7	9.8	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	0.5	-2.4	1.8	-9.5	19.2	-12.6	-11.8	-9.6	-7.6	-8.2

Table 6. São Tomé and Príncipe: Balance of Payments, 2001-10 (concluded)

(In millions of U.S. dollars, unless otherwise specified)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
				Est.	Prog.			Proj.		
Overall balance	0.5	-2.4	1.8	-9.5	19.2	-12.6	-11.8	-9.6	-7.6	-8.2
Financing	-0.5	2.4	-1.8	9.5	-19.2	12.7	11.8	9.6	7.6	8.2
Change in net international reserves (increase -)	-2.6	-2.4	-5.9	4.5	-3.0	1.5	0.5	-1.0	-2.5	-2.0
Use of Fund resources (PRGF)	0.0	0.0	0.0	0.0	1.1	0.7	0.7	0.1	-0.6	-0.4
Permanent oil fund (increase -)	0.0	0.0	0.0	0.0	-22.8	4.6	4.6	4.6	4.6	4.6
Medium- and long-term arrears (net; decrease -) 4/	2.1	4.9	4.0	5.0	-15.3	0.0	0.0	0.0	0.0	0.0
Debt relief (HIPC bilateral) 5/	0.0	0.0	0.0	0.0	2.6	5.8	5.1	5.1	5.2	5.1
Financing gap	0.0	0.0	0.0	0.0	18.1	0.1	0.9	0.9	0.9	0.9
Reschedulable arrears	0.0	0.0	0.0	0.0	18.1	0.0	0.0	0.0	0.0	0.0
Residual financing gap	0.0	0.0	0.0	0.0	0.0	0.1	0.9	0.9	0.9	0.9
Memorandum items:										
Cocoa export volume (in thousands of metric tons)	3.0	3.1	3.5	3.7	3.7	3.7	3.7	3.7	3.7	3.7
Cocoa export unit value (in U.S. dollars per kilogram)	0.93	1.46	1.57	1.42	1.54	1.54	1.53	1.53	1.52	1.52
Exchange rate (in dobras per U.S. dollars; average)	8,842	9,088	9,348	9,780	...	...	...	...	...	...
GDP (in billions of dobras)	422.0	486.8	552.6	629.2	745.1	893.7	1,054.0	1,229.6	1,431.0	1,650.9
Debt-service ratio (before debt relief) 6/ 7/	41.3	60.8	58.0	50.6	56.7	51.9	49.6	48.9	46.1	42.6
Debt-service ratio (after debt relief, and assuming HIPC Completion point in 2006) 6/ 7/	41.3	60.8	58.0	50.6	32.6	27.6	11.5	12.3	11.9	11.0
Debt service paid 6/ 7/ 8/	23.9	20.0	25.4	…	...	...	...	...	...	...
Current account balance, including official transfers (in percent of GDP)	-25.3	-24.6	-20.2	-27.3	-28.2	-23.5	-28.7	-33.3	-34.6	-33.9
Non-oil current account balance, including official transfers (in percent of non-oil GDP) 2/	-25.3	-24.6	-20.4	-29.5	-24.5	-16.4	-16.1	-15.2	-14.2	-15.6
Current account balance, excluding official transfers (in percent of GDP)	-63.2	-54.0	-54.5	-61.5	-60.3	-60.3	-63.1	-64.7	-63.1	-58.7
Non-oil current account balance, excluding official transfers (in percent of GDP) 3/	-63.2	-54.0	-54.7	-63.7	-56.6	-53.2	-50.4	-46.6	-42.6	-40.4
Gross reserves (in months of following year's non-oil imports of goods and nonfactor services) 9/	4.0	3.9	4.5	3.4	3.4	3.5	3.5	3.5	3.5	3.5

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

1/ Excluding oil re-export from Nigeria grant, c.i.f. imports of oil sector-related goods and services, and oil sector profit remittances.
2/ During 2004-07, includes US$1.4 million in re-exports of oil arising from aid in kind received from Nigeria.
3/ Covers external payments for services by petrol companies during the course of petroleum exploration.
4/ For 2005 assumes a new Paris Club rescheduling agreement.
5/ São Tomé and Príncipe is assumed to reach HIPC completion point in the first half of 2006.
6/ In percent of exports of goods and nonfactor services, calculated as a three-year backward-looking average (e.g., average over 2001-03 for exports in 2003).
7/ Includes obligations to the IMF; excludes arrears.
8/ Excludes HIPC interim assistance.
9/ Excluding guarantee deposits placed at the central bank by prospective financial institutions pending operating licenses.

Table 7. São Tomé and Príncipe: Millennium Development Goals

	1990	1995	2001	2002
Goal 1. Eradicate extreme poverty and hunger				
Target 1: Halve between 1990 and 2015, the proportion of people whose income is less than one dollar a day.				
1. Population below US$ 1 a day (percent)	..	..	..	..
2. Poverty gap ratio at US$ 1 a day (percent)	..	..	..	..
3. Share of income or consumption held by poorest 20 percent (percent)	..	…	..	..
Target 2: Halve, between 1990 and 2015, the proportion of people suffering hunger				
4. Prevalence of child malnutrition (percent of children under 5)	..	..	12.9	..
5. Population below minimum level of dietary energy consumption (percent)	..	..	..	..
Goal 2. Achieve universal primary education				
Target 3: Ensure that, by 2015, children will be able to complete a full course of primary schooling				
6. Net primary enrollment ratio (percent of relevant age group)	..	..	97.1	..
7. Percentage of cohort reaching grade 5	..	..	61.5	..
8. Youth literacy rate (percent age 15-24)	..	..	..	..
Goal 3. Promote gender equality and empower women				
Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education by 2015				
9. Ratio of girls to boys in primary and secondary education (percent)	..	..	92.1	..
10. Ratio of young literate females to males (percent ages 15-24)	..	..	..	..
11. Share of women employed in the nonagricultural sector (percent)	..	..	..	..
12. Proportion of seats held by women in the national parliament (percent)	..	7.0	..	..
Goal 4. Reduce child mortality				
Target 5: reduce by two-thirds between 1990 and 2015, the under-five mortality rate				
13. Under-five mortality rate (per 1,000)	…	…	…	118.0
14. Infant mortality rate (per 1,000 live births)	…	…	…	75.0
15. Immunization against measles (percent of children under 12-months)	71.0	74.0	75.0	85.0
Goal 5. Improve maternal health				
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.				
16. Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	…	..	..
17. Proportion of births attended by skilled health personnel	..	…	78.6	..
Goal 6. Combat HIV/AIDS, malaria and other diseases				
Target 7: Halt by 2015, and begin to reverse, the spread of HIV/AIDS				
18. HIV prevalence among females (percent ages 15-24)	..	..	…	..
19. Contraceptive prevalence rate (percent of women ages 15-49)	..	..	..	..
20. Number of children orphaned by HIV/AIDS	..	..	…	..
Target 8: Halt by 2015, and begin to reverse, the incidence of malaria and other major diseases				
21. Prevalence of death associated with malaria	..	..	..	..
22. Share of population in malaria risk areas using effective prevention and treatment	..	..	..	..
23. Incidence of tuberculosis (per 100,000 people)	..	..	132.0	130.0
24. Tuberculosis cases detected under DOTS (percent)	..	..	…	..

Table 7. São Tomé and Príncipe: Millennium Development Goals (concluded)

	1990	1995	2001	2002
Goal 7. Ensure environmental sustainability				
Target 9: Integrate the principles of sustainable development into policies and programs. Reverse the loss of environmental resources				
25. Forest area (percent of total land area)	28.1	..	28.1	..
26. Nationally protected areas (percent of total land area)	..	0.0	0.0	..
27. GDP per unit of energy use (PPP $ per kg oil equivalent)	..	..	..	..
28. CO2 emissions (metric tons per capita)	0.6	0.6	0.6	..
29. Proportion of population using solid fuels	..	..	..	..
Target 10: Halve by 2015 proportion of people without access to safe drinking water				
30. Access to improved water source (percent of population)	..	..	…	..
Target 11: Achieve by 2020 significant improvement for at least 100 million slum dwellers				
31. Access to improved sanitation (percent of population)	44.0	..	56.0	..
32. Access to secure tenure (percent of population)	..	..	..	..
Goal 8. Develop a Global Partnership for Development 2/				
Target 16: Develop and implement strategies for productive work for youth.				
45. Unemployment rate of population ages 15-24 (total)				
Female	..	..	..	..
Male	..	..	..	..
Target 17: Provide access to affordable essential drugs				
46. Proportion of population access with access to affordable essential drugs	..	..	..	..
Target 18: Make available new technologies, especially information and communications				
47. Fixed line and mobile telephones (per 1,000 people)	19.2	19.7	36.3	54.4
48. Personal computers (per 1,000 people)	..	..	..	..

Sources: World Bank; and Fund staff estimates.

1/ Targets 33-44 are excluded because they can not be measured on a country specific basis. These are related to official development assistance, market access, and the HIPC initiative.

Table 8. São Tomé and Príncipe: External Financing Requirements and Sources, 2005-07

(In millions of U.S. dollars, unless otherwise specified)

	2005	2006	2007
		Prog.	
1. Gross financing requirements	**-76.4**	**-48.4**	**-49.1**
Current account, excluding current official	-41.8	-45.5	-52.3
Exports, f.o.b. 1/	7.3	7.3	7.3
Imports, f.o.b.	-38.0	-40.6	-45.2
Services and income (net)	-12.6	-15.2	-18.4
Private transfers	1.5	2.9	3.9
Capital account	-16.4	-4.4	2.7
Scheduled amortization	-8.9	-9.6	-10.1
IMF repayments	-0.2	-0.6	-0.6
Other capital (net)	-7.4	5.9	13.4
Change in arrears (net)	-15.3	0.0	0.0
2. Available Funding	**76.4**	**48.4**	**49.1**
Oil Fund (net)	26.4	4.6	4.6
Oil signature bonuses	49.2	0.0	0.0
Saving (accumulation of oil reserve fund -)	-22.8	4.6	4.6
Expected disbursements	30.6	42.5	42.5
HIPC Initiative-related grants 2/	5.7	8.9	8.2
Grants 1/	19.1	24.6	25.4
Concessional loans	5.8	8.9	8.9
Project loans	3.8	3.8	3.8
Program loans	2.0	5.2	5.2
IMF 3/	1.3	1.3	1.3
Financing gap	18.1	0.1	0.9
Reschedulable arrears 4/	18.1	0.0	0.0
Residual financing gap (actual debt service)	0.0	0.1	0.9

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

1/ Includes US$1.4 million in re-exports of oil arising from aid in kind received from Nigeria.
2/ Savings from assistance under the HIPC Initiative. Assumes that São Tomé and Principé reaches HIPC completion point in the first half of 2006.
3/ Includes projected disbursements under new PRGF.
4/ For 2005, assumes Paris Club rescheduling agreement on Cologne terms in the third quarter of 2005, and comparable treatment by non-Paris Club creditors.

Table 9. São Tomé and Príncipe: Net Present Value (NPV) of External Debt and Debt Service Due, 1999-2010 1/
(Assuming Paris Club debt rescheduling on Cologne terms in 2005 and HIPC Completion Point by mid-2006)

(In millions of U.S. dollars, unless otherwise indicated)

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
						Est.	Projections					
NPV of total debt 2/	230.9	75.2	77.4	86.5	96.0	100.6	116.2	97.3	110.4	122.6	133.4	144.2
NPV of outstanding debt	230.9	75.2	77.4	86.5	96.0	100.6	103.8	72.5	73.0	73.6	73.9	74.0
Multilateral 3/	109.6	32.8	33.5	37.7	42.2	41.3	42.2	42.4	42.5	42.5	42.3	41.7
Official bilateral 4/	121.3	42.4	44.0	48.8	53.9	59.3	61.6	30.0	30.5	31.1	31.6	32.3
Paris Club 5/	82.9	31.5	32.7	34.0	35.3	36.5	37.8	14.6	14.4	14.1	13.9	13.7
Other official bilateral 6/	38.4	10.9	11.3	14.8	18.6	22.8	23.8	15.4	16.1	16.9	17.7	18.6
NPV of new borrowing 7/	0.0	0.0	0.0	0.0	0.0	0.0	12.4	24.8	37.4	48.9	59.5	70.2
Total debt service due 8/	...	4.6	2.4	2.4	2.0	2.0	2.9	2.4	3.5	3.6	4.0	4.4
Multilateral 3/ 8/	...	4.1	1.9	1.9	1.4	1.5	1.2	1.8	2.1	2.1	2.4	2.7
Official bilateral 4/	...	0.5	0.5	0.5	0.5	0.6	1.6	0.3	1.0	1.0	1.0	1.0
Paris Club 5/	...	0.2	0.3	0.4	0.4	0.4	0.5	0.3	1.0	0.9	0.9	0.9
Other official bilateral 6/	...	0.3	0.1	0.1	0.1	0.1	1.1	0.0	0.0	0.0	0.0	0.0
New borrowing	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.3	0.4	0.5	0.7	0.8
Memorandum items:												
Exports of goods and nonfactor services	16.5	15.5	15.5	19.6	22.6	25.1	27.3	29.2	31.7	33.2	35.6	38.9
Three-year export average 9/	13.6	14.6	15.8	16.9	19.2	22.4	25.0	27.2	29.4	31.4	33.5	35.9
Government revenues (excl. grants)	9.1	10.0	10.2	12.5	15.1	18.3	18.7	22.8	25.1	26.2	29.1	32.6
GDP	46.9	46.3	47.7	53.6	59.1	64.3	68.2	74.3	81.6	90.4	100.9	112.9
NPV of debt-to-exports ratio (in percent) 9/												
For total debt	...	513.2	489.2	512.7	499.2	449.0	465.3	358.1	375.6	390.8	398.5	401.9
For outstanding debt only	...	513.2	489.2	512.7	499.2	449.0	415.6	266.7	248.4	234.7	220.8	206.3
NPV of debt-to-revenue ratio (in percent) 10/												
For total debt	...	750.6	755.9	693.2	634.2	550.6	619.7	427.3	440.6	468.5	458.0	442.8
For outstanding debt only	...	750.6	755.9	693.2	634.2	550.6	553.6	318.3	291.4	281.4	253.7	227.3
Debt-service ratio (current year)	...	31.0	42.1	52.4	49.5	45.3	29.9	25.6	10.6	11.7	11.2	10.2
Debt-service ratio (three-year average) 9/	...	32.8	41.3	60.8	58.0	50.6	32.6	27.6	11.5	12.3	11.9	11.0
Debt-service-to-revenue ratio	...	48.0	63.8	82.2	73.7	62.1	43.5	32.9	13.5	14.8	13.7	12.2

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

1/ Existing debt is as of end-December 2004. Refers to public and publicly guaranteed debt only, and includes short-term debt ineligible for treatment under the HIPC Initiative. The end-1999 debt stock has been updated to include loans totalling US$27 million from the IDA, AfDB/AfDF, the EU, Italy, and France for which full information were not available at the time of the HIPC decision point debt sustainability analysis (DSA).

2/ Discounted on the basis of the average commercial interest reference rate for the respective currency for the second half of 2004. Conversion of currency-specific NPVs into U.S. dollars is made at end-December 2004 exchange rate. 1999 NPV based on assumption of no further debt relief beyond 2000 rescheduling.

3/ Projected and not fully reconciled. IDA and European Investment Bank (EIB) have provided HIPC Initiative interim assistance on 100 percent of debt service 2001, while AfDB/AfDF has been providing HIPC Initiative interim assistance on 83 percent of debt service since 2001. IDA, EIB and AfDB/AfDB are assumed to continue providing assistance through end-2005; the International Fund for Agricultural Development (IFAD) and the Arab Bank for Economic Development in Africa (BADEA) do not provide any HIPC Initiative interim assistance. OPEC has been providing HIPC Initiative interim assistance since March 2003.

4/ Projected and not fully reconciled. Assumes the conclusion, in the second haf of 2005, of a new rescheduling of Paris Club and non-Paris Club debt with São Tomé and Príncipe on Cologne terms, retroactive since HIPC decision point (December 2000).

5/ Debt to Italy has been under discussion since the 2000 HIPC Initiative decision point, and it is assumed that this debt will benefit from treatment similar to that provided by the other Paris Club creditors, including HIPC treatment, once the Italian authorities have resolved an internal dispute with the Italian export agency, and an agreement on this debt is reached with São Tomé and Príncipe.

6/ Includes three interest-free US$5 million advances from Nigeria in 2002, 2003, and 2004, and a US$ 1 million loan from Angola in 2005. It is assumed that the advances from Nigeria would be repaid in 2012. The US$1 million loan from Angola will be repaid in 2005.

7/ Projected from 2005. Also includes known estimated and projected disbursements by IDA and AfDB/AfDF; additional projected external disbursements are assumed to be provided on IDA and OPEC terms with no implied assumption regarding their source.

8/ Including interim assistance provided under the HIPC Initiative, and assuming Paris Club and non-Paris Club rescheduling on Cologne terms, retrospective since HIPC decision point (December 2000).

9/ Exports of goods and nonfactor services are calculated as a three-year backward-looking average (e.g., average over 2001-03 for exports in 2003).

10/ NPV of total debt in percent of government revenue.

Table 10. São Tomé and Príncipe: Net Present Value (NPV) of External Debt and Debt Service Due, 1999–2010 1/
(Assuming no further debt relief beyond 2000 Paris Club debt rescheduling)

(In millions of U.S. dollars, unless otherwise indicated)

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
						Est.	Projections					
NPV of total debt 2/	230.9	184.0	190.1	192.7	197.1	201.6	208.9	215.3	221.4	225.7	228.9	232.2
NPV of outstanding debt	230.9	184.0	190.1	192.7	197.1	201.6	197.9	193.3	188.2	182.1	175.9	169.5
Multilateral 3/	109.6	110.9	112.6	113.3	115.9	116.5	115.2	113.2	110.6	107.2	103.6	100.0
Official bilateral 4/	121.3	68.1	69.3	70.8	72.2	74.0	71.4	68.7	66.0	63.3	60.5	57.7
Paris Club 5/	82.9	48.1	48.7	46.8	44.8	42.8	40.8	38.8	36.7	34.7	32.7	30.5
Other official bilateral 6/	38.4	20.0	20.6	24.0	27.4	31.1	30.5	29.9	29.3	28.6	27.8	27.2
NPV of new borrowing 7/	0.0	0.0	0.0	0.0	0.0	0.0	11.0	22.0	33.2	43.6	53.1	62.7
Total debt service due 8/	...	4.8	6.5	10.3	11.2	11.3	12.1	13.3	13.6	14.2	14.7	14.7
Multilateral 3/ 8/	...	3.9	4.4	5.4	6.0	6.2	6.2	7.1	7.6	8.5	8.5	8.5
Official bilateral 4/	...	0.9	2.1	4.9	5.2	5.1	5.8	6.0	5.6	5.1	5.5	5.4
Paris Club 5/	...	0.4	1.7	4.3	4.2	4.1	3.3	3.9	3.6	3.2	3.4	3.4
Other official bilateral 6/	...	0.5	0.5	0.6	1.0	1.0	2.6	2.1	2.0	1.9	2.0	1.9
New borrowing	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.3	0.4	0.5	0.7	0.8
Memorandum items:												
Exports of goods and nonfactor services	16.5	15.5	15.5	19.6	22.6	25.1	27.3	29.2	31.7	33.2	35.6	38.9
Three-year export average 9/	13.6	14.6	15.8	16.9	19.2	22.4	25.0	27.2	29.4	31.4	33.5	35.9
Government revenues (excl. grants)	9.1	10.0	10.2	12.5	15.1	18.3	18.7	22.8	25.1	26.2	29.1	32.6
GDP	46.9	46.3	47.7	53.6	59.1	64.3	68.2	74.3	81.6	90.4	100.9	112.9
NPV of debt-to-exports ratio (in percent) 9/												
For total debt	...	1,256.4	1,200.9	1,142.5	1,024.5	899.7	836.8	792.5	753.0	719.6	683.7	647.5
For outstanding debt only	...	1,256.4	1,200.9	1,142.5	1,024.5	899.7	792.9	711.5	640.0	580.7	525.2	472.7
NPV of debt-to-revenue ratio (in percent) 10/												
For total debt	...	1,837.5	1,855.6	1,544.7	1,301.6	1,103.4	1,114.4	945.7	883.3	862.7	785.7	713.4
For outstanding debt only	...	1,837.5	1,855.6	1,544.7	1,301.6	1,103.4	1,056.0	849.1	750.8	696.2	603.6	520.8
Debt-service-to-export ratio (current year)	...	31.0	42.1	52.4	49.5	45.3	51.5	47.6	45.1	45.1	42.0	37.9
Debt-service-to-export ratio (three-year average) 9/	...	32.8	41.3	60.8	58.0	50.6	56.3	51.2	48.7	47.7	44.6	41.0
Debt-service-to-revenue ratio	...	48.0	63.8	82.2	73.7	62.1	75.0	61.1	57.1	57.2	51.3	45.2

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

1/ Existing debt is as of end-December 2004. Refers to public and publicly guaranteed debt only, and includes short-term debt ineligible for treatment under the HIPC Initiative. The end-1999 debt stock has been updated to include loans totalling US$27 million from the IDA, AfDB/AfDF, the EU, Italy, and France for which full information were not available at the time of the HIPC decision point debt sustainability analysis (DSA).

2/ Discounted on the basis of the average commercial interest reference rate for the respective currency for the second half of 2004. Conversion of currency-specific NPVs into U.S. dollars is made at the end-December 2004 exchange rate.

3/ Projected and not fully reconciled. IDA and European Investment Bank (EIB) have provided HIPC Initiative interim assistance on 100 percent of debt service since 2001, while AfDB/AfDF has been providing HIPC Initiative interim assistance on 83 percent of debt service since 2001. IDA, EIB and AfDB/AfDB are assumed to continue providing assistance through end-2005; the International Fund for Agricultural Development (IFAD) and Arab Bank for Economic Development in Africa (BADEA) do not provide any HIPC Initiative interim assistance. OPEC has been providing HIPC Initiative interim assistance since March 2003.

4/ Projected and not fully reconciled. All arrears on eligible outstanding debt to Paris Club creditors at end-March 2000 and on current maturities from April 2000-April 2003 were rescheduled on Naples terms on May 16, 2000; the first phase of the rescheduling was for April 1, 2000-April 30, 2001, while the second and third phases were inoperative. Consequently, the assistance planned under the second and third phases is assumed to have accrued as arrears for May 2001-March 2003. Non-Paris Club creditors are assumed to provide similar treatment.

5/ Debt to Italy has been under discussion since the 2000 HIPC Initiative decision point, and it is assumed that this debt will benefit from treatment similar to that provided by the other Paris Club creditors, including HIPC treatement, once the Italian authorities have resolved an internal dispute with the Italian export agency, and an agreement on this debt is reached with São Tomé and Príncipe.

6/ Includes three interest-free US$5 million advances from Nigeria in 2002, 2003, and 2004, and a US$1 million loan from Angola in 2005. It is assumed that the advances from Nigeria would be repaid in 2012. The US$1 million loan from Angola will be repaid in 2005.

7/ Projected from 2005. Also includes known estimated and projected disbursements by IDA and AfDB/AfDF; additional projected external disbursements are assumed to be provided on IDA and OPEC terms with no implied assumption regarding their source.

8/ Excluding interim assistance provided under the HIPC Initiative.

9/ Exports of goods and nonfactor services are calculated as a three-year backward-looking average (e.g., average over 2001–03 for exports in 2003).

10/ NPV of total debt in percent of government revenue.

Table 11. São Tomé and Príncipe: Schedule of Disbursements Under the Proposed PRGF Arrangement, 2005-2008

SDR Millions	Percent of Quota	Date available	Disbursement conditions
0.423	5.7	Aug-2005	Board approval of arrangement
0.423	5.7	Dec-2005	Observance of PCs for end-September 2005 and completion of review
0.423	5.7	Apr-2006	Observance of PCs for end-December 2005 and completion of review
0.423	5.7	Nov-2006	Observance of PCs for end-June 2006 and completion of review
0.423	5.7	Apr-2007	Observance of PCs for end-December 2006 and completion of review
0.423	5.7	Nov-2007	Observance of PCs for end-June 2007 and completion of review
0.422	5.7	Mar-2008	Observance of PCs for end-December 2007 and completion of review

Table 12. São Tomé and Príncipe: Indicators of Fund Credit, 2004–09

(In millions of SDRs, unless otherwise indicated)

	2004	2005	2006	2007	2008	2009
		Projections				
Fund credit outstanding 1/						
In millions of SDRs	1.90	2.65	3.12	3.58	3.63	3.25
In millions of U.S. dollars	2.87	4.09	4.81	5.53	5.59	5.00
In percent of quota	25.70	35.85	42.14	48.43	49.00	43.86
Fund obligations						
Fund total charges and interest	0.00	0.03	0.03	0.03	0.03	0.03
Existing drawings	0.00	0.03	0.02	0.02	0.02	0.02
Prospective drawings	-	0.00	0.01	0.01	0.01	0.01
Fund total repayment/repurchases	-	0.10	0.38	0.38	0.38	0.38
Existing drawings	-	0.10	0.38	0.38	0.38	0.38
Prospective drawings	-	-	-	-	-	-
Fund credit in percent of						
Export of goods and nonfactor services	11.46	15.00	16.48	17.43	16.86	14.06
Gross official reserves	16.19	21.40	22.55	24.52	23.67	19.58
		0.00	0.00	0.00	0.00	
Memorandum items:						
Export of goods and nonfactor services (In millions of US dollars)	25.05	27.27	29.19	31.73	33.17	35.55
Gross official reserves (In millions of US dollars)	17.73	19.12	21.33	22.55	23.62	25.53

Sources: Fund staff estimates; and projections

1/ Includes the prospective disbursements under the Poverty Reduction and Growth Facility arrangement for a total of SDR2.96 million (40 percent of quota).

São Tomé and Príncipe: Relations With The Fund
(As of March 31, 2005)

I. **Membership Status**: Joined 09/30/1977; Article XIV

II. **General Resources Account**:	SDR million	Percent Quota
Quota	7.40	100.00
Fund holdings of currency	7.40	100.05

III. **SDR Department**:	SDR million	Percent Allocation
Net cumulative allocation	0.62	100.00
Holdings	0.00	1.63

IV. **Outstanding Purchases and Loans**:	SDR million	Percent Quota
Poverty Reduction and Growth Facility (PRGF) arrangements	1.90	25.70

V. **Financial Arrangements**:

Type	Approval date	Expiration date	Amount approved (SDR million)	Amount drawn (SDR million)
PRGF	04/28/2000	04/27/2003	6.66	1.90
Structural Adjustment Facility (SAF)	06/02/1989	06/01/1992	2.80	0.80

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

	Forthcoming				
	2005	2006	2007	2008	2009
Principal	0.10	0.38	0.38	0.38	0.38
Charges/interest	0.02	0.02	0.02	0.02	0.02
Total	0.12	0.40	0.40	0.40	0.40

VII. **Implementation of HIPC Initiative**:

	Enhanced framework
Commitment of HIPC assistance	
Decision point date	12/20/00
Assistance committed (NPV terms) [1]	
Total assistance (US$ million)	97.00
Of which: Fund assistance (SDR million)	0.00
Completion point date	Floating
Disbursement of IMF assistance (SDR million)	
Assistance disbursed to the member	0.00
Interim assistance	0.00
Completion point	0.00
Amount applied against member's obligations (cumulative)	0.00

VIII. **Safeguards Assessments**:

Under the Fund's safeguards assessment policy, the Central Bank of São Tomé and Príncipe is subject to a full safeguards assessment with respect to a forthcoming arrangement. The assessment, which was completed on August 2, 2004, found vulnerabilities in the area of financial reporting, internal audit and internal control and measures to strengthen the control framework and help safeguard Fund resources were proposed. Recommendations are in the process of implementation.

IX. **Exchange Arrangements**:

Since December 2, 1994, the official exchange rate has been market determined. The official exchange rate is determined on a daily basis as a simple average of the previous day's selling rates in the commercial banks, foreign exchange bureaus, and parallel market. The intervention currency for the dobra is the U.S. dollar. São Tomé and Príncipe's exchange rate regime is currently classified by the Fund as managed floating. The central bank introduced foreign exchange auctions in December 2004. The exchange rate was Db.10,104 per US dollar on December 31, 2004; the spread between the official and parallel market exchange rates has been less than 1 percent since 1999.

[1] Net present value (NPV) terms at the decision point under the enhanced framework.

X. **Article IV Consultation**:

The last Article IV consultation with São Tomé and Príncipe was concluded by the Executive Board on March 17, 2004.

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

None.

XII. **Technical Assistance**:

February 2005: STA technical assistance mission on national accounts statistics.

December 2004: STA mission to advice on compilation and reporting of monetary statistics.

October 2004: STA technical assistance mission on government finance statistics.

September 2004: MFD multi-sector mission to develop foreign exchange and interbank money markets.

July-September 2004: MFD expert mission on Banking Supervision.

June 2004: STA technical assistance mission on balance of payments statistics.

July 2004: MFD expert mission on Monetary Operations.

June 2003: STA technical assistance mission on balance of payments statistics.

March and June 2003: STA technical assistance missions on national accounts statistics.

March 2003 and April 2004: Visits by MFD advisors on the conduct of monetary policy and bank supervision.

March 2003: STA technical assistance mission on national accounts statistics.

January 1998-December 2001: MFD advisor on the conduct of monetary policy, banking supervision, and foreign exchange management.

June 2001: MFD mission on handling of banking crisis and foreign exchange market organization.

XIII. **Resident Representative**:

A Fund Resident Representative office has been maintained in since November 1999. The current Resident Representative, Mr. Randriamaholy, took up his post in October 2003.

SÃO TOMÉ AND PRÍNCIPE: RELATIONS WITH THE WORLD BANK GROUP

IDA operations

1. São Tomé and Príncipe joined the World Bank and IDA in 1977. New lending was suspended between 1992 and 2000 owing to the lack of an appropriate macroeconomic framework.

2. The World Bank strategy for the period 2000–05 is to support the government in the pursuit of its objectives as set out in the full poverty reduction strategy paper (PRSP), namely: (i) to sustain strong economic growth that will raise income and reduce poverty; and (ii) to broaden access to services and improve their quality. IDA also aims to strengthen public resource management through technical assistance and reform projects. The World Bank also supports government reforms by providing advisory services in the petroleum sector and telecommunications. A country economic memorandum and a gender study have been completed and a poverty diagnostic is being finalized to enrich country specific knowledge and provide a base for policy dialogues and the new CAS which will be developed in the first half of 2005. An IDF (Institutional Development Grant) was approved in early 2005 to assist the government in its Judicial reform program. A GEF (Global Environmental Fund) was approved in late 2004 to support the development of a national action plan to adapt to environmental and global warming impacts.

Statement of IDA Credits as of February 2, 2005

(In millions of U.S. dollars)

Credit Number	Fiscal Year	Purpose	IDA Commitment[1]	Undisbursed
1590	1985	Economic rehabilitation	5.0	0.0
A029	1987	Special African Facility	3.0	0.0
1825	1987	Structural adjustment credit	4.0	0.0
1830	1987	Cocoa rehabilitation credit	7.9	0.0
2038	1989	Multisector credit	5.0	0.0
2165	1990	Second structural adjustment credit	9.8	0.0
2280	1991	Multisector II credit	6.0	0.0
2325	1991	Agricultural sector	9.8	0.3
2343	1992	Health and education	11.4	0.5
3428	2000	Public resource management project	7.5	2.5
3429	2000	Public resource management technical assistance	2.5	0.2
3902	2004	Social sector support project	6.5	6.1
3993	2005	Governance Capacity Building technical assistance	5.0	4.7
Total:			78.4	14.3
	Of which: repaid		4.6	

[1]Less cancellation.

3. IDA approved a US$6.5 million social sector credit in May 2004 (social sector support project, US$5 million IDA, US$1.5 million grant). A Governance Capacity Building Technical Assistance credit (US$5 million) became effective on February 3rd, 2005. The Public resource Management Credit approved in November 2000 closed in June 2004. Its companion TA closed end 2004.

IFC operations

4. São Tomé and Príncipe is not a member of the IFC. FIAS has reviewed the country's tax system and private sector investment incentives.

São Tomé and Príncipe: Statistical Issues

Introduction

São Tomé and Príncipe's statistical system is still developing and suffers from serious resource constraints (qualified staff as well as financial and computer resources). These constraints have slowed down efforts to strengthen the system.

The authorities participate in the Fund's General Data Dissemination System (GDDS) and, since 2003, are benefiting from the technical assistance provided by the Statistics Department (STA) under the GDDS project for Lusophone Africa.

São Tomé and Príncipe began reporting monetary and balance of payments statistics for *International Financial Statistics (IFS)* in March 1998. (Table 1).

National accounts

Since the mid-1990s, some technical assistance for the compilation of the national accounts has been provided by the World Bank and the United Nations Development Program (UNDP). Since 2003, the Fund has also provided technical assistance in the context of the GDDS Lusophone project.

As a result of the technical assistance in the mid 1990s, the national account estimates compiled for 1994-1997 follow to some extent the *1993 System of National Accounts (SNA)* methodology, reflecting an initial improvement in the source data, compilation methodology, and statistical techniques. However, improvements could not be sustained and beginning in 1998, the quality of national accounts data deteriorated again mainly owing to a decline in the availability of source data and dwindling resources allocated to statistical work. Since then, only preliminary flash estimates of GDP at current and constant prices have been compiled using industry coefficients and growth rate estimates.

With technical assistance provided mainly in the context the GDDS Lusophone Project, the National Institute of Statistics (INE) has made considerable efforts to improve source data, namely, in the context of the country's poverty reduction strategy. It has approved classification systems for the compilation of national accounts, which are broadly consistent with internationally accepted classifications. Efforts are also underway to compile national account aggregates with an improved methodology. An important goal of this project is to elaborate a new GDP series in broad conformity with the *1993 SNA* by mid-2005, and to assist in compiling a quarterly production index.

Progress achieved in strengthening the INE's statistical capacity is very fragile mainly because of the lack of incentives to retain qualified staff. From the four national accounts compilers recruited by INE that attended the three-week regional course held under the

GDDS Lusophone project in mid-2004, one has already left. The allocation of adequate human, financial and computer resources to INE remains critical to achieve a sustainable strengthening of INE's institutional capacity.

Consumer prices

The CPI is calculated monthly and reported to AFR with a lag of one month. Since 1997, the compilation of the CPI has been based on a household survey, financed by the UNDP. Price surveys only cover the capital, although the authorities intend to develop a regional price series by 2004/2005, based on a new household survey.

Unemployment

In 2003, the authorities completed the first comprehensive survey of unemployment with assistance from the World Bank. The survey provides a detailed breakdown of unemployment by age, gender and geographic location.

Government finance statistics

A summary of fiscal data is compiled on a monthly basis, and reported to AFR with a lag of about three weeks. The main weaknesses in the data reported are: (i) expenditures on projects financed by donors, which are not adequately monitored by the Ministry of Finance (MOF); and (ii) the below-the-line financing items are not yet sufficiently reliable.

In the context of the GDDS Lusophone project, the first government finance statistics (GFS) technical assistance mission was undertaken in October 2004. The main objective of this GFS technical assistance was to assist the MOF in compiling and disseminating GFS for the general government in accordance with the IMF's *Government Finance Statistics Manual 2001(GFSM 2001)* . An immediate objective of this project is to enhance the usefulness of existing fiscal data for the formulation, implementation, and monitoring of fiscal policy in São Tomé and Príncipe.

The mission prepared tables bridging the national budget classifications and those recommended in the *GFSM 2001*. These bridge tables are to be used to compile GFS for reporting to STA and AFR, as well as for policy analysis within the MOF. Given the importance of the oil-related revenues, the mission also reviewed in detail the classification of the oil revenues regulated under the recently approved Oil Revenue Management Law, and made recommendations on the classification of these transactions in accordance with the *GFSM 2001.* The mission's report contains an action plan for implementing its recommendations that were agreed with the MOF officials.

No GFS are reported to STA for publication in the *Government Finance Statistics Yearbook* (*GFSY*) and *International Financial Statistics* (*IFS*).

Monetary statistics

An STA mission provided technical assistance on monetary and statistics in December 2004. Since then, the lags with which monthly monetary data are being reported by the Central Bank of São Tomé and Principe (BCSTP) to STA are shorter and data are now reported with two-months lag.

The mission conducted a review of the current collection and compilation procedures of monetary statistics compiled by BCSTP. It developed a work program to address shortcomings, including the statistical issues recently raised by the Safeguards Assessment mission, and provided training to the CBSTP staff to facilitate the compilation of the monetary statistics.

The mission found that the CBSTP monthly balance sheets were adequate to compile monetary statistics in line with the *Monetary and Financial Statistics Manual (MFSM).* Although the accounting treatment of revaluation adjustments (holding gains) is not consistent with recommended practices, data are available for the correct reclassification of the revaluation adjustments. The plan of accounts of the other depository corporations is not fully consistent with the *MFSM,* raising additional challenges in the compilation of the monetary statistics, particularly for recently created banks. The mission report, including the action plan to implement its recommendations, will be sent to the authorities shortly.

External sector

Exchange rates. The authorities record the rates of the official exchange bureaus, commercial banks, and the parallel market. These rates are available on the internet with a one-day lag. The official rate is the simple average of the market rates for the previous day.

Merchandise trade. There are significant weaknesses in the source data collection, and some transactions, including some imports related to investment, are not being fully captured in the balance of payments.

Monthly data on the main exports and imports are reported to AFR regularly. However, unit prices and volumes of exports are only occasionally included.

Balance of Payments. Balance of payments statistics are compiled by the BCSTP. Annual balance of payments data are reported to STA and published in the *IFS*, albeit with long lags and subject to substantial revisions.

In the context of the GDDS Lusophone project, STA launched a technical assistance program to improve balance of payments compilation and dissemination. The GDDS project targets a substantial improvement in the source data, including the response rate to the surveys, and in the methodology for compiling the balance of payments consistent with the Fund's *Balance of Payments Manual*. The first mission, in June 2003, reviewed the shortcomings of current and financial account transactions that are reported, and concluded that the weaknesses were mainly due to the under coverage of several important sectors, including foreign direct investment and commercial banks' reports on international transactions.

The follow-up mission undertaken in early June 2004 found that despite the effort to implement the previous mission's recommendations, several measures, in particular those related to improving source data, were only partially implemented or, in some cases, not implemented at all. As a result, inconsistencies in the classification of BOP operations still persisted and the disaggregated BOP components continued to be largely estimated because of weak source data. Resource constraints, particularly with regard to qualified staff, contribute to the lack of follow up with respondents to improve the response rate to the balance of payments surveys.

The mission recommended improving the coordination and data sharing among data producing agencies. In addition, it suggested intensifying contacts with survey respondents, and using alternative sources identified by the mission in order to substantially improve the source data to compile the balance of payments.

Debt issues

The authorities have built on previous efforts to strengthen debt data management. A new unit was created in late 2003 within the Ministry of Finance, incorporating staff from the debt department of the BCSTP. New staff, including a director, has been appointed, which should improve the monitoring of debt statistics. However, the 2003 technical assistance mission on balance of payments statistics noted that the data available for external debt are incomplete and do not conform to international guidelines.

TABLE 1. SÃO TOMÉ AND PRÍNCIPE: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

AS OF JUNE 27, 2005

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange Rates	June 2005	June 2005	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	May 2005	June 2005	M	M	M
Reserve/Base Money	May 2005	June 2005	M	M	M
Broad Money	April 2005	June 2005	M	M	M
Central Bank Balance Sheet	May 2005	June 2005	M	M	M
Consolidated Balance Sheet of the Banking System	April 2005	June 2005	M	M	M
Interest Rates[2]	April 2005	June 2005	M	M	M
Consumer Price Index	May 2005	June 2005	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	May 2005	June 2005	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	May 2005	June 2005	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Dec. 2004	May 2005	Q	Q	I
External Current Account Balance	Dec. 2004	May 2005	A	I	A
Exports and Imports of Goods and Services	May 2005	June 2005	A	I	A
GDP/GNP	2004	May 2005	A	I	A
Gross External Debt	Dec. 2004	May 2005	Q	Q	I

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).

São Tomé, June 30, 2005

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. de Rato:

1. We enclose with this letter the Memorandum of Economic and Financial Policies (MEFP) that underpins our economic program and poverty-reduction strategy for 2005-2007, and sets out specific objectives and quarterly financial and structural targets for 2005.

2. To strengthen the efforts to alleviate poverty in São Tomé and Príncipe, we need a stable macroeconomic framework to revitalize growth while keeping inflation low and improving our external position. Given the importance of ensuring that the macroeconomic adjustment in the program is acceptable to the Sãotomean people, our government has made every effort to reflect social concerns in the program and conducted an ample news campaign to explain to the population at large the benefits of the proposed economic program. The increase in the monthly minimum wage from US$31 to US$40 in 2005 is one of the government's venues to address social demands, although we are aware that further wage increases of this magnitude would be unsustainable. Also, the government has submitted to the IMF and the World Bank its full poverty reduction strategy paper (*Estratégia Nacional para Redução da Pobreza*; PRSP), that was promulgated by the President of the Republic in January 2003 and an update of the strategy issued in January 2005.

3. The key components of the 2005–07 program are:

- A medium-term macroeconomic framework consistent with price stabilization and the PRSP's macroeconomic targets;

- A strong fiscal adjustment that will contain the growth of public expenditure and strengthen tax collections, while allowing increases in pro-poor government spending;

- Gradual use of the oil signature bonus on Block 1 (totaling US$49.2 million), which has been deposited into the government's National Oil Account held with the Federal Reserve Bank of New York, and the receipt of which is a prior action for the approval of the new PRGF arrangement, and;

- Structural adjustment measures in the areas of public enterprise reform, public expenditure management, banking sector prudential regulation, business climate, and central bank safeguards assessment implementation.

4. To support these objectives and policies São Tomé and Príncipe hereby requests a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF), covering the period July 2005-July 2008, in a total amount equivalent to SDR 2.96 million (40 percent of quota), to be provided in seven semi-annual disbursements.

5. The Government of São Tomé and Príncipe believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of its program, but it will take further measures that may become appropriate to this purpose. São Tomé and Príncipe will consult with the Fund on the adoption of these measures, and in advance of the revisions to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation. São Tomé and Príncipe will provide the Fund with the necessary data on a timely basis for monitoring purposes. During the program period, the government will not introduce or intensify any exchange rate restrictions or multiple currency practice that are inconsistent with Article VIII of the Fund's Articles of Agreement, or introduce or intensify import restrictions for balance of payments purposes. Consistent with its intention to keep the public informed about its policies and objectives, the government will publish the MEFP and will report periodically on progress under the program.

6. We propose that the Fund carry out reviews under the 2005 program in December 2005 and April 2006 based on the observance, respectively, of end-September and end-December 2005 quantitative performance criteria, and structural performance criteria, as established in Tables 1 and 2 of the attached memorandum.

7. We are confident that the program will deliver sustained growth and substantive poverty-reduction, and hence that it deserves the support of the international financial community.

Sincerely yours,

/s/

Maria do Carmo Trovoada
Prime Minister and Minister of Planning and Finance

SÃO TOMÉ AND PRÍNCIPE

Memorandum of Economic and Financial Policies for 2005–07

June 2005

I. Introduction

1. The Government of São Tomé and Príncipe has embarked on a medium-term program for poverty reduction and growth that can be supported by the International Monetary Fund and will give São Tomé and Príncipe access to further debt relief from the international community under the enhanced HIPC Initiative.

A. Program Objectives

2. The program centers around two principal objectives: (i) create the conditions for high and sustained economic growth over the medium-term; and (ii) contribute to a reduction in poverty. To achieve these objectives, the program will pursue rigorous financial policies and wide-ranging structural reforms, while safeguarding pro-poor spending, as envisioned in the government's Poverty Reduction Strategy (*Estratégia Nacional de Redução da Pobreza)*.

3. The government, conscious of the need to ensure that such a program is acceptable to Sãotomean public, will ensure that, in implementing fiscal adjustment, pro-poor spending would not be compromised. To this end, expenditure on health and education will increase during the course of the program. Moreover, the adjustment measures will be accompanied by reforms that will seek to strengthen good governance and transparency in the management of public resources. The program deserves the financial support of the international financial community, not only because of the courageous adjustment measures it contains, but more importantly because of its fundamental goal is to raise the living standards of the Sãotomean people.

B. Recent Economic Developments

4. Real GDP grew by 3.8 percent in 2004. Growth was less buoyant than initially envisaged, as expectations of a take-off driven by the oil sector did not materialize. A relaxation of macroeconomic policies helped maintain growth close to the 2003 level, but inflation edged up to 15.2 percent (end-of-year). Real GDP per capita has been increasing only marginally during the last five years; 54 percent of the population remain poor, with 15 percent of living in extreme poverty.

5. The overall fiscal deficit (on a commitment basis) remained very high in 2004, at 26.3 percent of GDP. The deficit was mainly financed by short- and medium-term external borrowing and central bank financing, while the anticipated receipt of oil signature bonuses lagged and the government sought to meet pressing demands for social spending. The

domestic primary deficit, which excludes from the overall deficit definition all foreign financed outlays and external interest payments, increased significantly between 2003 and 2004: from 11.7 percent of GDP in 2003 to 20.6 percent in 2004. External payment arrears to Paris Club and non-Paris Club member countries continued to accumulate in 2004. The government expects to reschedule its debts to the Paris Club, and benefit from debt relief under the Enhanced HIPC initiative from Paris Club creditors and other creditors, once the Fund arrangement is in place and other floating Completion Point triggers are fulfilled.

6. At the same time, throughout 2004, the central bank relied heavily on intervention in the foreign exchange market to avoid a depreciation of the dobra and mop-up excess liquidity stemming from large fiscal deficits and a very rapid expansion of bank credit to the private sector. As a result, gross official reserves declined from US$23 million at end-2003 to US$18 million at end-2004 (from 4.5 to 3.4 months of imports of goods and services).

II. Macroeconomic Framework for 2005–07

7. The program for 2005–07 aims at correcting widening macroeconomic imbalances and creating the conditions for high and sustained growth over the medium term. Annual GDP growth is envisaged to slow down in 2005 in response to tight financial policies, but pick up gradually during the next two years mainly on account of expanding economic activity in the services sector. End-year inflation is projected to drop to single-digit levels by end-2007. The framework envisages maintaining gross international reserves at around 3 ½ months of imports, and limiting the deterioration of the current account deficit.

8. The fiscal program will seek to secure medium-term fiscal consolidation while allowing for appropriate pro-poor spending as identified in the PRSP. To that end, it will aim at increasing tax revenue, reducing wasteful government expenditure, and eliminating government recourse to central bank financing after 2005. No new domestic or non-reschedulable external payment arrears will be accumulated during the program period.

9. The external current account deficits after grants will remain large during the program period owing mainly to growing imports of oil sector-related investment goods. These deficits will be largely financed by a mix of medium- and long-term borrowing, foreign direct investment (including by petroleum exploration companies), debt relief assuming the reaching of HIPC completion point in the first half of 2006, and the gradual use of revenue from the oil bonus payment on Block 1 to be received in late-June 2005. The remaining financing gaps, averaging less than US$0.5 million during 2006–07—down from US$18 million in 2005—could be covered by program grants and loans from donors and multilateral creditors for poverty alleviation and reforms of the public sector. The government will also seek additional support from donors in the context of the upcoming Donors' Round Table tentatively scheduled for October 2005.

10. The combination of domestic adjustment and external debt relief should lead to an improvement in the external debt indicators. Total external debt is expected to decline from

483 percent of GDP in 2004 to 308 percent in 2007. Domestic debt will remain insignificant over the medium-term.

III. The Economic Program for 2005

11. The program for 2005 will seek to: (i) reverse the upward trend in inflation registered in 2004; (ii) address the rapidly deteriorating fiscal situation; (iii) tackle the weakening central bank reserve position; and (iv) set the stage for a new external debt rescheduling agreement with the Paris Club. Achieving the 2005 macro objectives will require concerted implementation of fiscal and monetary policies, and of key structural reforms embodied in the PRSP. The government has decided to create an inter-ministerial commission by end-July 2005, that will monitor the implementation of the program.

A. Fiscal Policy

12. The 2005 budget envisages a large adjustment mainly driven by the need for fiscal consolidation and the limited sources of financing. The budget targets a reduction in the domestic primary deficit from 20.6 percent of GDP in 2004 to 17.5 percent in 2005; domestic financing of the deficit will be limited to 0.7 percent of GDP. The fiscal adjustment will be buttressed by: (i) tax policy reform aimed at increasing excise duties and reforming the personal and corporate tax codes; (ii) a major tax administration reform; and (iii) an austere spending envelope for goods and services and capital expenditure financed by the treasury. However, the government expenditure envelope accomodates an increase in the monthly minimum wage from US$31 to US$40 dollars which will help in addressing social concerns. To ensure macroeconomic stability, the wage increase will be implemented together with a reform of the public sector compensation system (see para. 16 below).

Tax policy reform

13. To simplify and provide for a more equitable tax system, and to place public finances on a permanently sound footing, the 2005 fiscal program includes measures to increase excise duties levied on imported goods and domestically-produced goods and services, as well as urban property taxes. The program also assumes that the government will submit to the National Assembly a thorough tax reform package[12] by end-July 2005 that will become effective in 2006. Overall, the measures already taken or contemplated for 2005 include:

- The (dobra-denominated) reference prices used to assess excise duties on a core group of nonfood imports were increased on January 7, 2005. Previous reference prices dated from the 1990s and their nominal values had become outdated due to the

[12] The tax reform package includes a new code on personal income tax, a new code on corporate taxation, a new tax procedural code, new guidelines on urban property taxation, and new legislation on inheritance taxes.

devaluation of the dobras in recent years. This measure is expected to yield an estimated dobras 9.5 billion, equivalent to 1.4 percent of GDP in 2005.

- The excise tax applicable to the provision of services will be increased effective July, 15, 2005, from 2 percent to 5 percent. This measure is expected to yield an estimated dobras 3.3 billion, equivalent to 0.4 percent of GDP in 2005. Also, the concession on excise duty on domestically-produced beer has been terminated, with the new ad valorem rate set at 25 percent. This measure is expected to yield an estimated dobras 1.5 billion, equivalent to 0.2 percent of GDP in 2005.

- The government's policy is to keep retail petroleum prices in line with world market prices. To this end, in November 2004, the domestic price of gasoline and gas oil were increased by 24 percent and 46 percent, respectively, to fully pass-through the rise in international prices that occurred last year. However, for 2005, and in view of the need for fiscal revenue, any decline in world market prices will not be passed-through to consumers, and instead the margin would accrue to the treasury, thus improving tax revenue beyond the program targets.

- Revenue from urban property taxes will be boosted in 2005 by an increase in coverage and tighter enforcement of regulations governing the collection of these taxes. It is expected that the coverage could be tripled from the current level of 4,000 registered dwellings, yielding dobras 800 million (0.1 percent of GDP) in additional revenue in 2005.

- The government will submit to the National Assembly by end-July 2005, a new personal income tax code that will become effective in 2006. The tax reform will involve broadening the tax base and introducing a progressive income tax system (structural performance criterion). New sources of income—including bonuses, other monetary premiums, and in-kind benefits—will be brought into the definition of taxable income. The minimum tax-exemption threshold will be updated, while new tax rate schedules will be adjusted to provide more progressivity to the system. Preliminary government estimates show that the reform will lower personal income tax revenues by 0.3 percentage points of GDP in 2006.

- The government will submit to the National Assembly by end-July 2005, a new corporate income tax code that will also become effective in 2006. The new code will seek to lower the average profit tax rate to the 25–30 range, which would bring the corporate tax rate more in line with international norms and should make the environment more conductive to the growth and development of new and old companies alike. The reform will also lead to a more equal treatment for businesses by limiting the granting of tax holidays—which currently benefit selected large businesses—to new licensed investors to a maximum of three years, with tax deductions only covering up to 75 percent of the profit taxes due (structural performance criterion). Preliminary estimates show a net revenue loss of 0.4 percent of GDP in 2006, which the government believes could be partially offset by the increased investment spurred by the more attractive tax framework in place.

Tax administration reform

14. The reform of tax administration has several objectives. First, it will aim at removing certain ambiguities in various tax laws. Second, a new tax code *(Codigo General Tributario)* and a new tax procedural code *(Codigo de Processo Tributario)* will establish, inter alia, (i) tax tribunals at different levels of government (regional and national level) to handle tax issues and disputes (structural performance criterion), (ii) penalties and fines for underpayment, late payment, and other tax violations (structural performance criterion), and (iii) more adequate resources for tax collection and enforcement agencies. Third, in the case of the urban property tax *(Contribuiçao Predial Urbana)*, the reform targets the development of new official registries of the quantity, value, and ownership of urban real estate used in apportioning taxes (structural performance criterion). And, fourth, taxes like inheritance taxes (structural benchmark), taxes on grants, and taxes on asset transfers will be simplified further, while broadening their taxable base and increasing their tax rates. In addition to the reforms above, the government will continue to enforce the use of taxpayer identification numbers (*cartao de identidad fiscal)* throughout the territory.

Wage bill and other government expenditure

15. Given the low level of minimum wages, the government has decided to increase the civil servants' minumum wage to US$40 per month in 2005. We are commited to avoid any other ad-hoc increases in wages to keep the wage bill sustainable in the medium-term.

16. At the same time, to correct distortions stemming from the current compensation system, including an obsolete wage grid, the 2005 fiscal program will seek to eliminate all selective salary increases and/or special wage regimes. The new policy framework will: (i) broaden the scope of wage negotiations to cover all government employees at the same time; and (ii) for purposes of wage negotiations, redefine the concept of remuneration to include the basic salary, overtime fees, supplementary salary payments, and other subsidies. With these measures in place, the increase in the nominal wage bill will be contained below the annual inflation rate in 2006 and 2007. In the case of embassies overseas, the wage bill for 2006–07 will be kept constant at the end-2005 euro values for embassies in European countries and US dollars for other embassies.

17. Outlays in goods and services are projected to decline from 15.2 percent of GDP in 2004 to 7.8 percent in 2005. While a reduction of 3.3 percent of GDP can be attributed to the exceptional expenditures stemming from the conference of Community of Portuguese Language Countries (CPLP) held in São Tomé in July 2004, the remaining spending cuts will be attained through a sharp decline in: (i) telecommunication spending of budgetary units, from 2.8 percent of GDP in 2004 to 1.3 percent in 2005, (ii) water and electricity consumption, from 4.0 percent of GDP in 2004 to 3.0 percent in 2005, and (iii) spending on official travel, from 1.5 percent of GDP in 2004 to 1.0 percent in 2005. Such cuts will be

enforced through the enactment of directives by the Ministry of Planning and Finance and the corresponding reductions in 2005 budget allocations for all affected budgetary units. Other categories of expenses in goods and services are projected to grow in line with inflation.

18. Domestically-financed capital expenditure will also be restrained. From dobras 51 billion in 2004 (equivalent to 8.0 percent of GDP), domestically-financed projects will be targeted at dobras 29 billion in 2005 (equivalent to 3.9 percent of GDP). While this reduction is necessary in view of our objective of fiscal restraint in 2005, the government will ensure that any disruption to its program of social spending is kept at a minimum by effectively prioritizing projects. In addition, part of the reduction reflects projects which had initially been earmarked for domestic funding, but for which the government now intends to fund through counterpart funds from the Japanese government.

19. Aggregate pro-poor spending, as defined in the government's Poverty Reduction Strategy (see also, paragraph 44, below), is budgeted at 29.3 percent of GDP, including HIPC financed expenditure. This compares with estimated pro-poor spending of 22.2 percent of GDP in 2004. At the same time, social safety mechanisms have been further strengthened to mitigate the cost of macroeconomic adjustment on the poorest sections of the population. Pro-poor spending on health will be substantially increased, as it is considered the sector with the highest impact on living standards, given the incidence of various tropical diseases affecting the population.

B. Public Expenditure Management

20. The government attaches the highest importance to the effective control and monitoring of public expenditure, as a means of ensuring that the spending priorities identified in the government's Poverty Reduction Strategy and reflected in our 2005 budget are implemented as planned. A number of steps have been taken or will be implemented shortly to improve public expenditure management:

- A PRSP unit has been set up at the Ministry of Planning and Finance, with the objective of ensuring the implementation and monitoring of the PRSP. Currently, the unit is updating some areas of the PRSP for which information had become outdated, such as recent developments in the domestic oil sector, including the adoption of the legislation for management of oil revenues. By end-September 2005, the unit will issue a report on the status of implementation of the PRSP.

- The PRSP unit, in coordination with the Directorate of Planning in the Ministry of Planning and Finance, has also the responsibility of monitoring grants. One key objective in this area will be to ensure that projects for which funds have been donated are executed adequately. Particular emphasis will be on implementation of pro-poor oriented projects. Information gathered by the unit will form the basis of reporting of pro-poor spending for the Ministry of Planning and Finance and eventually to the Fund. This would allow an effective monitoring of pro-poor spending in the context of the 2005-08 PRGF- supported program.

- With the support of the UNDP, the central government will review its payment system of wages and salaries, and develop a public employees' register. In particular, the reform will computerize wage and salary payments, and update information about the number of public sector employees, their job description, and their place of work within the sector. By September 2005, the government expects to have in place: (i) a computerized registry to be used for public sector human resource management; (ii) trained personnel to handle the registry; and (iii) the necessary hardware and other technical equipment. The rest of the project will be implemented no later than January 2006.

- During 2005, the government will implement the recommendations from the Auditor General's Office stemming from the review of the 2004 financial accounts of the central government. This report is expected to become available during the third quarter of 2005.

21. A fully integrated, computerized budget and public expenditure management system, developed with assistance from the Fund's Fiscal Affairs department (FAD) and the World Bank, will be launched in 2005. The government established a timetable in June 2005 that provides for the implementation of the integrated budgetary classification system by mid-2006 which would include, among other things, new budget classifiers and a double-entry method compatible with a new chart of government accounts (structural benchmark).

22. To improve the management of resources and avoid the re-emergence of domestic arrears the government will introduce an expenditure/cash management system underpinned by quarterly projections of government revenue. Specifically, expenditure commitments will be prioritized in line with expected revenue. This approach will allow the Budget Directorate at the Ministry of Planning and Finance to better identify and monitor the seasonality in revenues and grants, and adapt the expenditure path accordingly within the calendar year.

23. The government is also committed to improve the system of public procurement during the next three years. Key objectives are: (i) to establish guidelines for government accounting practices regarding the acquisition, transfer and consumption of goods and services; and (ii) update and computerize the cadastre of government assets. The World Bank's loan on Governance and Capacity Building Technical Assistance will be financing this project. The new procurement practices are expected to be in place by end-2005.

C. Monetary and Exchange Rate Policy

Monetary policy

24. Monetary policy will aim at reducing inflation to 15 percent by end-2005. To this end, the stock of net domestic assets of the BCSTP will be limited to dobras -82.9 billion at end-2005, while the floor on the stock of net international reserves (NIR) of the BCSTP will be set at US$14.9 million. This floor should allow end-2005 gross international reserves to remain at 3.4 months of imports of goods and services, and provide more than 100 percent

coverage of short-term liabilities, including base money. The improved fiscal stance expected for 2005 will facilitate meeting these targets.

25. The monetary program assumes a broadly stable velocity of money, which is consistent with broad money growth projected at 12.3 percent. This, in turn will be consistent with a slowdown in private sector credit growth from 116 percent in 2004 to 19 percent in 2005, while safeguarding the banking sector's NFA position. This path reflects a comfortable level of use of bank credit already achieved (that is, the stock of bank credit to the private sector is about 28.1 percent of GDP), as well as the tightening of liquidity conditions needed to reduce inflation as planned.

26. The BCSTP will also continue to work closely with the Fund's Monetary and Financial Systems Department (MFD) regarding the implementation of the technical assistance recommendations in the areas of implementation of indirect monetary instruments such as certificates of deposit and the special liquidity facility for banks. To actively manage liquidity, the BCSTP stands ready to rely on changes in reserve requirements, if necessary. Enhanced coordination of fiscal and monetary policies will be implemented to secure an effective use of the oil bonus.

27. The BCSTP is committed to the continuation of a flexible exchange rate arrangement, as already signaled by the recent introduction of foreign exchange auctions recommended by MFD. The scope and timing of the foreign exchange auctions will be consistent with the NIR targets set under the program.

D. Financial Sector Reform

28. To improve the soundness of the banking system, the BCSTP has been implementing a number of programs that include actions to improve regulation on the licensing of new banks and enhance prudential standards. The reform will also strengthen mechanisms to prevent money laundering and financing of terrorism and deter domestic financial crime.

Licensing of financial institutions

29. During the last sixteen months, in consultation with MFD, the BCSTP has been improving its instruments, as well as training its staff, on the procedures for licensing financial institutions and the criteria to be adopted by supervisors to approve or deny these licenses. The regulation on the licensing of financial institutions was approved in April 2004. As of end-December 2004, two applications had already been reviewed according to the new standards.

Prudential regulation and supervision

30. The strengthening of supervision and prudential regulations will provide the Directorate of Banking Supervision at the BCSTP with the instruments to guarantee that all financial institutions maintain healthy solvency and liquidity indicators. The main actions to be enacted during 2005 include:

- The implementation, by September 2005, of a consolidated reporting mechanism on financial conditions to be submitted by banks to the central bank on a quarterly basis. This "call report" will permit off-site surveillance of quality of assets, liquidity ratios, capital adequacy, profitability, interest rate and foreign exchange risk.

- Review of banking sector prudential regulation with emphasis on capital requirements, asset classification, auditing and internal controls, with a view to incorporate elements of Basel II recommended guidelines such as the standard approach for credit risk.

- Implementation of on-site examination guidelines to evaluate banks' credit portfolios, with emphasis on the credit policy soundness, loan classification, necessary provisions, examination procedures and remedial actions to be undertaken by bank supervisors.

- The establishment of a Credit Risk Bureau during the third quarter of 2005 that will permit global surveillance of the financial sector's credit risk.

- Keeping under strict surveillance by the monetary authorities the Banco do Equador, which ceased operations in 2001 but was authorized to open again in March 2004, following an initial recapitalization of the bank. In light of the bank's still difficult liquidity position, the BCSTP has agreed with the bank's shareholders on a plan for additional recapitalization effective March 2005.

31. The government of São Tomé and Príncipe is committed to have in place legislation to criminalize money laundering and the financing of terrorism. To this end, in consultation with the Fund's Legal department, the BCSTP will develop an action plan on the technical steps required for a successful submission to the National Assembly—by September 2005—of the proposed legislation criminalizing money laundering and financing of terrorism (structural benchmark). A formal request for technical assistance on this matter was submitted to the IMF in January 2005.

E. External Sector Policies

32. During 2005, the government will continue to seek technical advice from the international community in the context of the Integrated Framework for Trade-Related Technical Assistance. Topical areas in this regard include, in particular: (i) an in-depth analysis of the economic effects of free trade zones on São Tomé and Príncipe's economy; (ii) adoption by end-September 2005 of an action plan for streamlining the process of establishing businesses; and (iii) a review and update of the commercial code in consultation with the World Bank and other donors.

33. In coordination with the World Bank and other donors, the Ministry of Commerce will continue to assess major trade policy issues during 2005. In assessing São Tomé and

Príncipe's participation in bilateral and regional trade arrangements, the government will be mindful of the impact of these memberships on domestic tax revenue collections.

34. Regarding the trade regime, in 2005, the government will conduct a survey of existing customs exemptions with a view to their gradual elimination during the coming years, except for those exemptions contemplated in international agreements. At the same time, the existing non-tariff barrier related to the privately-managed (though partially state-owned) telecommunications company (CST) will be eliminated by end-December 2005. Existing regulations protecting CST from competition will expire on that date, opening the sector to new operators.

F. Governance and Structural Reform

Oil sector issues

35. The government is committed to zero-tolerance for all acts of corruption and, during 2005–07, it will strive to continue improving governance in São Tomé and Príncipe. In the oil sector, envisaged policies include:

- A further strengthening of the public information campaign launched in 2004 to disseminate basic information on the petroleum industry to the public. A National Forum with the civil society, which took place during June 16 to July 12, 2004, was well received by population, and was an effective venue to survey the expectations that the Sãotomean public has about the future of the country's economy, and in particular, the management of the petroleum revenues. In 2005, the government will continue this dialogue with the civil society. During February 28–March 1, 2005, a workshop marked the launching of a public information campaign on: (i) the content of the Oil Revenue Management Law (see paragraph 49 below); (ii) the status of contract negotiations on Block 1 and the most recent round of bids; and (iii) the setting of the National Petroleum Agency (ANP).

- The formulation of an overall strategy for petroleum sector development that would include plans for transparent, orderly, and well-managed sector development. The strategy, which is being developed in consultation with the World Bank and the UNDP, will address options for institutional settings regarding the development of the country's Exclusive Development Zone (EDZ), the country's possible participation in petroleum exploration and development activities either through the establishment of a national oil company and/or direct joint ventures with the international petroleum companies. The strategy will be finalized during the third quarter of 2005 and will be part of the referred public information campaign on the oil sector.

- Implementation of the Abuja Declaration, signed by the Presidents of Nigeria and São Tomé and Príncipe in June 26, 2004, concerning: (i) the alignment of publication and other information-transparency practices of the Joint Development Authority (JDA) with in the Extractive Industries and Transparency Initiative (EITI); and (ii) the implementation of appropriate amendments to the confidentiality clauses of the Joint Development Authority's Regulation for Petroleum Operations. The practices called for under the Abuja Declaration were adopted by the Joint Ministerial Council governing the JDA in November 2004.

- Implementation of the work plan, developed in consultation with the World Bank staff, on the setting and development of the National Petroleum Agency (ANP). Also, with financial support from the World Bank's EITI Trust Fund, the government intends to foster the production, publication, and dissemination of oil sector-related information. As a first step, emphasis will be placed in developing an efficient website, as well as in setting of effective internal controls and auditing practices for the national petroleum agency.

Public enterprise reform

36. The government believes that the financial position of the public water and electricity company (EMAE) should be strengthened as soon as possible. As a first step, EMAE will introduce a system of prepayment through electricity metering keypads for residential and commercial users, which would generate advance cash flow for utilities, eliminate customer debt, reduce fraud risk and lower the costs of meter reading and billing. To implement this system, EMAE will receive a bank loan, for which the government has agreed to grant a guarantee on the condition that EMAE develops a broader financial strategy to address its weak financial position, including a timetable for the reduction of outstanding payments arrears by electricity customers, no later than end-July 2005 (structural benchmark). At the time of the first review, the government intends to present a firm timetable for arrears clearing; it is expected that this timetable would provide a basis for proposing a new structural performance criterion in this area for end-December 2005.

37. Over the medium term, it is envisaged that electricity production will be in the hands of private sector investors with renowned technical capabilities. A contract with a reputable international electricity company was signed by the government in mid-2004 for the construction of a new hydroelectric plant. The contract also granted the refurbishing and exploration rights of the Contador hydroelectric plant to the same private investor. In addition, the government is currently considering granting exploration rights of the thermal electricity plant to another private foreign investor. EMAE will remain in charge of electricity distribution to final users.

38. The government is aware that privatization of public enterprises can play an important role in fiscal consolidation. On the one hand, it could raise revenue from the sale of state-owned assets. On the other, the transfer of state enterprises to private owners would allow the state to avoid pressures to subsidize public enterprises. In this context, the government intends to complete feasibility studies by end-2005 (structural benchmark) and decide on the privatization of the public enterprises administering airports (ENASA) and sea ports (ENAPORT).

Judicial sector reform and business climate

39. During 2005–07, with the support of the World Bank, the government will seek to address the most urgent needs for institutional reform and technical capacity building of the judicial system. Grant financing from the World Bank will support a work plan in four main areas: (i) an assessment of the justice sector's capacity, including potential costs and timetables of reform proposal, as the basis for a multi-year reform strategy; (ii) training for judges, prosecutors and court personnel on strategic issues, such as criminal, civil, commercial, labor, family and juvenile law, as well as judicial methods, management and research; (iii) review and modernization of the country's legal framework, including reforms of the civil, criminal, and commercial codes based on national experience and circumstances; and (iv) a review of the informal conflict resolution systems (that is, traditional or community-based mediation mechanisms) currently in place.

40. To improve the business climate, the government will submit to the National Assembly by end-July 2005 a new investment code that will provide equal treatment for domestic and foreign investors operating in São Tomé and Príncipe (structural performance criterion). This new investment code, together with the new corporate income tax code (see paragraph 13), will rationalize preferential tax regimes. In the same vein, before end-July 2005, the government will revisit other relevant existing tax legislation with a view to close any possible tax loopholes. The new investment code will guarantee: (i) free and fair competition among investors; (ii) investors' rights to freely transfer abroad receipts and/or profits according to the law; and (iii) repatriation of capital. Benefits to be awarded under the new investment code include access to land for construction of investment premises and granting of user rights on urban or rural dwellings owned by the state that are deemed necessary for a successful implementation of the investment project. In light of the sensitivities connected with the granting rights over land and/or dwellings belonging to the state, the government will seek technical advice from the World Bank and other donors to analyze and best regulate this process.

41. In an effort to support broad-based economic growth over the medium-term, the government will develop by end-December 2005, the terms of reference for a study on land tenure, which would analyze, among other things, the economic effects of a lack of complete property rights for land-holders (structural benchmark).

Central bank safeguards assessment

42. A safeguards assessment of the CBSTP conducted by the Fund's Finance department in March/April 2004 found that the central bank had made progress in strengthening its safeguards framework since the completion of a transitional assessment in 2001. During the last twelve months, the government has been working steadily to address the remaining structural weaknesses identified in the assessment, particularly in the areas of legal, reporting, internal audit, and internal control measures. A number of specific measures have been implemented or will be implemented shortly in this regard:

- On May 31, 2005, a Letter of Commitment between the Governor of the BCSTP and the Minister of Planning and Finance was signed allowing the central bank to distribute only realized earnings to General Reserve and to the government.

- By end-August 2005 a protocol between the Governor of the BCSTP and the Minister of Planning and Finance will be signed to confirm the outstanding stock of government debt to the BCSTP and set: (i) the interest rate to be paid on such a debt and (ii) its amortization schedule.

- Necessary documentation was provided to the Fund staff confirming that the position of BCSTP Vice-Governor was filled in on September 20, 2004.

- On October 20, 2004 the BCSTP Board of Directors authorized the hiring of the firm BDO Binder Co. to audit the annual financial statements of the BCSTP with a three year term and a yearly renewal clause.

- By end-July 2005, the BCSTP will post in its internet website the 2003 and 2004 central bank's audited financial statements including the detailed explanatory notes together with the audit opinion. Publication of the audited financial statements will become a norm for the BCSTP from now on.

- During 2005, the BCSTP, in consultation with the Fund's Statistics Department, will start deriving the monetary statistics automatically from the central bank's accounting department's balance sheet. To this end, the BCSTP is working to generate the balance sheets of the central bank and the deposit money banks in an electronic format.

- In coordination with the Fund's Finance department (FIN), the BCSTP will seek to implement during 2005 any remaining technical recommendations included in the safeguards assessment of the BCSTP. These include recommendations on the early adoption of International Financial Reporting Standards (IFRS); implementation of a plan to modernize the central bank's internal audit function and financial risk analysis; and the development of formal investment guidelines of foreign reserves.

G. Statistical issues

43. The government is committed to the production of more timely and accurate statistics, in support of transparency and to allow better assessment of developments in the economy. To this end, the CBSTP will be working with the Fund's Statistics Department on the introduction of standardized forms for reporting monetary data to the Fund and the development of an integrated monetary database. Technical assistance provided by STA under the Fund's General Data Dissemination System (GDDS) Lusophone Project is viewed by the government as crucial in the authorities' efforts to revamp the country's statistical capacity. Ongoing work regarding the production of a revised system of national accounts for the period 1996–2002 and the development of new survey systems to compile national

accounts data by the National Statistics Institute (INE) is evidence of this policy commitment by the government. In addition, the outstanding World Bank Governance Capacity Building technical assistance credit also envisions supporting INE's capacity-building efforts.

IV. The Social Framework for the Program

44. The government's ability to implement the program will depend critically on the public support that can be assembled. To this end, it has been operating on a twofold social strategy, in addition to ongoing work towards attaining the HIPC goals:

- First, the full Poverty Reduction Strategy Paper (PRSP) includes a detailed account of critical social projects, a review of the PRSP implementation record to date, and the macroeconomic framework which is the basis for the economic program described in this Memorandum of Economic and Financial Policies (MEFP). Thus, the program's policies aim at responding to the needs of the population (and in particular the less privileged) as fully as financial resources permit without endangering fiscal sustainability.

- Second, in consultation with the World Bank and IMF staff, the government has made a preliminary identification of expenditure items—both current and capital outlays—that it believes best represent pro-poor spending. Current pro-poor spending consists of: (i) salaries of the ministries of Education and Culture, Health, and Labor and Solidarity; and (ii) spending on goods and services, and on transfers, of the Education and Culture, and of the Health ministries that have a direct impact on alleviating poverty. For capital outlays, pro-poor spending includes, inter alia, projects in the areas of: (a) provision of potable water and electricity to low-income communities; (b) education (e.g., building and furnishing classrooms); and (c) health (that is, equipping and provision of technical assistance for the main hospital in São Tomé). The government will review the categorization further to ensure accuracy in identifying pro-poor spending. A template agreed with Fund staff will form the basis of regular reporting in the context of the 2005–07 program.

V. Progress Towards HIPC Goals

45. The government considers attaining the HIPC Initiative completion point as one of its priorities. To this end, it has progressed steadily towards the implementation of policy reforms and social measures laid out in the HIPC decision point document. Notably, the sectoral strategies for health and education have already been developed and costed.

46. In the education sector, since 1999 the government has built most of the primary and secondary school classrooms agreed to as a HIPC completion trigger point. Furthermore, between 1999 and 2004, 134 primary school teachers and 174 kindergarten teachers where hired.

47. In the health sector, 7 health centers have been built during 1999–2002 and another 2 posts have been re-habilitated. Three of the newly built health centers have been equipped.

Vaccination of the children for major childhood diseases (DPT3, Polio, BCG and measles) has met or surpassed the HIPC completion triggers (set at 85 percent). As of 2002 the government had not yet succeeded in reducing the mortality of children (under 5) from malaria; however, the anti-malarial campaign launched in 2003 in Príncipe (education, fumigation, bed nets) and extended in 2004 to the island of São Tomé provides anecdotal evidence of a large drop in infections, and will reduce mortality rates, particularly that of children.

48. Regarding public expenditure management, the government has been active on several fronts, although it recognizes that more work is needed to fulfill these trigger points:

(i) To date, the government monitors closely the use of HIPC funds. These funds are included in the budget and supervised by the directorates of Treasury and Planning. The Ministry of Planning and Finance has undertaken internal and external audits.

(ii) Programming and execution of foreign-financed capital expenditure (loans) are under the control of the Ministry of Planning and Finance. At the same time, to streamline reporting and avoid execution inconsistencies with regards to some grants, the government has requested all development partners to help in bringing all externals assistance under the budgetary system.

(iii) The country does not yet have a medium term expenditure framework (MTEF). However, the government is committed to develop such a framework within the next three to four years with the support from the World Bank and IMF staffs. Ongoing work on the development of a computerized budget and public expenditure management system (see paragraph 21 above) would be fundamental in this endeavor.

49. The government has implemented several of the governance HIPC completion trigger points:

(i) In the petroleum sector, the Oil Revenue Management law was approved by the National Assembly in December 2004.The institutional framework for developing the national petroleum policy and to supervise and to regulate the sector became operational in the first half of 2004. This framework includes the National Committee on Petroleum (NCP)—headed by the President of the Republic and including the Prime Minister, other senior government officials, as well as representatives from NGOs and the private sector—and the National Petroleum Agency (NPA), which absorbed the small technical petroleum unit already functional since 2002.

(ii) The Auditor General's Office (*Tribunal de Contas*) has been functional since mid-June 2003. However, the tribunal of arbitration of business and contract matters has not been made operational yet.

VI. Challenges with Oil Sector Development

50. The government sees the development of the oil sector as a key element in its economic growth and development strategy. Progress with the auctioning of the oil fields in the Joint Development Zone confirms the country's potential in this regard. The government is fully aware, however, of the consequences of ineffective management of oil revenue and the possible distortions to the non-oil economy of a booming capital-intensive energy sector. Against this background, the government is committed to foster transparency and accountability in the management of oil revenue. At the same time, an effective implementation of the PRSP should raise the productivity of today's Sãotomeans through increases in basic health and education services, as well as higher physical and human capital called for in the poverty reduction strategy. With a better-trained labor force, the country would be ready to absorb future high-tech, capital-intensive, enterprises that might develop in the future, such as oil-sector related activities (that is, manufacturing and services enterprises supporting the development of the oil sector), offshore fishing, trans-shipment entrepôt services, specialized agriculture, and eco-tourism.

VII. Program Monitoring for 2005

51. **Technical Memorandum of Understanding (TMU)**. The program will be monitored using the definitions, data sources, and frequency of monitoring set out in the accompanying TMU. The government will make available to the Fund all necessary data, appropriately reconciled and on a timely basis, as specified in the TMU.

52. **Prior Actions**. The government will undertake actions prior to the IMF Board meeting to consider the request for a three-year arrangement under the PRGF, in order to ensure effective implementation of the economic strategy described in this memorandum (Table I.2).

53. **Performance criteria**. Table I.1 shows the quantitative performance criteria set for September and December 2005. Structural performance criteria and benchmarks for 2005 with corresponding dates are identified in Table I.2. In addition, the nonaccumulation of external payment arrears (as defined in the TMU) will constitute a continuous performance criterion, as will the standard injunctions against imposing or intensifying restrictions on current payments introducing or modifying multiple currency practices, concluding bilateral payments agreements that are inconsistent with Article VIII, or imposing or intensifying import restrictions for balance of payments reasons.

Table I.1. São Tomé and Príncipe: Performance Criteria for 2005

(In billions of dobras, unless otherwise specified)

	2005	
	end-Sept. Perf. criteria	end-Dec. Perf. criteria
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	-84.4	-130.6
2. Ceiling on domestic primary spending (cumulative from beginning of the year) 1/	223.9	329.4
3. Ceiling on changes in net domestic financing of the government (cumulative from beginning of year, in billions of dobras at program exchange rate) 2/ 3/	-27.6	0.8
4. Ceiling on changes in net domestic assets of the central bank (cumulative from beginning of year, in billions of dobras at program exchange rate) 2/ 3/	-18.5	9.9
5. Floor on changes in the net international reserves of the central bank (cummulative from beginning of the year, in millions of U.S. dollars) 4/	4.8	0.9
6. Ceiling on central government's outstanding external payment arrears (stock, in millions of U.S dollars) 5/	0.0	0.0
7. Ceiling on the contracting or guaranteeing of new non-concessional external debt with original maturity of more than one year by the central government or the BCSTP (cumulative from the beginning of the year, in millions of euros) 6/ 7/	1.7	1.7
8. Ceiling on the outstanding stock of external debt with original maturity of less than one year owed or guaranteed by the central government or the BCSTP (cumulative from the beginning of the year, in millions of U.S. dollars) 8/	15.0	15.0
Memorandum items:		
Oil signature bonuses (in millions of U.S. dollars)	49.2	49.2
Official external program support as defined in the TMU (in billions of dobras)	10.4	21.6

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

1/ Equal to government domestic expenditure, as defined in the TMU, excluding all interest payments.
2/ The ceiling will be adjusted downward (upward) by the cumulative negative (positive) deviations in external debt service and the cumulative positive (negative) deviation of actual from projected disbursements of external program support. The downward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.
3/ The ceiling will be adjusted downwards by the amount of accumulated domestic arrears.
4/ The floor on net international reserves will be adjusted upwards (downwards) by the cumulative negative (positive) deviation in external debt service, and the cumulative negative (positive) deviation of actual from projected disbursements of external program support. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.
5/ This is a continuous performance criterion.
6/ This performance criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received.
7/ With a grant element of less than 50 percent.
8/ The term “debt” has the meaning set forth in point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000.

Table I.2. Prior Actions, Structural Performance Criteria and Benchmarks for 2005

Prior actions for approval of new PRGF arrangement

- Obtain parliamentary passage of a 2005 budget with aggregate revenues, expenditures, and net domestic financing that are consistent with the MEFP.

- Receipt of the oil signature bonus on Block 1 (totaling US$49.2 million) and deposit of these funds in the government's National Oil Account held with the Federal Reserve Bank of New York.

Structural performance criteria

By end-July 2005, submit to the National Assembly a new tax code on personal income taxation broadening the tax base (to include bonuses, monetary premiums, and in-kind benefits) and updating the tax rate schedules to provide progressivity to the personal income tax system (MEFP, para. 13);

By end-July 2005, submit to the National Assembly a new code on corporate taxation that limits the granting of tax holidays to new licensed investors to a maximum of three years, with tax reductions only covering up to 75 percent of profit taxes due (MEFP, para. 13);

By end-July 2005, submit to the National Assembly a new tax procedural code establishing tax tribunals at different levels of government (regional and national) to handle tax issues and disputes, as well as penalties and fines for underpayment, late payment, and other tax violations (MEFP, para.14);

By end-July 2005, submit to the National Assembly a new investment code that provides equal treatment for domestic and foreign investors and is consistent with the new code on corporate taxation (MEFP, para. 40).

Structural benchmarks

By end-July 2005, establish a timetable for the reduction of outstanding payments arrears to the water and electricity company (EMAE) (MEFP, para.36).

By end-December 2005, complete feasibility studies on the privatization of ENASA and ENAPORT (MEFP, para. 38).

By end-July 2005, submit to the National Assembly new guidelines on urban property taxation to support the development of new official registries of the quantity, value, and ownership of urban real estate used in apportioning taxes (MEFP, para.14);

By end-July 2005, submit to the National Assembly new legislation on inheritance taxes that clarifies the tax rate and tax base applicable (MEFP, para.14).

By end-September 2005, submit to the National Assembly proposed legislation criminalizing money laundering and financing of terrorism (MEFP, para. 31).

By end-December 2005, develop the terms of reference for a study on land tenure, which would analyze, among other things, the economic effects from a lack of complete property rights for land-holders (MEFP, para. 41).

São Tomé and Príncipe

Technical Memorandum of Understanding

1. This technical note contains definitions and adjuster mechanisms that are intended to clarify the measurement of items in Table I.1, Quantitative Performance Criteria, PRGF Arrangement, 2005, attached to the Memorandum of Economic and Financial Policies. Unless otherwise specified, all quantitative performance criteria and benchmarks will be evaluated in terms of cumulative flows from December 31, 2004.

Provision of Data to the Fund

2. Data with respect to all variables subject to performance criteria and indicative benchmarks will be provided to Fund staff on a monthly basis with a lag of no more than four weeks for data on the net domestic assets and net international reserves of the Central Bank of São Tomé and Príncipe (BCSTP), and eight weeks for other data. The authorities will transmit promptly to Fund staff any data revisions. For variables that are relevant for assessing performance against program objectives but are not specifically defined in this memorandum, the authorities will consult with Fund staff as needed on appropriate measurement and reporting.

Definitions

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

4. **Government domestic revenue** comprises all tax and non-tax revenue of the government (in domestic and foreign currency), excluding foreign grants, the receipts from the local sale of crude oil received from Nigeria as in-kind grant, and any gross inflows to government on account of oil signature bonus payments. Revenue will be measured on a cash basis as reported in the table of government financial operations prepared by the Directorate of Budget and Directorate of Treasury in the Ministry of Planning and Finance.

5. **Domestic primary expenditure** comprises all government spending assessed on a commitment basis, excluding: (i) foreign-financed capital expenditure, (ii) expenditure under the overseas scholarship program that are externally-financed, and (iii) other foreign-financed current expenditures, for which data are reported by the Directorate of Budget and Directorate of Treasury. Reporting of government domestic expenditure will be based on the state budget execution prepared every month by the Directorate of Budget and Directorate of Treasury in the Ministry of Planning and Finance.

6. Within the above total, **pro-poor expenditure** refers to government outlays that, as it has been agreed with the IMF and World Bank staffs, have a direct effect in reducing

poverty. These expenditures, which includes both current and capital outlays, are defined as follows:

a. **Pro-poor current spending**: These cover the following ministries and expenditure categories (by budget code) as described in the matrix below, with items marked with an "x" representing social expenditures by the referred ministries.

Code	Description of current expenditure	MINISTRY OF EDUCATION AND CULTURE	MINISTRY OF HEALTH	MINISTRY OF LABOUR AND SOLIDARITY
01.00.00	Despesa com Pessoal	X	X	
02.01.05	Outros bens duradouros	X	X	
02.02.02	Combustíveis e lubrificantes	X	X	
02.02.04	Alimentação		X	
02.02.05	Medicamentos	X	X	
02.02.06	Roupas e calsados		X	
02.02.09	Outros bens não duradouros		X	
02.03.01.01	Agua e energia	X	X	
02.03.02	Conservação de bens		X	
02.03.06	Comunicações	X	X	
04.01.01	Orçamento do estado		X	
04.02.01	Instituições particulares		X	X
04.03.01	Particulares		X	X
04.04.02	Outras transferências para exterior			X
06.01.00	Ensino e formação	X		
06.04.01	Custos recorrentes de projectos	X	X	
06.04.04.02	Outros Diversos	X	X	

Expenditures on "combustiveis e lubrificantes" (fuels and lubricants) that are effected for administrative purposes are excluded. Likewise, "alimentacao" (food) and "roupas e calsados" (clothing and shoes) supplied to administrative staff are excluded.

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

c. **Reporting Requirements:** Data on execution of pro-poor current and capital spending will be provided on a quarterly basis to the staff by the Directorate of Budget (for current expenditure) and by the Directorate of Planning (for capital expenditure) at the Ministry of Planning and Finance.

7. The **domestic primary balance** is defined as the difference between government domestic revenue and noninterest government domestic expenditure. This balance for the year 2004 was assessed at dobras -128.1 billion, broken down as follows:

Government domestic revenue:	Db 165.0 billion
Less: government primary expenditure, excluding foreign-financed investment, foreign-financed scholarships, and transfers to the JDA:	Db 293.1 billion
Equals: Domestic primary balance:	Db -128.1 billion

8. **The program exchange rate** for the purposes of this memorandum will be Db10,104 per US dollar, which corresponds to the simple average of the buying and selling rates for the BCSTP for December 31, 2004. The exchange rate of the dobra against the euro at end-December 2004 was 12,314 and against the SDR was 15,558.

9. **Net domestic financing of the government** is defined as the change in net credit to government by the banking system—that is, the stock of all outstanding claims on the government held by the BCSTP, less all deposits held by the central government with the BCSTP, plus the stock of all outstanding claims on the government held by deposit money banks (DMBs)[13], less all deposits held by the central government with DMBs--as they are reported monthly by the BCSTP to the IMF. All foreign exchange denominated accounts will be converted to dobras at the program exchange rate. At end-December 2004, outstanding net credit to the government was assessed at dobras 35.8 billion, broken down as follows:

BCSTP credit, including use of IMF resources:	Db 83.6 billion
Less: government deposits with BCSTP:	Db 41.0 billion
Equal: Net credit to government by the BCSTP:	Db 42.6 billion
Plus: DMBs credit:	Db 0.0 billion
Less: government deposits with DMBs (including counterpart funds):	Db 6.9 billion
Equals: Net domestic financing of the government:	Db 35.8 billion

[13] Deposit money banks (DMBs) refers to Other Depository Corporations as stated in the Monetary and Financial Statistics Manual.

10. **Base money** is defined as the sum of currency issued—which consists of currency outside banks and cash in vaults—and bank reserves. Bank reserves refer to reserves of commercial banks held with the central bank, and include reserves in excess of the legal reserve requirement. At end-December 2004, base money was assessed at dobras 119.2 billion, calculated as follows:

Currency issued:		Db 67.2 billion
Of which:	Cash in vaults:	Db 7.2 billion
	Currency outside banks:	Db 60.0 billion
Plus: Bank Reserves:		Db 52.1 billion
Equals: Base Money:		Db 119.2 billion

11. **Net international reserves** (NIR) of the BCSTP are defined for program monitoring purposes as short term-term foreign assets of the BCSTP minus short-term external liabilities. All short-term foreign assets that are not fully convertible external assets readily available to and controlled by the BCSTP (i.e., they are pledged or otherwise encumbered external assets, including, but not limited to, the HIPC umbrella SDR account, and assets used as collateral or guarantees for third party liabilities) will be excluded from the definition of NIR. All values are to be converted to U.S. dollars at actual market exchange rates prevailing at the test date. At end-December 2004, NIR was assessed at dobras 169.2 billion, calculated as follows:

Net Foreign Assets:		Db 189.3 billion
Less:	Other foreign assets:	Db 49.5 billion
Plus:	Other liabilities:	Db -29.4 billion
Equals: Net International Reserves:		Db 169.2 billion
Of which:	Gross reserves:	Db 197.1 billion
	Short-term liabilities:	Db - 27.9 billion

12. **Net domestic assets** of the central bank of São Tomé and Príncipe are defined as the difference between base money and net foreign assets of the BCSTP. All foreign denominated accounts will be converted to dobras at the program exchange rate. At end-December 2004, net domestic asset was assessed at dobras -70.0 billion, calculated as follows:

Base Money:	Db 119.2 billion
Less: Net Foreign Assets:	Db 189.3 billion
Equals: Net domestic assets of the BCSTP:	Db -70.0 billion

13. The performance criterion on **short-term external debt** refers to the outstanding stock of external debt with original maturity of one year or less, including overdraft positions and debt owed or guaranteed by the government or the BCSTP.[14] At end-December 2004, the stock of short-term external debt stood at US$1.0 million.

14. The performance criterion on **nonconcessional medium- and long-term external debt** refers to the contracting or guaranteeing of external debt with original maturity of more than one year by the government of BCSTP.[15] [16] Debt reschedulings and restructurings are excluded from the ceilings set on nonconcessional borrowing. Medium- and Long-term debt will be reported by the Debt Management Unit of the Ministry of Finance and Planning and (as appropriate) by the BCSTP, measured in US dollars at current exchange rates. The government of São Tomé and Príncipe will consult with Fund staff before contracting obligations if it is uncertain as to whether those obligations are included in the performance criterion limits. At end-December 2004, nonconcessional medium- and long-term external debt stood at US$15 million.

[14] The term "debt" is defined in accordance with point 9 of the Guidelines on Performance Criteria with respect to Foreign Debt (Decision No. 12274-(00/85) August 24, 2000).

[15] This performance criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000 but also to commitments contracted or guaranteed for which value has not been received.

[16] The concessionality of loans is assessed according to the reference interest rate by currency published by the Development assistance Committee of the Organization for Economic Cooperation and Development (OECD). For loans of terms of no less than 15 years, the ten-year average of commercial interest reference rates (CIRR) for the currency in which the loan is denominated will be used. For loans of shorter terms, the six month average will apply. A loan is deemed to be on concessional terms if, on the initial date of disbursement, the ratio of the present value of the loan, calculated on the basis of the reference interest rate, to the nominal value of the loan is less than 50 percent (in other words, a grant element of at least 50 percent, excluding Fund resources). For currencies with no available reference interest rates, the SDR rate will be used.

15. The nonaccumulation of new **external payment arrears** is a continuous performance criterion. Government external payment arrears are defined as all unpaid external public debt obligations, according to the data established by the Debt Management Unit of the Ministry of Planning and Finance and (as appropriate) by the BCSTP, with the exception of arrears pending rescheduling arrangements. Debt would be deemed to be in arrears when it has not been paid by the time it is due, unless the definition of an arrear has been otherwise contractually defined. The performance criterion relating to external arrears does not apply to external arrears pending the conclusion of a debt-rescheduling agreement with the Paris Club. The outstanding stock of external arrears pending debt-rescheduling agreement at end-December 2004 stood at US$18 million.

16. **Official external program support** is defined as grants and loans provided by foreign official entities that are received by the budget—**excluding project grants and loans**—and other exceptional financing. Amounts assumed in the program consistent with this definition are shown in the memorandum item entitled "external program support" of Table I.1. For 2004, official external program support totaled US$7.1 million, being the sum of non-project grants (US$2 million) and program loans (US$5.1 million).

Adjusters

17. **Deviations in official external program support** from the amounts programmed in Table I.1. will trigger adjusters for domestic financing of the government, net domestic assets of the BCSTP and net international reserves as indicated below. These and other adjusters as set out below will be measured cumulatively from December 31, 2004.

18. **Ceilings on net domestic financing (NDF) of the government and net domestic assets (NDA) of the BCSTP.** Monthly differences between projected and actual official external program support and external debt service payments in foreign exchange will be converted to dobras at the actual monthly exchange rate and cumulated to the test date. The ceilings on NDF and NDA will be reduced by the sum of: (i) excess official external program support; and (ii) the shortfall in external debt service payments. Both ceilings will be increased by 100 percent of any cumulative shortfall in official external program support or excess in external debt service. The downward adjustment to NDF and NDA for higher than programmed official external program support will not take place to the extent that additional external program support is used to accommodate higher capital outlays by the government, up to US$1 million, converted to dobras at actual exchange rates, as indicated in Table I.1.

19. **Floor on net international reserves (NIR) of the BCSTP.** Quarterly difference between projected and actual official external program support and external debt service payments will be converted to U.S. dollars at the actual exchange rates prevailing at the test date. The floor on NIR will be raised by the sum of: (i) excess external program support and (ii) any shortfall in external debt service payments. The upward adjustment to NIR for higher than programmed official external program support will not take place to the extent that additional external program support is used to accommodate higher capital outlays by the

government, up to US$1 million, converted to dobras at actual exchange rates, as indicated in Table I.1.

Data Reporting

20. The following information will be provided to the IMF staff for the purpose of monitoring the program. Except for net domestic assets and net international reserves, which data are to be provided by the BCSTP within four weeks at the end of each month, other monetary data will be furnished within eight weeks after the end of each month for monthly data, within eight weeks after the end of each quarter for quarterly data, and within eight weeks after the end of each year for annual data.

i. Fiscal data

The Directorate of Budget at the Ministry of Planning and Finance will provide to IMF staff:

- Monthly data on central government operations for revenues, expenditure and financing
- Monthly detailed tax and non-tax revenues
- Monthly detailed current and capital expenditure data
- Quarterly data on official external program support (non-project)
- Quarterly data on the execution of the public investment program (PIP) and sources of financing
- Quarterly data on project grant disbursement (HIPC and Non-HIPC)
- Quarterly data on project loans disbursement

ii. Monetary data

The BCSTP will provide the IMF staff:

- Weekly data on exchange rates
- Monthly data on interest rates
- Monthly balance sheet data of BCSTP (in BCSTP and IMF formats)
- Monthly balance sheet data of individual deposit money banks (in BCSTP and IMF formats)
- Monthly consolidated balance sheet data of deposit money banks (in BCSTP and IMF formats)
- Monthly monetary survey (in BCSTP and IMF formats)
- Monthly central bank foreign exchange balance (Balança cambial)
- Latest position of NIR and Liquid Reserves of the BCSTP (last available; monthly)

iii. External debt data

The Debt Management Unit at the Ministry of Planning and Finance will provide the IMF staff:

- Monthly data on amortization of external debt (HIPC and Non-HIPC)
- Monthly data on paid interest on external debt (HIPC and Non-HIPC)
- Monthly data on disbursements external project and BOP support loans

iv. National accounts and trade statistics

The National Institute of Statistics will provide the IMF staff:

- Monthly consumer price index data
- Monthly data on imports as reported by Customs (value and import taxes collected)
  Monthly commodity export values

SÃO TOMÉ AND PRÍNCIPE: DEBT SUSTAINABILITY ANALYSIS

1. This appendix analyses the trends of public and publicly guaranteed external debt implied in the government's medium-term economic and financial program[17]. While the debt rescheduling, including the retroactive Cologne treatment from bilateral creditors, and attainment of HIPC completion point results in a significant improvement in the debt outlook, the debt sustainability analysis (DSA) shows that São Tomé and Príncipe's external debt remains high when gauged against the standard benchmarks of debt-to-GDP, debt-to-exports, and debt-to-government revenue ratios. The debt ratios are highly vulnerable to exchange rate depreciation, changes in export growth, and changes in non-debt creating flows (i.e., foreign grants and FDI).

A. Public Debt Sustainability

2. **In the baseline scenario, São Tomé and Príncipe's public debt outlook shows steady improvements over the medium-term.** Reflecting an austere public expenditure envelope underpinning the government's medium-term reform program, the NPV of public debt-to-GDP ratio falls from 131 percent in 2005 to 124 in 2007, and to 95 percent in 2011 (Table 1a). Furthermore, in 2012, the ratio drops sharply to 13 percent due to the impact of the start of oil production. Under the baseline scenario the NPV of debt-to-revenue ratio improves significantly in 2006—reflecting the impact of HIPC completion point—and remains broadly stable until it drops significantly in 2012 and beyond. The debt service-to-revenue ratio (estimated at 6 percent in 2004) also remains stable through 2011; it increases sharply in 2012—when the outstanding debt to Nigeria (totaling US$15 million) falls due—before declining sharply thereafter.

3. **The debt ratios are particularly vulnerable to external shocks**. Sensitivity analysis using the standard IMF Low Income Country DSA template indicates that under the most extreme stress test, defined as a 30 percent depreciation of the dobra exchange rate (measured in terms of US dollars), the NPV of debt-to-GDP ratio increases to 209 percent in 2005, compared to 131 percent for the same year under the baseline scenario (Table 1b). This reflects the fact that São Tomé and Príncipe's public debt is totally denominated in foreign currency. Figures 1 and 2 also show the results of a scenario assuming no fiscal reform (defined to include an unchanged primary fiscal balance from its 2004 percent-of-GDP-level), which, by definition, worsens the debt indicators vis-à-vis the baseline. This highlights the importance of fiscal reform in improving debt outlook.

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[17] The baseline scenario is the reform scenario. It is based on the following assumptions: (i) a Paris Club rescheduling in mid-2005, providing São Tomé and Príncipe a retroactive Cologne treatment from decision point (December 2000), with comparable treatment by other bilateral creditors, and (ii) the attainment of HIPC completion point in the first half of 2006.

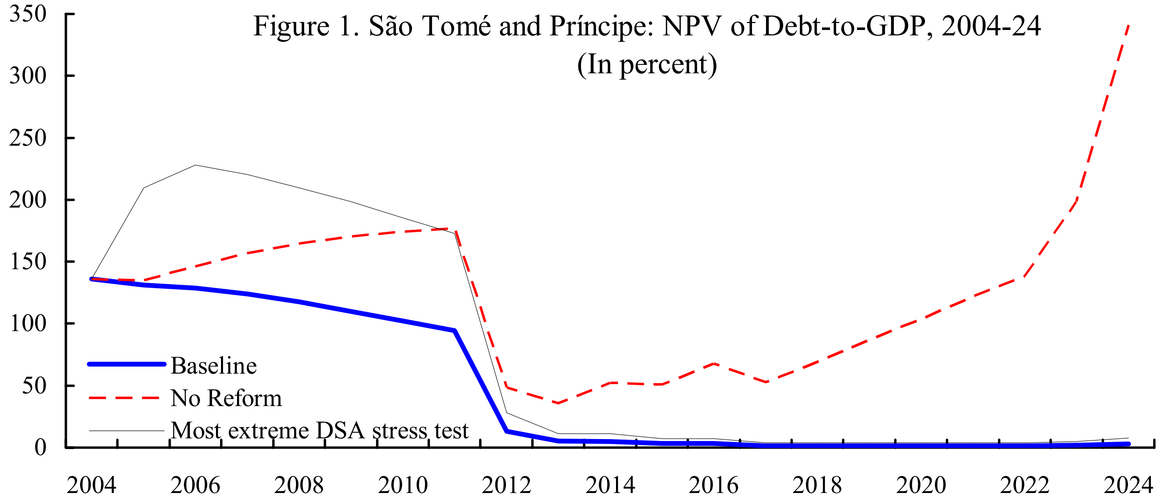


Figure 1. São Tomé and Príncipe: NPV of Debt-to-GDP, 2004-24
(In percent)

Source: Staff projections and simulations.

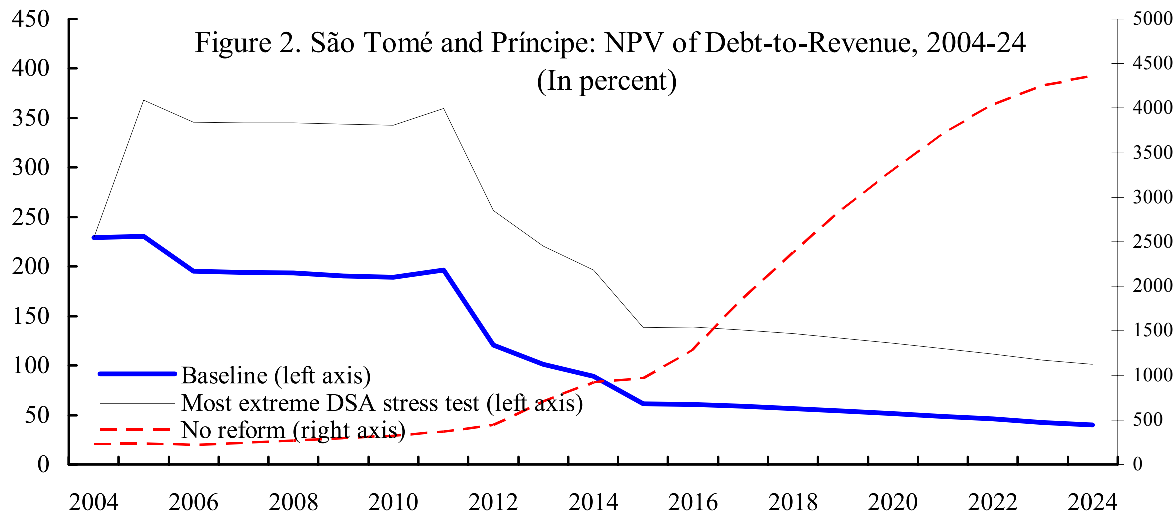


Figure 2. São Tomé and Príncipe: NPV of Debt-to-Revenue, 2004-24
(In percent)

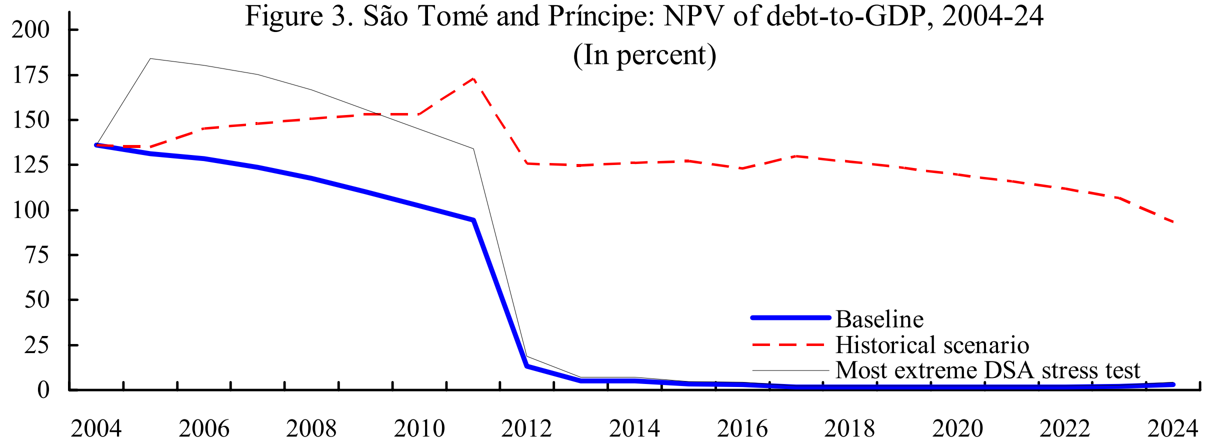
Source: Staff projections and simulations.

B. External Debt Sustainability

4. **The NPV of debt-to-exports ratio improves steadily in the baseline scenario.** The NPV of debt-to-export ratio decreases from 326 percent in 2004 to 298 percent in 2007, to 276 percent in 2011 (Table 2a). The ratio falls below the 150 percent threshold only in 2012, when oil production and exports begin. The debt service-to-exports ratio increases between 2005 and 2009 but it starts to decline thereafter.

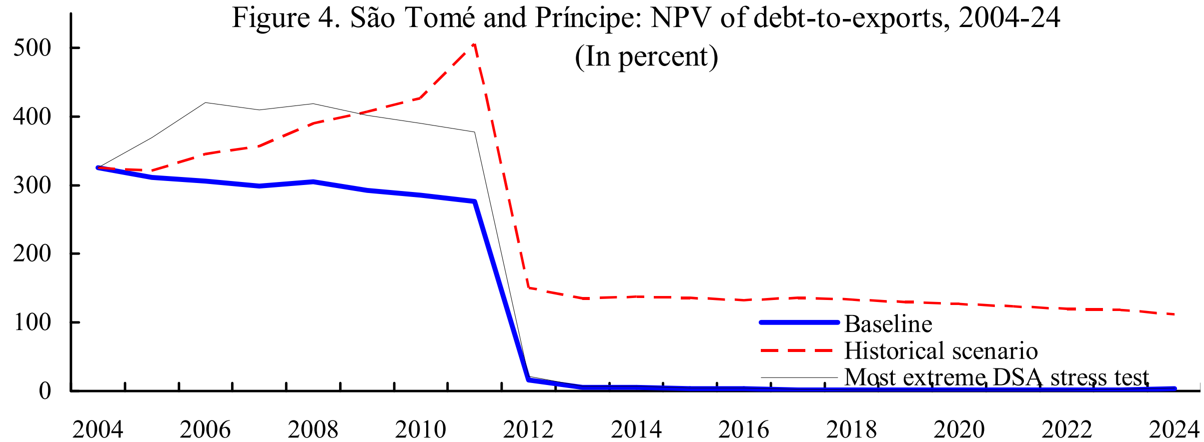
5. **In addition to exchange rate fluctuations, the external debt outlook is vulnerable to declining exports and non-debt creating flows (that is, foreign grants and FDI).** Sensitivity analysis using the Low Income Country DSA template indicates that the most extreme shock on the NPV of debt-to-export ratio results from a fall in exports. Specifically, a decline in the export level in 2005–06 by one standard deviation from historical levels (that is, the average export level in 1995–2004) pushes the ratio to 421 percent in 2006 compared with 306 percent under the baseline scenario (Figure 4; Table 2b). The NPV of debt-to-export ratio also deteriorates significantly under the "historical scenario", which assumes that the main macroeconomic variables—real GDP, export value, U.S. dollar GDP deflator, and net non-debt creating flows—were subject to one half standard deviation shocks from their historical levels (that is, their average levels for 1995–2004). Under this scenario, the ratio rises to 346 percent in 2006. The debt outlook worsens, albeit less sharply, when non-debt creating flows decline; however, the impact is felt with a one-year lag.

Figure 3. São Tomé and Príncipe: NPV of debt-to-GDP, 2004-24
(In percent)



Source: Staff projections and simulations.

Figure 4. São Tomé and Príncipe: NPV of debt-to-exports, 2004-24
(In percent)



Source: Staff projections and simulations.

Table 1a. São Tomé and Príncipe: Public Sector Debt Sustainability Framework, Baseline Scenario, 2001-2024

(In percent of GDP, unless otherwise indicated)

	Estimate						Projections											
	2001	2002	2003	2004	Historical Average 5/	Standard Deviation 5/	2005	2006	2007	2008	2009	2010	2005-10 Average	2011	2012	2015	2024	2011-24 Average
Public sector debt 1/	**590.8**	**532.5**	**491.8**	**468.0**			**425.6**	**336.7**	**298.2**	**261.0**	**226.2**	**195.6**		**168.6**	**31.5**	**6.5**	**3.6**	
o/w foreign-currency denominated	590.8	532.5	491.8	468.0			425.6	336.7	298.2	261.0	226.2	195.6		168.6	31.5	6.5	3.6	
Change in public sector debt	10.5	-58.2	-40.8	-23.8			-42.4	-88.9	-38.5	-37.2	-34.8	-30.5		-27.1	-137.1	-4.2	1.2	
Identified debt-creating flows	67.9	-56.7	-38.6	-8.7			-10.7	-50.0	-38.7	-39.3	-33.2	-31.9		-28.5	-135.9	-4.2	1.2	
Primary deficit	18.1	14.7	15.6	25.0	17.8	4.8	18.6	4.9	0.9	1.1	0.2	0.6	4.4	0.4	-1.0	0.0	0.0	-0.1
Revenue and grants	59.0	50.5	58.1	59.3			56.9	65.9	63.8	60.8	57.8	54.1		48.1	10.9	5.3	7.8	
of which : grants	37.8	27.2	32.5	30.9			28.2	33.2	31.2	30.0	27.2	23.7		19.1	4.0	0.4	0.0	
Primary (noninterest) expenditure	77.0	65.2	73.7	84.3			75.5	70.8	64.7	61.9	58.0	54.7		48.4	9.9	5.2	7.8	
Automatic debt dynamics	54.6	-67.1	-48.5	-28.9			-21.1	-43.1	-29.7	-31.5	-25.4	-25.3		-22.0	-133.5	-3.8	1.4	
Contribution from interest rate/growth differential	-31.6	-30.6	-28.2	-26.5			-24.1	-26.0	-22.3	-22.3	-20.6	-18.8		-13.8	-133.9	-4.0	1.4	
of which : contribution from average real interest rate	-9.3	-7.4	-7.7	-8.5			-9.6	-7.7	-4.7	-4.1	-3.5	-3.0		0.7	-0.7	-0.1	-0.1	
of which : contribution from real GDP growth	-22.3	-23.3	-20.5	-18.0			-14.5	-18.3	-17.6	-18.2	-17.1	-15.8		-14.5	-133.3	-3.9	1.4	
Contribution from real exchange rate depreciation	86.2	-36.5	-20.3	-2.3			3.0	-17.1	-7.4	-9.2	-4.8	-6.5		-8.3	0.4	...	...	
Other identified debt-creating flows	-4.8	-4.3	-5.8	-4.9			-8.2	-11.8	-9.8	-8.9	-8.1	-7.2		-6.9	-1.5	-0.3	-0.2	
Privatization receipts (negative)	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	0.0	0.0	
Debt relief (HIPC and other)	-4.8	-4.3	-5.8	-4.9			-8.2	-11.8	-9.8	-8.9	-8.1	-7.2		-6.9	-1.5	-0.3	-0.2	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	0.0	0.0	
Residual, including asset changes	-57.4	-1.6	-2.2	-15.1			-31.6	-38.9	0.2	2.1	-1.6	1.3		1.4	-1.1	0.0	0.0	
NPV of public sector debt	**...**	**...**	**...**	**135.9**			**131.2**	**128.6**	**123.8**	**117.7**	**110.1**	**102.3**		**94.6**	**13.1**	**3.2**	**3.1**	
o/w foreign-currency denominated	...	...	...	135.9			131.2	128.6	123.8	117.7	110.1	102.3		94.6	13.1	3.2	3.1	
o/w external	...	...	...	135.9			131.2	128.6	123.8	117.7	110.1	102.3		94.6	13.1	3.2	3.1	
NPV of contingent liabilities (not included in public sector debt)	...	...	...	...			...	...	...	...	...	...		...	...	...	...	
Gross financing need 2/	24.0	19.8	19.8	28.8			23.8	9.4	6.3	6.1	5.1	5.3		4.4	2.0	0.1	0.1	
NPV of public sector debt-to-revenue ratio (in percent) 3/	...	...	...	229.3			230.5	195.3	194.0	193.7	190.7	189.0		196.7	120.8	61.5	40.1	
o/w external	...	...	...	229.3			230.5	195.3	194.0	193.7	190.7	189.0		196.7	120.8	61.5	40.1	
Debt service-to-revenue ratio (in percent) 3/ 4/	10.1	10.0	7.3	6.3			4.6	3.8	5.5	5.3	5.6	5.8		5.3	27.2	2.6	2.1	
Primary deficit that stabilizes the debt-to-GDP ratio	7.6	72.9	56.4	48.8			60.9	93.8	39.4	38.3	35.1	31.1		27.5	136.1	4.2	-1.2	
Key macroeconomic and fiscal assumptions																		
Real GDP growth (in percent)	4.0	4.1	4.0	3.8	2.8	1.1	3.2	4.5	5.5	6.5	7.0	7.5	5.7	8.0	377.6	57.6	-37.4	47.2
Average nominal interest rate on forex debt (in percent)	0.5	0.3	0.3	0.3	1.6	1.6	0.3	0.1	0.5	0.5	0.5	0.6	0.4	0.4	0.4	0.5	1.0	0.6
Average real interest rate on domestic currency debt (in percent)																		
Real exchange rate depreciation (in percent, + indicates depreciation)	15.2	-6.5	-4.0	-0.5	26.3	48.6	...	...	...	...	...	...		...	...	...	...	...
Inflation rate (GDP deflator, in percent)	9.8	10.8	9.2	9.7	5.2	4.1	14.8	14.8	11.8	9.5	8.8	7.3	11.2	5.2	0.0	0.0	0.0	0.4
Growth of real primary spending (deflated by GDP deflator, in percent)	33.9	-11.9	17.6	18.7	33.9	33.9	-7.6	-2.1	-3.6	1.9	0.3	1.5	-1.6	-4.4	-2.7	47.4	4.6	10.1

Sources: Staff simulations.

1/ Covers general government. Debt stock are on a gross basis.

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

3/ Revenues including grants.

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

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

Table 1b. São Tomé and Príncipe: Sensitivity Analyses for Key Indicators of Public Sector Debt , 2004-2024

	Est.	Projections													
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2015	2020	2021	2022	2023	2024
								NPV of Debt-to-GDP Ratio 1/							
Baseline	136	131	129	124	118	110	102	95	13	3	2	2	2	2	3
A. Alternative scenarios															
A1. Real GDP growth and primary balance are at historical averages	136	131	140	143	142	141	138	136	100	94	92	92	91	90	88
A2. Primary balance is unchanged from 2004	136	135	146	157	164	170	174	177	48	51	104	122	138	198	341
A3. Permanently lower GDP growth 2/	136	132	130	126	121	114	106	99	14	4	2	2	2	3	5
B. Bound tests															
B1. Real GDP growth is at historical average minus one standard deviations in 2005-2006	136	133	136	132	127	120	112	105	15	4	2	2	3	3	6
B2. Primary balance is at historical average minus one standard deviations in 2005-2006	136	134	143	138	131	123	115	106	16	4	2	2	2	2	4
B3. Combination of B1-B2 using one half standard deviation shocks	136	133	144	138	131	122	113	104	15	4	2	2	2	2	3
B4. One time 30 percent real depreciation in 2005	136	209	228	220	210	199	185	173	28	7	4	4	4	5	8
B5. 10 percent of GDP increase in other debt-creating flows in 2005	136	141	138	132	125	117	108	100	14	3	2	2	2	2	3
								NPV of Debt-to-Revenue Ratio 3/							
Baseline	229	231	195	194	194	191	189	197	121	62	51	49	46	43	40
A. Alternative scenarios															
A1. Real GDP growth and primary balance are at historical averages	229	230	211	219	224	230	236	258	333	704	1287	1291	1287	1110	1029
A2. Primary balance is unchanged from 2004	229	238	222	246	271	295	322	369	444	969	3302	3712	4041	4250	4368
A3. Permanently lower GDP growth 2/	229	231	197	197	198	196	195	205	128	68	66	65	64	63	63
B. Bound tests															
B1. Real GDP growth is at historical average minus one standard deviations in 2005-2006	229	233	202	203	204	203	204	214	137	76	76	75	74	72	72
B2. Primary balance is at historical average minus one standard deviations in 2005-2006	229	235	217	217	216	213	212	221	143	73	60	57	54	50	47
B3. Combination of B1-B2 using one half standard deviation shocks	229	233	215	214	212	209	206	215	136	68	56	53	50	46	44
B4. One time 30 percent real depreciation in 2005	229	368	346	345	345	344	342	360	257	139	122	117	112	106	101
B5. 10 percent of GDP increase in other debt-creating flows in 2005	229	248	209	207	206	202	200	209	131	66	54	51	48	45	42
								Debt Service-to-Revenue Ratio 3/							
Baseline	6	5	4	6	5	6	6	5	27	3	2	2	1	1	2
A. Alternative scenarios															
A1. Real GDP growth and primary balance are at historical averages	6	5	4	6	6	7	8	8	62	51	147	159	171	165	180
A2. Primary balance is unchanged from 2004	6	5	4	6	7	8	9	9	32	21	96	115	137	155	185
A3. Permanently lower GDP growth 2/	6	5	4	5	5	5	6	5	27	2	2	2	2	2	3
B. Bound tests															
B1. Real GDP growth is at historical average minus one standard deviations in 2005-2006	6	5	4	6	5	6	6	5	28	3	2	2	2	2	3
B2. Primary balance is at historical average minus one standard deviations in 2005-2006	6	5	4	6	6	6	6	6	28	3	2	2	2	2	2
B3. Combination of B1-B2 using one half standard deviation shocks	6	5	4	6	6	6	6	5	28	3	2	1	1	1	2
B4. One time 30 percent real depreciation in 2005	6	5	4	7	6	6	7	6	28	3	2	2	1	2	2
B5. 10 percent of GDP increase in other debt-creating flows in 2005	6	5	4	5	5	5	6	5	27	2	1	1	1	1	2

Sources: Stafff projections and simulations.

1/ By the year 2023 real GDP growth slows down significantly due to the projected decline in petroleum production.
2/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of 20 (i.e., the length of the projection period).
3/ Revenues are defined inclusive of grants.

Table 2a. São Tomé and Príncipe: External Debt Sustainability Framework, Baseline Scenario, 2001-2004 1/
(In percent of GDP, unless otherwise indicated)

	Estimate						Projections											
	2001	2002	2003	2004	Historical Average 5/	Standard Deviation 5/	2005	2006	2007	2008	2009	2010	2005-10 Average	2011	2012	2015	2024	2011-24 Average
External debt (nominal) 1/	**590.8**	**532.5**	**491.8**	**468.0**			**425.6**	**336.7**	**298.2**	**261.0**	**226.2**	**195.6**		**168.6**	**31.5**	**6.5**	**3.6**	
o/w public and publicly guaranteed (PPG)	590.8	532.5	491.8	468.0			425.6	336.7	298.2	261.0	226.2	195.6		168.6	31.5	6.5	3.6	
Change in external debt	10.5	-58.2	-40.8	-23.8			-42.4	-88.9	-38.5	-37.2	-34.8	-30.5		-27.1	-137.1	-4.2	1.2	
Identified net debt-creating flows	1.4	-46.4	-35.6	-18.0			2.0	-9.8	-11.5	-11.9	-12.6	-9.8		-44.6	-154.6	-58.2	-42.9	
Non-interest current account deficit	**22.9**	**22.9**	**18.8**	**26.0**	**18.3**	**10.4**	**27.2**	**23.1**	**27.3**	**32.0**	**33.5**	**32.8**		**212.9**	**27.1**	**-48.6**	**-41.0**	-12.4
Deficit in balance of goods and services	53.3	46.3	50.0	53.6			55.7	57.3	61.4	63.4	61.2	58.1		235.6	-27.3	-84.8	-72.3	
Exports	38.1	40.3	41.0	41.8			42.1	42.0	41.5	38.6	37.6	35.9		34.2	83.9	93.8	83.5	
Imports	91.4	86.6	91.0	95.4			97.7	99.3	102.9	101.9	98.8	93.9		269.8	56.6	9.1	11.2	
Net current transfers (negative = inflow)	-39.1	-30.8	-37.3	-33.9	-40.3	13.7	-34.3	-40.6	-39.1	-35.9	-33.1	-29.7		-27.0	-5.5	-0.8	-0.6	-4.5
Other current account flows (negative = net inflow)	8.7	7.4	6.1	6.3			5.8	6.4	5.0	4.6	5.3	4.4		4.4	60.0	36.9	31.9	
Net FDI (negative = inflow)	**-6.8**	**-6.6**	**-5.8**	**-5.4**	**-6.0**	**2.5**	**-12.3**	**-15.8**	**-23.3**	**-27.7**	**-30.8**	**-28.4**		**-244.3**	**-49.0**	**-5.7**	**-3.4**	-40.2
Endogenous debt dynamics 2/	**-14.7**	**-62.7**	**-48.6**	**-38.6**			**-12.9**	**-17.1**	**-15.5**	**-16.3**	**-15.2**	**-14.1**		**-13.2**	**-132.7**	**-3.9**	**1.5**	
Contribution from nominal interest rate	2.4	1.7	1.4	1.3			1.0	0.4	1.4	1.3	1.2	1.1		0.7	0.1	0.0	0.0	
Contribution from real GDP growth	-22.5	-21.6	-19.3	-17.2			-13.9	-17.6	-16.9	-17.5	-16.4	-15.2		-13.9	-132.9	-3.9	1.4	
Contribution from price and exchange rate changes	5.4	-42.8	-30.7	-22.7			...	...	...	...	...	...		...	...	...	...	
Residual (3-4) 3/	**9.1**	**-11.8**	**-5.2**	**-5.8**			**-44.4**	**-79.1**	**-27.0**	**-25.3**	**-22.3**	**-20.8**		**17.5**	**17.5**	**54.0**	**44.1**	
o/w exceptional financing	-9.3	-13.3	-12.6	-12.6			11.9	-13.6	-11.4	-9.6	-8.1	-7.2		-6.9	-1.5	-0.3	-0.2	
NPV of external debt	...	...	...	135.9			131.2	128.6	123.8	117.7	110.1	102.3		94.6	13.1	3.2	3.1	
In percent of exports	...	...	...	325.5			311.6	306.2	298.4	305.1	292.9	285.2		276.4	15.7	3.5	3.7	
NPV of PPG external debt	**...**	**...**	**...**	**135.9**			**131.2**	**128.6**	**123.8**	**117.7**	**110.1**	**102.3**		**94.6**	**13.1**	**3.2**	**3.1**	
In percent of exports	...	...	...	325.5			311.6	306.2	298.4	305.1	292.9	285.2		276.4	15.7	3.5	3.7	
Debt service-to-exports ratio (in percent)	15.6	12.5	10.3	9.0			6.2	6.0	8.5	8.4	8.5	8.7		7.4	3.5	0.1	0.2	
PPG debt service-to-exports ratio (in percent)	15.6	12.5	10.3	9.0			6.2	6.0	8.5	8.4	8.5	8.7		7.4	3.5	0.1	0.2	
Total gross financing need (billions of U.S. dollars)	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	-0.1	-1.4	-1.4	
Non-interest current account deficit that stabilizes debt ratio	12.4	81.1	59.6	49.8			69.5	112.0	65.8	69.2	68.3	63.3		240.0	164.2	-44.4	-42.2	
Key macroeconomic assumptions																		
Real GDP growth (in percent)	4.0	4.1	4.0	3.8	2.8	1.1	3.2	4.5	5.5	6.5	7.0	7.5	5.7	8.0	377.6	57.6	-37.4	65.4
GDP deflator in US dollar terms (change in percent)	-0.9	7.8	6.1	4.8	0.9	7.0	4.4	4.3	4.2	4.0	4.4	4.0	4.2	4.0	0.3	0.3	0.3	0.8
Effective interest rate (percent) 4/	0.4	0.3	0.3	0.3	1.0	0.8	0.2	0.1	0.5	0.5	0.5	0.5	0.4	0.4	0.4	0.5	1.0	0.5
Growth of exports of G&S (US dollar terms, in percent)	17.6	18.6	12.2	10.9	9.7	16.0	8.6	8.7	8.5	2.9	8.9	6.7	7.4	7.1	1,075.0	61.7	-42.1	154.3
Growth of imports of G&S (US dollar terms, in percent)	16.2	6.4	15.9	14.1	5.5	17.4	10.4	10.7	13.9	9.7	8.2	6.3	9.9	222.6	0.5	-35.9	3.9	31.0
Grant element of new public sector borrowing (including IMF; in percent)	...	...	...	...	...	...	47.7	47.6	47.6	49.5	51.9	51.9	49.4	51.9	51.9	51.9	51.9	51.9
Grant element of new public sector borrowing (excluding IMF; in percent	...	...	...	...	...	...	51.9	51.9	51.9	51.9	51.9	51.9	51.9	51.9	51.9	51.9	51.9	51.9
Memorandum item:																		
Nominal GDP (billions of US dollars)	0.0	0.1	0.1	0.1			0.1	0.1	0.1	0.1	0.1	0.1		0.1	0.6	2.6	3.1	

Source: Staff simulations.

1/ External public debt only.
2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.
3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
4/ Current-year interest payments devided by previous period debt stock.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2b. São Tomé and Príncipe: Sensitivity Analyses for Key Indicators of Public and Publicly Guaranteed External Debt, 2004-2024
(In percent)

	Est.	Projections													
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2015	2020	2021	2022	2023	2024
							NPV of debt-to-GDP ratio 1/								
Baseline	136	131	129	124	118	110	102	95	13	3	2	2	2	2	3
A. Alternative Scenarios															
A1. Key variables at their historical averages in 2004-24 2/	136	135	145	148	151	153	153	173	126	127	120	116	112	107	94
A2. New public sector loans on less favorable terms in 2004-24 3/	136	131	131	128	123	116	109	102	15	4	2	2	2	3	4
B. Bound Tests															
B1. Real GDP growth at historical average minus one standard deviation in 2005-06	136	133	134	129	123	115	107	99	14	3	2	2	2	2	3
B2. Export value growth at historical average minus one standard deviation in 2005-06 4/	136	134	131	126	120	112	104	96	13	3	1	1	1	2	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2005-06	136	146	159	153	146	136	127	117	16	4	2	2	2	2	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2005-06 5/	136	139	136	131	124	116	108	99	14	3	2	1	1	2	3
B5. Combination of B1-B4 using one-half standard deviation shocks	136	142	153	147	139	130	121	112	15	4	2	2	2	2	3
B6. One-time 30 percent nominal depreciation relative to the baseline in 2005 6/	136	184	181	175	167	156	145	134	19	5	2	2	2	3	4
							NPV of debt-to-exports ratio								
Baseline	326	312	306	298	305	293	285	276	16	3	2	2	2	2	4
A. Alternative Scenarios															
A1. Key variables at their historical averages in 2004-23 2/	326	321	346	357	390	407	426	506	150	136	127	123	120	118	112
A2. New public sector loans on less favorable terms in 2004-23 3/	326	312	311	308	319	309	305	299	18	4	2	2	2	3	5
B. Bound Tests															
B1. Real GDP growth at historical average minus one standard deviation in 2005-06	326	316	306	299	305	293	285	277	16	3	2	2	2	2	4
B2. Export value growth at historical average minus one standard deviation in 2005-06 4/	326	369	421	410	418	401	390	378	21	5	2	2	2	3	4
B3. US dollar GDP deflator at historical average minus one standard deviation in 2005-06	326	347	307	299	306	294	286	277	16	3	2	2	2	2	4
B4. Net non-debt creating flows at historical average minus one standard deviation in 2005-06 5/	326	330	324	315	322	308	300	289	17	4	2	2	2	2	3
B5. Combination of B1-B4 using one-half standard deviation shocks	326	334	351	342	349	335	326	315	18	4	2	2	2	2	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2005 6/	326	437	306	301	308	295	288	279	16	3	2	2	2	2	4
							Debt service ratio								
Baseline	9	6	6	8	8	9	9	7	4	0	0	0	0	0	0
A. Alternative Scenarios															
A1. Key variables at their historical averages in 2004-23 2/	9	7	7	10	11	12	15	16	28	9	18	20	23	27	34
A2. New public sector loans on less favorable terms in 2004-23 3/	9	6	6	9	9	10	11	9	4	0	0	0	0	0	0
B. Bound Tests															
B1. Real GDP growth at historical average minus one standard deviation in 2005-06	9	6	6	9	9	9	10	10	4	0	0	0	0	0	0
B2. Export value growth at historical average minus one standard deviation in 2005-06 4/	9	7	8	12	12	13	14	14	5	0	0	0	0	0	1
B3. US dollar GDP deflator at historical average minus one standard deviation in 2005-06	9	7	6	9	9	9	10	10	4	0	0	0	0	0	0
B4. Net non-debt creating flows at historical average minus one standard deviation in 2005-06 5/	9	6	6	9	9	9	11	11	4	0	0	0	0	0	0
B5. Combination of B1-B4 using one-half standard deviation shocks	9	7	7	10	10	11	12	12	5	0	0	0	0	0	0
B6. One-time 30 percent nominal depreciation relative to the baseline in 2005 6/	9	9	6	9	9	9	10	10	4	0	0	0	0	0	0
Memorandum item:															
Grant element assumed on residual financing (i.e., financing required above baseline) 7/	54	52	50	48	46	44	42	41	41	38	35	34	33	33	32

Source: Staff projections and simulations.

1/ By the year 2023 real GDP growth slows down significantly due to the projected decline in petroleum production.
2/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
4/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
5/ Includes official and private transfers and FDI.
6/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
7/ Based on historical level of concessionality. Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Statement by the IMF Staff Representative
August 1, 2005

1. This statement reports on information received since the staff report was issued. This information does not alter the thrust of the staff appraisal.

2. The two prior actions for Executive Board consideration of a new PRGF arrangement with São Tomé and Príncipe were met. This included the passage of the 2005 budget consistent with the authorities' Memorandum of Economic and Financial Policies and the receipt of the oil signature bonus on Block 1 (Staff Report, Table I. 2, page 70).

3. The authorities informed the staff on July 26, 2005, that all structural performance criteria set for end-July 2005 under São Tomé and Príncipe's request of a three-year arrangement under the Poverty Reduction and Growth Facility were met. This included the submission to the National Assembly of:

   (i) a new tax code on personal income-taxation, broadening the tax base and updating the tax rate schedules to provide progressivity to the personal income-tax system;

   (ii) a new code on corporate taxation that limits the granting of tax holidays to new licensed investors to a maximum of three years, with tax reductions only covering up to 75 percent of profit taxes due;

   (iii) a new tax procedural code establishing tax tribunals at different levels of government to handle tax issues and disputes, as well as penalties and fines for underpayment, late payment and other tax violations; and

   (iv) a new investment code that provides for equal treatment of domestic and foreign investors and is consistent with the new code on corporate taxation.

4. On July 29, 2005, the authorities provided the staff with a timetable for the reduction of outstanding payments arrears to the water and electricity company (EMAE). This is a structural benchmark set for end-July 2005 under the proposed PRGF arrangement.

5. Retail prices for fuel products increased, on average by 22 percent, on July 9, 2005. This is consistent with the government's policy to fully pass-through increases in world crude oil prices to domestic consumers. In turn, the water and electricity company (EMAE) has requested the government's authorization to increase electricity tariffs to cover the price increase in diesel, which is extensively used in the production of thermal electricity.

The programmed increase in excise duties on services and domestically-produced beer was implemented on July 29, 2005; i.e., with a two-week delay from originally planned.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No. 05/187
FOR IMMEDIATE RELEASE
August 5, 2005

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$4.3 Million Three-Year PRGF Arrangement for São Tomé and Príncipe

The Executive Board of the International Monetary Fund (IMF) has approved a three-year arrangement for São Tomé and Príncipe under the Poverty Reduction and Growth Facility (PRGF) in an amount of SDR 2.96 million (about US$4.3 million) to support the government's program of economic reform and poverty reduction. Disbursements under this arrangement shall not exceed the equivalent of SDR 1.269 million (about US$1.9 million) until July 31, 2006.

The last PRGF arrangement for São Tomé and Príncipe was approved in April 2000, and went off track in early 2001. A staff-monitored program was put in place for 2002, under which the country established a broadly satisfactory track record. Preliminary discussions on a new PRGF arrangement were held in 2003, but the authorities could not commit to medium-term macroeconomic policies at that time due to the difficult political environment. São Tomé and Príncipe reached the decision point under the enhanced HIPC Initiative in December 2000.

The Executive Board also considered São Tomé and Príncipe's full Poverty Reduction Strategy Paper (PRSP) and the Joint-Staff Advisory Note (JSAN), prepared by the Fund and World Bank Staffs.

In commenting on the Executive Board's discussion on São Tomé and Príncipe, on August 1, 2005 Mr. Agustín Carstens, Deputy Managing Director and Acting Chair, stated:

“The authorities are to be commended for the actions taken to address the relaxation in fiscal policy and rapid credit growth that had led to increased inflation in 2004. The medium term program for 2005-07, which targets significant real GDP growth and a reduction in inflation to single digits, provides a sound basis for the stable macroeconomic environment needed to achieve the ambitious reform agenda set out in the Poverty Reduction Strategy Paper (PRSP). With a transition to oil-producing status in prospect, the decisive implementation of the PRSP would bolster efforts to address the country's macroeconomic imbalances, while substantially reducing poverty and moving forward towards reaching HIPC completion point.

"The new three-year PRGF is embedded in the PRSP, which provides a credible, if highly ambitious, framework for achieving the government's objectives of raising private sector-led growth and reducing poverty. The attainment of these objectives will depend in large part on prioritizing sectoral strategies, while making them fully consistent with the annual fiscal budget and the government's price stability target. The steadfast implementation of economic policies, including the timely execution of a broad range of institutional and structural reforms supported by technical and financial support from development partners, will help mobilize to concessional financing from donors, and strengthen policy credibility.

"Fiscal consolidation, which will require reining in expectations fueled by the prospect of oil riches, while protecting pro-poor spending, remains an essential element of macroeconomic stabilization. New revenue measures incorporated into the 2005 budget, together with prospective reforms of the personal and corporate tax code, reforms in tax administration and debt relief projected under the enhanced HIPC initiative, should make it possible to achieve the spending priorities set out in the PRSP. However, the continuous large increases in the civil service wage bill are a matter of concern. In this regard, the wage increases granted in 2005 should be treated as exceptional and any other ad-hoc wage increases should be avoided in the future.

"Addressing the fragile financial position of the water and electricity company (EMAE), while fostering private investment in the energy sector, is also critical to secure macroeconomic stability. It will be important therefore to implement programmed measures, including steps to eliminate outstanding payment arrears to EMAE.

"The authorities are to be commended on the passage of the Oil Revenue Management Law and the government's decision to participate in the Extractive Industries Transparency Initiative (EITI), which are important steps towards securing transparency and accountability in the management of oil revenue. Efforts to devise a comprehensive structural reform program contained in the PRSP, including in the areas of agriculture, basic education and health services, public expenditure management, and the privatization of state enterprises, are also most welcome," Mr. Carsten said.

ANNEX

Recent Economic Developments

São Tomé and Príncipe is a small economy greatly dependent on external financial assistance and is heavily indebted. Exports of goods and services---primarily tourism and cocoa—are equivalent to a third of GDP, which is about US$60 million (or US$375 GDP per capita). In the early 1990s, oil and natural gas deposits were discovered offshore from São Tomé and Príncipe, but revenues from these deposits—while potentially high—are still uncertain. Oil production is expected to start no earlier than 2012. São Tomé and Príncipe has announced that it will participate in the Extractive Industries Transparency Initiative (EITI)

In 2004, the economy of São Tomé and Príncipe grew at a moderate pace, but inflation increased to 15 percent by year-end, as bank credit to the private sector rose sharply and the government loosened fiscal policy. Also, External payments arrears continued to increase in 2004.

Program Summary

The PRGF-supported program for 2005-07 aims at correcting macroeconomic imbalances and sets the conditions for sustained strong growth. Real GDP is envisaged to slow down in 2005 in response to tight financial policies, but pick up thereafter. Inflation is projected to decline to single-digit levels by 2007. Gross international reserves would be kept at around 3½ months of imports and services. The program includes a major fiscal consolidation effort over the next three years, and the implementation of key structural reforms embodied in the country's Poverty Reduction Strategy Paper.

In 2005, the program envisages a large fiscal adjustment, based on a strong revenue effort and significant spending cuts, while safeguarding spending levels on education and health. Structural reforms are expected in the areas of tax reform, transparency in the management of government revenue, the finances of the water and electricity company, the development of an effective anti-money laundering/combating the financial of terrorism (AML/CFT) regime, and business climate.

The PRGF is the IMF's concessional facility for low-income countries. PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in a PRSP. This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent and are repayable over 10 years with a 5½-year grace period on principal payments.

Table 1. São Tome and Principe: Selected Economic Indicators, 2002-07

	2002	2003	2004	2005	2006	2007
					Prog.	
	(Annual percentage changes, unless otherwise specified)					
National income and prices						
GDP at constant prices	4.1	4.0	3.8	3.2	4.5	5.5
Consumer prices (percentage change; end of period)	8.9	10.2	15.2	15.0	12.0	9.4
Consumer prices (percentage change; average)	9.2	9.6	12.8	15.1	13.4	10.6
External trade						
Exports, f.o.b. 1/	37.6	19.4	13.8	6.0	0.2	0.0
Imports, c.i.f.	16.6	17.2	9.0	4.6	6.7	11.3
Exchange rate (in dobras per U.S. dollar; end of period)	9,192	9,456	10,104	...	...	...
Real effective exchange rate (depreciation -)	-5.2	-8.7	-2.7	…	…	…
Terms of trade	52.7	-11.6	-20.3	0.2	0.4	-0.2
Money and credit (end of period)						
Net domestic assets 2/	-0.2	11.0	17.1	3.6	9.0	14.0
Of which: credit to government (net) 2/	-0.2	15.3	6.0	1.8	-11.4	-15.9
credit to the economy 2/	12.1	20.6	34.4	11.3	15.1	14.1
Broad money	26.9	41.8	7.4	12.3	21.9	21.9
Velocity (ratio of non-oil GDP to average broad money)	2.8	2.3	2.2	2.4	2.4	2.3
	(In percent of GDP, unless otherwise specified)					
National accounts						
Consumption	117.5	116.7	122.0	122.0	121.4	118.1
Gross investment	32.5	36.1	34.5	37.3	40.2	47.7
Public investment	14.5	20.1	19.4	16.4	16.0	15.5
Private investment	18.0	16.0	15.1	21.0	24.3	32.2
Gross domestic savings	-17.5	17.6	12.2	10.6	16.0	16.8
Public savings 3/	12.5	13.8	6.6	84.4	23.2	23.8
Gross national savings	8.0	15.9	7.1	9.2	16.7	18.9
Government finance						
Total revenue, grants and oil signature bonus	50.5	58.1	59.3	127.9	63.9	61.9
Of which: tax revenue	19.5	20.7	23.4	24.1	24.2	24.6
grants	27.2	32.5	30.9	28.2	33.2	31.2
oil signature bonus	…	…	…	71.0	…	…
unidentified revenue measures	…	…	…	…	2.0	1.9
Total expenditure and net lending	66.9	75.1	85.6	76.5	71.2	66.1
Of which: noninterest current expenditure	26.9	28.4	41.7	37.8	33.6	30.2
capital expenditure	28.8	35.8	35.8	29.3	28.9	28.1
Domestic primary balance (commitment basis; incl. HIPC Initiative spending) 4/	**-4.3**	**-11.7**	**-20.6**	**-17.5**	**-11.9**	**-7.6**
Overall balance (commitment basis; including grants)	-16.4	-17.0	-26.3	51.4	-7.3	-4.1
Overall balance (cash basis; including grants)	-6.4	-11.9	-19.8	27.7	-7.3	-4.1
External sector						
Current account balance (including official transfers)	-24.6	-20.2	-27.3	-28.2	-23.5	-28.7
Current account balance (excluding official transfers)	-54.0	-54.5	-61.5	-60.3	-60.3	-63.1
Net present value of total external debt 5/ 6/ 7/	512.7	499.2	449.0	465.3	358.1	375.6
Net present value of total external debt 5/ 6/ 8/	693.2	634.2	550.6	619.7	427.3	440.6
Scheduled external debt service before debt relief 7/	60.8	58.0	50.6	56.7	51.9	49.6
Overall balance (in millions of U.S. dollars)	-2.4	1.8	-9.5	19.2	-12.6	-11.8
Gross foreign reserves (in months of following year's non-oil imports of goods and nonfactor services) 9/	3.9	4.5	3.4	3.4	3.5	3.5
Permanent oil fund (in millions of U.S. dollars) 10/	…	…	…	23.1	19.2	15.1

Sources: São Tomé and Príncipe authorities; and IMF Staff estimates and projections.
1/ During 2004-07, includes US$1.4 million per year in re-exports of oil arising from aid in kind received from Nigeria.
2/ In percent of broad money at beginning of period.
3/ Government revenue includes HIPC debt relief. In 2005, reflects receipt of US$49.2 million from oil signature bonus on Block 1.
4/ Excluding oil revenue, grants, interest earned and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2002-04, it also excludes transfers to the JDA, which are to be repaid with proceeds from the oil signature bonus from Block 1.
5/ Including arrears to Italy on a loan that remains in dispute.
6/ Assumes that the completion point under the enhanced HIPC Initiative is reached in 2006.
7/ In percent of exports of goods and nonfactor services, calculated as a three-year backward-looking average.
8/ In percent of government revenue.
9/ Excluding guarantee deposits placed at the central bank by prospective financial institutions pending operating licenses.
10/ Includes interest income earned on oil fund.

Statement by Damian Ondo Mañe, Executive Director for São Tome and Príncipe
August 1, 2005

On behalf of my Sao Tomean authorities, I would like to express my appreciation to Management and the staff for their assistance and advice to Sao Tome and Principe (STP).

As I indicated in my previous statement on STP, the advent of oil era, while very welcome, as its resources will help to develop the country and reduce poverty, also brings major challenges. These include (i) the avoidance of the so-called "Dutch Disease", (ii) the adequate responsiveness to political pressures and social expectations and (iii) the building of extensive political consensus for the efficient use of oil resources.. Although oil production is not expected before 2012, my authorities have to face these daunting challenges that already loom.

By the time oil effectively starts, Sao Tome and Principe will remain a highly indebted and poor and as such it faces the challenges inherent to this group of countries. While oil bonuses receipts will help the government in its growth-enhancing and poverty-reduction efforts over that transition phase, support from the international community will still be needed.

Recent Economic Developments

Output in STP is estimated to have grown by around 4 percent in 2004, mostly driven by higher public demand. In anticipation of oil bonuses receipts in 2004, and under severe popular pressure, the government raised critical social expenditures aimed at meeting the demand for better conditions of living. However, the oil bonuses did not materialize and the fiscal situation deteriorated with the overall fiscal deficit increasing to 26.3 percent of GDP from 17 percent in 2003. To close the financial gap, the authorities resorted to credit from the central bank and external concessional borrowing from neighboring countries. At the same time, credit to the private sector expanded significantly, which despite the central bank's efforts to mop-up liquidity in the economy, resulted in consumer prices increasing to 15.2 percent in 2004 from 10.2 percent in 2003. In addition, reliance on intervention in the foreign exchange market to prevent a depreciation of the dobra led to a reduction of NIR.

During the first semester of 2005, macroeconomic policy implementation improved remarkably. Indeed my authorities have tightened their financial policies despite strong pressures to maintain the policy stance adopted in 2004.

Significant progress was made in the implementation of the triggers for reaching the floating completion points, under the HIPC Initiative. A poverty reduction strategy (PRS) elaborated and set out in a PRSP adopted in 2002 had been updated to take into account recent developments, notably regarding the macroeconomic framework.

It should be noted that the relaxation of macroeconomic policies in 2004 did not reduce the authorities' commitment to reform, improved transparency and governance. In particular, in the oil sector, the institutional framework for developing the national petroleum strategy and to supervise and regulate the sector became operational in the first half of 2004, with the settings of the National Committee on Petroleum (NCP) comprising of representatives of the government, the civil society and the private sector, and the National Petroleum Agency (NPA) which absorbed the small technical petroleum unit already functional since 2002. Furthermore, a public information campaign was started since last year to disseminate basic information on the petroleum industry, notably regarding the management of the petroleum revenues.

Poverty Reduction Strategy

The PRS revolves around five basic pillars that are

- Accelerated and redistributive growth;
- Creating opportunities to increase and diversify income;
- Developing human resources and access to basic social services;
- Reforming public institutions, capacity building and promotion of good governance; and
- Mechanisms for monitoring, assessing and updating the strategy.

The PRS sets as a long term objective the reduction by half of poverty by 2010 and by more than two thirds by 2015. To this end, the PRS develops measures that will reduce the gap in social indicators across all dimensions of poverty (urban and rural populations, gender and geographical locations). Among other measures, the PRS seeks to provide access to basic social services, notably health and education, for the entire population by 2015. In this regard, the health and education sectoral strategies have already been developed and costed.

As noted above, many changes occurred since the adoption of the PRSP in 2002, which called for a revision of its macroeconomic context. Among those changes is the emergence of the oil activity in the islands. My authorities are fully aware that good management of the oil resources will be key to maintain macroeconomic stability and to achieve their poverty reduction objectives. In this regard, the long-discussed and awaited Oil Revenue Management Law (ORML) was adopted by the Parliament in December 2004. As noted in Box 2 of the staff report, the ORML sets the conditions and mechanisms for a transparent use of oil resources. The institutional framework a National Petroleum Agency (ANP) has been set up with the assistance of the World Bank. In addition, my authorities have expressed their interest in participating in the EITI.

The PRS emphasizes that growth should not come from one source as this could be the case with the advent of oil. Therefore, the PRS contemplates alternatives sources of growth through the development of sectors where STP has a comparative advantage and where most of the poorest population is concentrated. These sectors include notably tourism and agriculture. The PRS envisions also a set of actions to improve the business climate. Some of them such as the Auditor General's Office have been implemented.

Above all, the PRS recognizes the need to maintain macroeconomic stability as condition to reduce poverty. In this regard and in order to achieve their growth and poverty reduction objectives, set in the PRSP, my authorities elaborated with the assistance of Fund staff a three-year economic and development program, for which they are requesting IMF support under the PRGF.

Program for 2005-2007

The program for 2005-07 aims at (i) achieving a GDP growth of 4.3 percent on average per year, (ii) further fiscal consolidation following the rise in current expenditures in late 2003 and 2004, while maintaining pro-poor spending consistently with the PRS objectives, and (iii) bringing back inflation to single digit level.

Fiscal consolidation over the medium-term will be achieved through increasing tax revenue and improving government expenditures. In particular, my authorities intend to reform tax policy and administration, in the context of a tax package to be submitted to the National Assembly. Significant cuts in expenditures will be undertaken over the program period. The wage bill, however, will increase in the first year of the program to reflect augmentation in the civil servants' minimum wage. No recourse to central bank financing is envisaged over the program period and as reflection of improved budget management, no new domestic or external arrears will be accumulated. As a result of these efforts, the program targets a reduction in the domestic primary deficit from 20.6 percent in 2004 to 7.6 percent in 2007.

Monetary policy will be consistent with the inflation reduction objective, and exchange rate policy will aim at achieving appropriate level of NIR. In particular, to improve liquidity management, the central bank will launch open market operations with central certificates of deposits and allow interest rates to be market-determined, while continuing with its policy of auctioning foreign exchange.

Efforts will be pursued to improve the financial sector reform and particularly the soundness of the banking sector through actions to improve regulation and licensing of new banks and enhance prudential standards. The reform will also strengthen mechanisms to prevent money laundering and financing of terrorism and deter financial crime.

My authorities will continue the reform process consistently with their objectives of improving public expenditure management, promote the development of the private sector and enhance the business climate. Most importantly, my authorities attach a great importance to transparency and governance in the oil sector. They will actively enforce the provisions of the ORML starting with the establishment of the bodies provided in the law.

STP is a highly indebted country and its debt will remain high over the medium-term. This debt situation is an impediment to the growth and poverty reduction strategy. Accordingly, in complement to their efforts to improve debt management, my authorities intend to request a debt rescheduling from the Paris Club in 2005, along with the agreement with the Fund on a PRGF-supported program. However, even after such a debt rescheduling, and further debt relief at the enhanced HIPC initiative completion point, the NPV of debt-to-export ratio is only projected to fall from 450 percent at end-2004 to 402 percent by end-2010, (table 9, page 36) compared with the threshold of 150 percent.

Policies for the Remainder of 2005

The medium-term economic program provides for a frontloading of measures in the first years. Hence, my authorities intend to maintain the policy stance adopted since late 2004.

More specifically, on the **fiscal** front, most of the enhancing-revenue measures related to changes in tax procedural code, coverage and rates will be implemented during this year and are expected to raise revenue by 2.1 percent of GDP in 2005. In addition, the draft new tax codes will be submitted to the National Assembly during this quarter, with the new tax regimes entering into effect in January 2006. On the expenditure side, cuts will be operated essentially in goods and services, including telecommunications, water and electricity and official travel items, and in domestically-financed investment expenditures, while ensuring that pro-poor spending is not affected. Both expenditure items will decrease by 11.5 percent of GDP.

As regards fiscal-related reforms, the government is developing a fully integrated, computerized budget and public expenditure management system with the assistance of the World Bank and FAD. It should be operational by mid-2006. The Auditor General's Office is expected to complete the review of the 2004 financial accounts of central government during this quarter. The government will start implementing recommendations of this review in the last quarter of this year. The government is committed to improve the system of public procurement during the next three years, with the assistance of the World Bank. The new procurement practices are expected to be in place by end-2005. A PRSP unit has been set up at the Ministry of Planning and Finance, with the objective of ensuring the implementation and monitoring of the PRSP. This unit will issue a report on the status of implementation by September 2005. My authorities will also undertake the revision of its payment of wages and salaries, and develop a public employee's register with the assistance of UNDP. By September 2005, a computerized registry of public servants, among others, will be developed.

Along with fiscal adjustment, my authorities will maintain a tight **monetary policy** stance in order to achieve their inflation reduction objective set at 15 percent this year. In particular, private sector credit growth will be reduced from 116 percent in 2004 to 19 percent in 2005. The central bank will also continue to work closely with MFD regarding the implementation of indirect monetary instruments such as certificates of deposit and the special liquidity facility. The central bank is committed to the continuation of a flexible exchange rate arrangement, as already signaled by the recent introduction of foreign exchange auctions in late 2004.

As regard bank supervision and prudential regulations in the **financial sector**, the central bank intends to implement a consolidated reporting mechanism on financial conditions to be submitted by banks to the central bank by September 2005 and to establish a Credit Risk Bureau during the third quarter of 2005. With the assistance of LEG, a legislation to criminalize money laundering and the financing of terrorism is being elaborated and is expected to be submitted by September 2005.

Other Structural reforms in 2005 will aim at developing and sustaining economic activity through the improvement of the business environment, the divestment of public enterprises and the strengthening of the governance, notably in the oil sector. Specifically, my authorities intend to submit to the National Assembly in the third quarter of 2005 a new investment code and adopt by end-September 2005 an action plan for streamlining the process of establishing businesses. The idea of a land reform is progressing with the elaboration of terms of reference for a study on land tenure by end-2005. With the support of the World Bank, my authorities will seek to address the most urgent needs for institutional reform and technical capacity building of the judicial system over the program period.

The restructuring of the **public enterprises** is progressing. To avoid further consumer debt accumulation, EMAE will introduce soon a prepayment system through electricity metering keypads for residential and commercial users. EMAE and the government agreed on a performance contract under which the government will grant a guarantee to a bank loan to EMAE for the implementation this system on the condition that EMAE develops a broader financial strategy to address its weak financial position. A first step of this strategy will be the elaboration of a timetable for the reduction of outstanding payments arrears by customers during this quarter. My authorities are also considering the divestment of other public enterprises. In particular, they intend to complete feasibility studies on the privatization of public enterprises administering airports (ENASA) and seaports (ENAPORT) by end-2005.

As regards transparency and governance in the **oil sector**, my authorities will finalize by the end-September 2005 an overall strategy for the oil sector development, with the assistance of the World Bank and UNDP. In particular, the strategy will address options for institutional settings regarding the development of the country's Exclusive Development Zone (EDZ) and the country's possible participation in petroleum exploration and development activities. In accordance with the Abuja Declaration, my authorities intend to foster the production, and dissemination of oil-related information.

Conclusion

My STP authorities view this string and ambitious medium-term program for which they are requesting Fund's assistance under a PRGF arrangement as being able to help them meet the objectives of growth and poverty reduction. The program will also contribute to strengthen the institutions of the country and help put in place the reforms that will improve economic performance and establish a strong foundation in preparation of the oil era. In their efforts my STP authorities are hopeful that they can continue to rely on the full support of the international community. In this regard, I would appreciate Directors' support for their request for a PRGF arrangement.