

**Democratic Republic of São Tomé and Príncipe: Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion—Staff Report; Press Release on the Executive Board Discussion; and Statement by the Executive Director for the Democratic Republic of São Tomé and Príncipe**

In the context of the fourth review under the 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 Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion prepared by a staff team of the IMF, following discussions that ended on March 23, 2007, with the officials of the Democratic Republic 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 June 1, 2007. 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 Press Release summarizing the views of the Executive Board as expressed during its June 25, 2007 discussion of the staff report that completed the review.
- A statement by the Executive Director for the Democratic Republic of São Tomé and Príncipe.

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

Letter of Intent sent to the IMF by the authorities of the Democratic Republic of São Tomé and Príncipe\*

Memorandum of Economic and Financial Policies by the authorities of the Democratic Republic of São Tomé and Príncipe\*

Technical Memorandum of Understanding\*

\*Also included in Staff Report

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

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INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

Fourth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criterion

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

Approved by Jean A. P. Clément and Scott Brown

June 1, 2007

**Program Review**

- This report recommends completion of the fourth review under the PRGF arrangement based on São Tomé and Príncipe's performance and understandings reached on policy implementation for the remainder of 2007.
- Staff supports the authorities' request for waiver for nonobservance of the structural performance criterion on adopting a decree to establish the new public accounting plan by end-March 2007. The government adopted the decree on May 31, 2007.

**Participants**

- The mission (March 12-23, 2007) comprised Mr. Wang (head), Mr. Ronci, Ms. Farhan, and Ms. Takebe (all AFR). The staff team worked closely with a parallel World Bank mission and a FAD technical assistance team. Mr. Shanghavi helped prepare the staff report.
- The mission met with the Prime Minister, the Deputy Prime Minister and Minister of Planning and Finance, the Governor of the Central Bank, and other senior officials. They also met with the Economic Commission of the National Assembly, representatives of the private sector, trade unions, the donor community, and the media.

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**ABBREVIATIONS AND ACRONYMS**

AML/CFT	Anti-Money Laundering/Counter Financial Terrorism
BCSTP	Banco Central de São Tomé e Príncipe (Central Bank of São Tomé and Príncipe)
EITI	Extractive Industries Transparency Initiative
FAD	Fiscal Affairs Department
GDP	Gross domestic product
HIPC	Heavily Indebted Poor Countries
JDA	Joint Development Agency (with Nigeria)
MEFP	Memorandum of Economic and Financial Policies
MDRI	Multilateral Debt Relief Initiative
NA	National Assembly
NIR	Net international reserves
LOI	Letter of intent
INE	Instituto Nacional de Estatísticas (National Institute of Statistics)
ORML	Oil Revenue Management Law
PRSP	Poverty Reduction Strategy Paper
SAFE	Sistema de Administração Financeira do Estado (Public Financial Management System)
eSAFE	Integrated Computerized SAFE
SAFINHO	Pilot System for eSAFE
TMU	Technical Memorandum of Understanding

## EXECUTIVE SUMMARY

**São Tomé and Príncipe has made progress in stabilizing its economy.** Real GDP growth accelerated in 2006. Inflation has been declining since August. The domestic primary fiscal deficit was significantly reduced. All quantitative performance criteria (as revised in the third review) and structural benchmarks for end-December 2006 were met. Progress continues on structural reform, albeit sometimes slower than originally envisaged.

**The authorities agreed to strengthen policy implementation in order to bring inflation further down.** Understandings were reached on continued efforts to consolidate the recent stabilization gains, including measures to safeguard the fiscal program and close cooperation between the treasury and the central bank to ensure timely sterilization of budgetary use of oil bonuses to contain liquidity growth.

**The authorities recognize the importance of accelerating structural reforms to lay the ground for sustained growth.** Their 2007 reform agenda focuses on strengthening public financial management, enhancing banking supervision, and improving the investment climate.

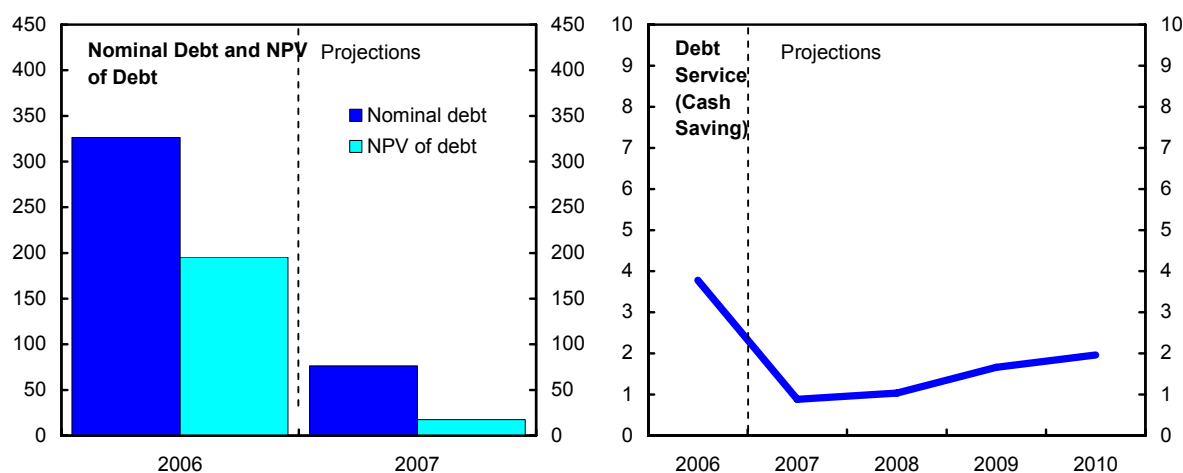
**Risks to program implementation are important but manageable.** The risks include further delays in approving the envisaged revenue measures, social pressures for more spending, weak capacity in monetary policy implementation, and unfavorable developments in oil prospects. The authorities are committed to adjusting their medium-term fiscal and external financing strategies, based on a careful review of oil revenue prospects.

**Staff recommend completion of the fourth review based on the country's performance and policy commitments.** It supports the authorities' request for a waiver for the nonobservance of the March 2007 structural performance criterion, owing to difficulties in obtaining timely technical assistance. This was implemented as a prior action.

## I. BACKGROUND

1. **São Tomé and Príncipe is a small, highly indebted poor country (HIPC), with a very narrow production and export base.** The country reached the completion point under the enhanced HIPC Initiative in mid-March 2007, thereby benefiting from HIPC and MDRI debt relief. While the reduction in the debt stock is substantial, annual savings in cash terms are relatively moderate. São Tomé and Príncipe has received large oil signature bonuses since 2005. The prospects for significant oil export earnings depend on confirmation of commercially extractable oil reserves.

**External Debt Indicators after HIPC, Topping-up and MDRI Debt Relief  
(Millions of U.S. dollars)**



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

2. **The country's GDP statistics have been revised based on the most recent population and business census (Box 1).** Despite the considerable upward revision, São Tomé and Príncipe remains a low-income country.

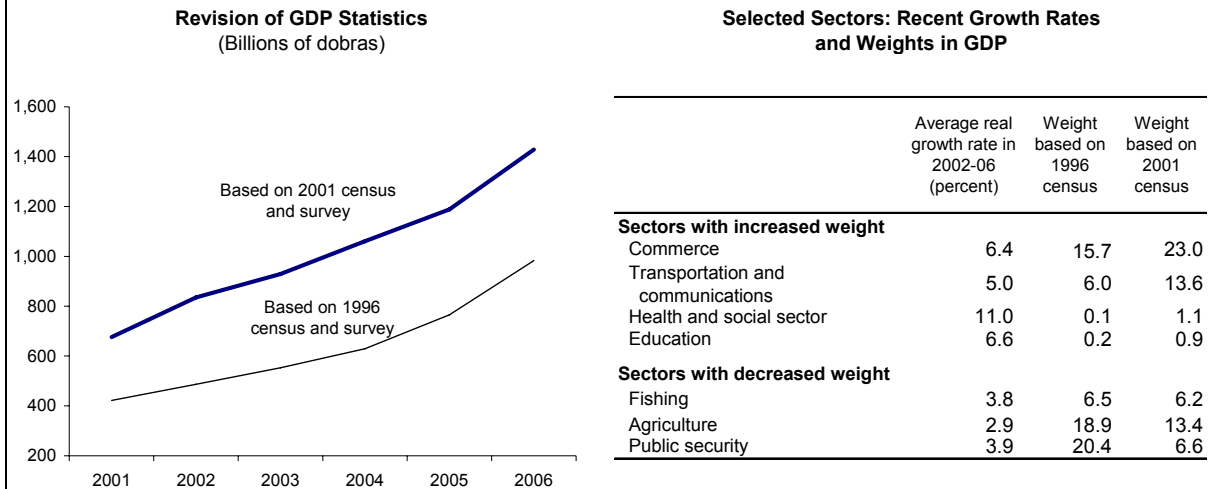
## II. PERFORMANCE UNDER THE ARRANGEMENT

3. **Economic activity picked up in 2006, driven largely by an upsurge in capital inflows, which boosted private investment, and by large public expenditure (Figure 1 and Table 1).** Real GDP grew at an estimated 7 percent in 2006, led by buoyant construction, services, and commerce activities.

4. **Inflation declined to 17 percent (year-on-year) in March 2007, from its peak of over 26 percent in August 2006.** The deceleration reflected fiscal tightening and a more active use of monetary policy to curb liquidity growth, and the resulting slower depreciation of the dobras. In real terms, the exchange rate appreciated somewhat owing to higher domestic inflation during the period.

### Box 1. Revision of GDP Statistics

The revised GDP series, with improved coverage and updated sectoral weights based on the 2001 population and business census, reflects more accurately economic developments in recent years (see Information Annex, Appendix IV).



Sources: National Institute of Statistics of São Tomé and Príncipe and IMF staff estimates.

#### Selected Economic Indicators Before and After the Revision of GDP Statistics

(Percent of GDP unless otherwise specified)

	Before the revision <sup>1</sup>			After the revision <sup>2</sup>		
	2005	2006	2007	2005	2006	2007
<b>Public Finance</b>						
Total revenue, grants and oil signature bonuses	127.2	58.0	254.7	81.9	37.4	164.5
Total expenditure and net lending	69.1	79.6	61.3	44.5	51.3	39.6
Of which: current expenditure	41.1	44.8	33.5	26.5	28.9	21.6
capital expenditure	24.4	31.3	23.3	15.7	20.1	15.0
HIPC initiative-related social expenditure	3.6	3.6	4.6	2.3	2.3	3.0
Domestic primary balance	-15.9	-13.3	-10.9	-10.3	-8.6	-7.0
<b>Balance of Payments</b>						
Current account balance	-31.0	-71.2	-63.9	-20.0	-45.9	-41.3
<b>External Sector</b>						
NPV of public external debt	268.6	251.9	25.3	172.9	162.2	16.3
<b>Memorandum Items</b>						
Nominal GDP (million US dollars)	73	80	92	114	123	142
GDP per capita (US dollars)	467	497	572	725	771	886

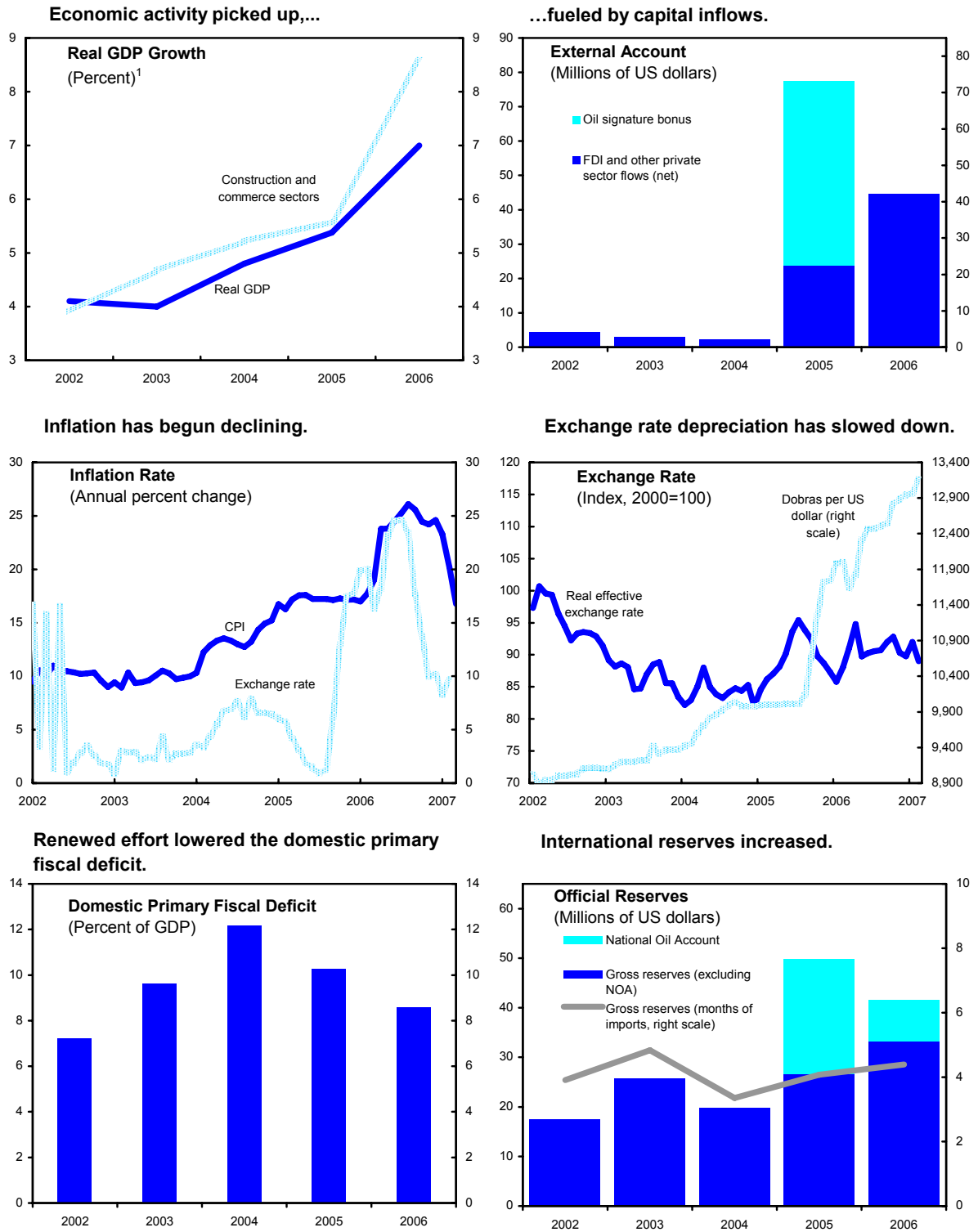
Sources: São Tomé and Príncipe authorities and IMF staff estimates and projections.

<sup>1</sup> GDP series using sectoral weights based on the 1996 census and survey.

<sup>2</sup> GDP series using sectoral weights based on the 2001 census and survey.



**Figure 1. Recent Macroeconomic Developments**



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

<sup>1</sup>There is a break in the data series between 2003 and 2004.

5. **The domestic primary fiscal deficit narrowed to 8.6 percent of GDP in 2006, down from 10.3 percent in 2005 and well below the program target of 9.8 percent** (Table 2). Domestic revenue was stronger than expected by 1.1 percent of GDP mainly due to higher fuel import duties and excise taxes resulting from an increase in petroleum prices and a higher volume of imports. Renewed efforts since mid-2006 also helped restrain non-interest current expenditures. As a result, the use of oil signature bonuses for budgetary financing (about US\$12.5 million) was lower than budgeted, despite larger than initially projected repayment of external debt.
6. **All quantitative performance criteria for end-December 2006 were met** (Table 7). The central bank (BCSTP) tightened monetary policy by stepping up foreign exchange sales to sterilize budgetary use of oil bonuses and foreign inflows, leading to a deceleration in monetary aggregates. Base money growth fell from 117 percent in June 2006 to 15 percent in March 2007. Net international reserves (NIR) of the BCSTP exceeded the performance criterion by a large margin, owing mainly to the government's much stronger net position at the central bank.
7. **Progress continues on structural reforms albeit sometimes slower than originally envisaged.** All structural benchmarks through December 2006 were met (Table I.2). A new organic budget law (SAFE) was adopted in early 2007. This law introduces better budget classification, more transparency, and other improvements in the budget system. In addition, a pilot system (SAFINHO) was introduced to improve budget preparation and execution. However, the authorities have experienced difficulties in obtaining timely assistance from a donor-financed consultant to prepare the decree establishing the public accounting plan, as required by the end-March 2007 structural performance criterion. Implementation of the anti-money laundering (AML/CFT) law, another March benchmark, is also delayed because the National Assembly (NA) has not yet given final approval of the law.

### III. CONSOLIDATING RECENT STABILIZATION GAINS AND SUSTAINING GROWTH

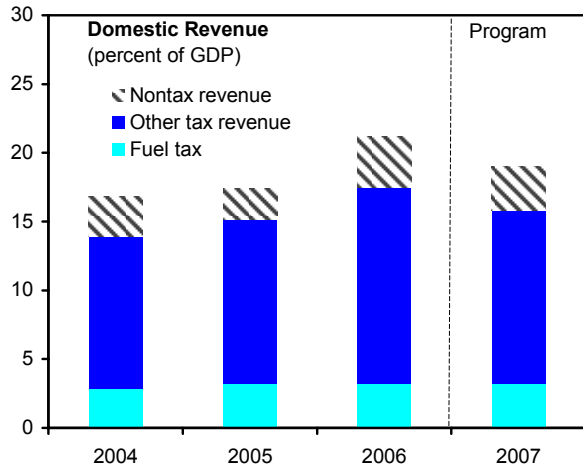
8. **The authorities made it clear that they intend to build upon the recent progress in macroeconomic stabilization, and to further reduce inflation** (Figure 2). They recognized that, while HIPC and MDRI relief has lifted the heavy debt burden on the country, reducing poverty will require persistent efforts to maintain macroeconomic stability and achieve sustainable growth, in line with their PRSP.<sup>1</sup> Policy discussions thus focused on measures to ensure continued fiscal consolidation and monetary tightening, and structural reforms to lay the ground for private sector-led growth. Because prospects for oil revenue have profound implications for São Tomé and Príncipe's economic policies, this was a key topic for discussion.

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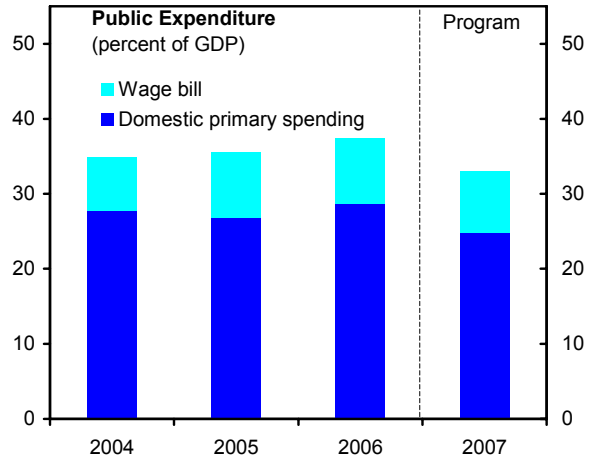
<sup>1</sup> The first progress report of the PRSP was circulated to the Board in October 2006.

**Figure 2. 2007 Program: Fiscal Consolidation and Monetary Tightening**

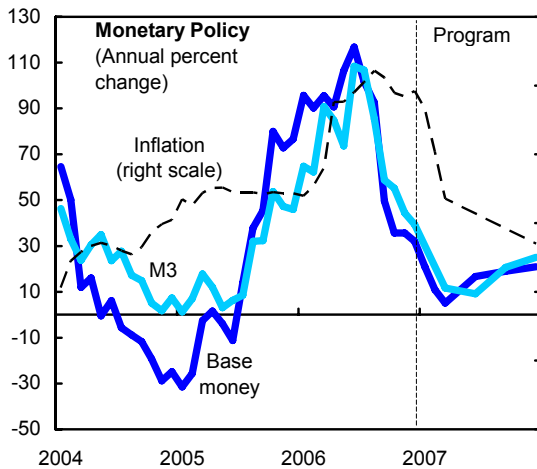
**Tax reforms to reduce distortions...**



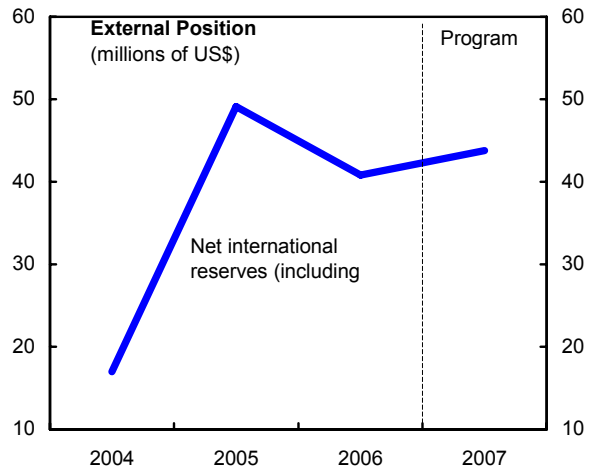
**...while reorienting expenditures to support growth and poverty reduction.**



**Monetary tightening to reduce inflation...**



**...while safeguarding net international reserves.**

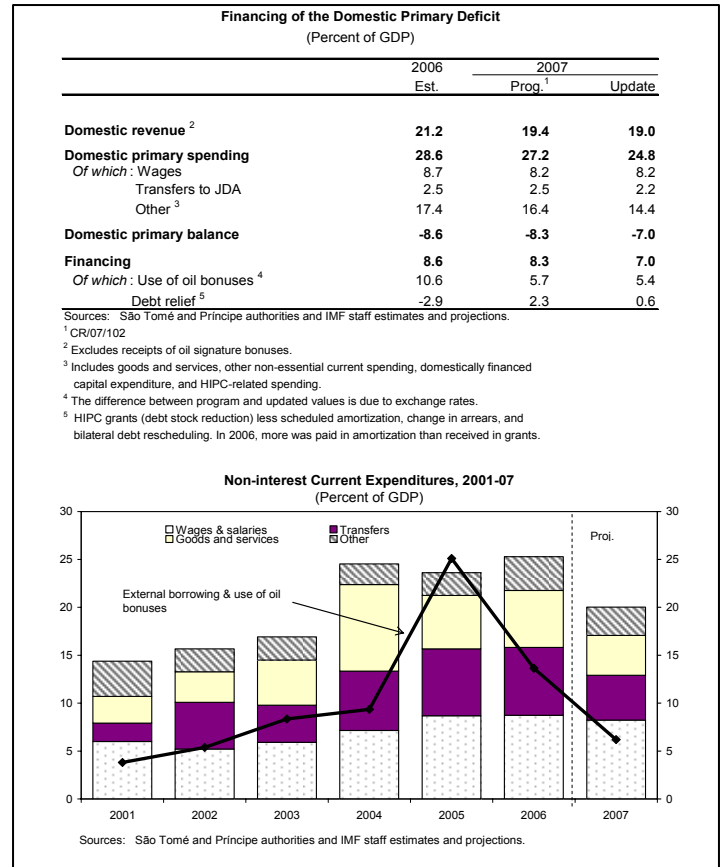


Sources: São Tomé and Príncipe authorities, and IMF staff estimates.

## A. Fiscal Policy

### 9. The fiscal program has been updated to take into account developments so far

**this year.**<sup>2</sup> The NA approved the 2007 budget in mid-March but delayed approval of the envisaged increase in the excise tax on services until it could consider the government's proposal to cut the corporate income tax rate.<sup>3</sup> Reform of the petroleum pricing structure and taxation, another revenue measure of the 2007 program,<sup>4</sup> has also been postponed due to procedural problems. More significantly, the latest debt relief figures have led to a downward revision of the savings available for budgetary use. To offset the lower financing, nonessential current spending has been revised downward.<sup>5</sup> The revised program, consistent with the envisaged use of oil bonuses of US\$8 million, is fully financed. It keeps essential spending intact while starting to lower other current expenditures toward the levels relative to GDP before the large inflows of oil-related resources, aiming to reduce the domestic primary deficit to 7 percent of GDP in 2007.



10. **Tax reform is an important element of the 2007 program.** The government submitted a tax reform package to the NA toward the end of 2006. The NA has adopted the tax administrative and procedural codes, which will help strengthen tax administration and arrears collection. The proposed corporate income tax law, new personal income tax code and a new urban property tax code, intended for implementation in 2008, aim to reduce distortions. The authorities are also preparing a new customs code, to modernize indirect taxation through simplifying the tax structure and broadening the tax base.

<sup>2</sup> The update maintains the thrust of the program to support poverty reduction. The new budget classification has complicated the compilation of pro-poor expenditures, which are not comparable with past data.

<sup>3</sup> The 2007 program includes the excise tax measure due to the unavailability of less distortionary, more transparent ways of raising indirect taxes (CR/07/102).

<sup>4</sup> See CR/07/102, Annex I for details.

<sup>5</sup> Nonessential current spending is defined as total current expenditure less wages, interest due, transfers to JDA, and foreign financed scholarships.

11. **To safeguard the program's fiscal objectives, understandings were reached on contingent measures** (MEFP, ¶12). Staff pointed out that there were special factors, such as very large use of oil bonuses and election-related capital inflows, behind the sharp increase in imports and related tax revenue in 2006. Such an increase is unlikely to be repeated this year and there are downside risks, including further delays in implementing the planned revenue measures. Unexpected movements in the exchange rate or oil import prices may adversely affect import duties and excise taxes. The authorities agreed that if revenue losses arise, they would have to reduce nonessential spending to fully offset them and keep domestic financing of the budget at levels below the program ceilings.

12. **The authorities are committed to strengthening public financial management** (MEFP, ¶14). With technical assistance from FAD and the World Bank, they are taking steps to improve upon SAFINHO, with the objective of putting in place a fully functioning eSAFE system in time for the 2008 budget. Introducing the new public accounting framework and procedures is an important element of the reform. The government formed an inter-ministerial committee in April and adopted a decree establishing the new public accounting plan in late May 2007.

13. **The authorities acknowledged the importance of maintaining debt sustainability after HIPC and MDRI debt relief** (MEFP, ¶25). They have signed agreements with Germany, France, and Spain in line with the 2005 Paris Club terms of reference and are in discussion or contact with non-Paris Club creditors (Algeria, Angola, Portugal, and China) to seek comparable debt relief. They have also obtained assurances for topping-up assistance from creditors accounting for 75 percent of debt after HIPC relief.

## **B. Monetary and Exchange Rate Policies**

14. **The monetary program for 2007 aims to reduce inflation to 10-15 percent by end-2007 through strict control of base money growth, in the context of a flexible exchange rate regime.** The authorities recognized that they have to rely primarily on foreign exchange sales and fiscal restraint to contain pressures on domestic prices and the exchange rate, because interest rates and other monetary instruments have had very limited impact on liquidity due to weak financial intermediation.

15. **The Ministry of Finance and the BCSTP agreed to cooperate closely to make monetary policy more effective** (MEFP, ¶17). They shared the view that such cooperation is needed to improve the BCSTP's liquidity forecast and to ensure timely interventions to offset the monetary impact of budgetary use of oil bonuses and HIPC and MDRI savings. Regular meetings of key officials would focus on the budget's cash outlays and their impact on base money and the BCSTP's foreign exchange market operations. Further fiscal tightening will be needed should the NIR target become at risk.

16. **The BCSTP is committed to further develop the foreign exchange market and ensure market determination of the exchange rate** (MEFP, ¶18). A number of actions have been identified, including holding regular foreign exchange auctions, limiting the

spread between commercial bank exchange rate and the rate used for central bank direct sales and progressively expanding the auction market. These measures, along with the adoption of the investment code, would remove the remaining exchange restrictions and multiple currency practices, paving the way for the country to accept the obligations under Article VIII of the Fund's Articles of Agreement.

### C. Structural Reforms

17. **There was a consensus that growth cannot be sustained unless adequate progress is made in structural reforms.** The authorities' reform agenda focuses on strengthening public resource management and improving the business climate. To ensure transparent management of existing and prospective oil resources, the government has compiled the Handbook of the ORML and is working toward posting it on the government's website (a structural benchmark). Efforts are being made for effective implementation of the measures under the ORML and the EITI (MEFP, ¶21),

18. **The authorities agreed that the cost of investing and doing business in São Tomé and Príncipe must be reduced** (MEFP, ¶22). This will require tax and regulatory reforms, financial sector development, and an upgrade of the country's infrastructure, including the airport, the sea port, and reliable provision of electricity and water. The authorities are in the process of introducing a new investment code, which would provide equal treatment to foreign and domestic investors. They also prepared a draft legislation that aims at sharply reducing the cost of and time for starting a business (Box 2). To reform the utilities' sector, the authorities have been installing prepaid electricity meters to improve payment collection while seeking foreign investors.

#### Box 2. Improving the Investment Climate

**To reduce the high cost of investing and doing business in São Tomé and Príncipe, the government has prepared a draft legislation, in consultation with the private sector.** The legislation would introduce a "one-stop shop" for business registration and related regulatory administration. This reform is expected to shorten the time needed for starting a business from over 140 days to below 3 days and significantly reduce the financial cost of this process.

Business Climate Ranking <sup>1</sup>				Starting a Business in São Tomé and Príncipe		
Ease of...	2005 rank	2006 rank	Change in rank	Activity	Time (days)	Cost (US \$)
<b>Doing Business</b>	<b>166</b>	<b>169</b>	<b>-3</b>	Total:	144	574
Starting a Business	115	122	-7	<i>of which:</i>		
Dealing with Licenses	136	142	-6	Notarize the company statutes	19	98
Employing Workers	175	175	0	Apply for advertising of the incorporation notice in the official gazette	45	0
Registering Property	140	144	-4	Advertise the incorporation notice in a national newspaper	11	200
Getting Credit	117	117	0	Register the company with the Commercial Registry	60	59
Protecting Investors	114	118	-4	Apply for commercial operations permit and tax payer identification number, and obtain and legalize special company books	15	207
Paying Taxes	144	149	-5			
Trading Across Borders	58	69	-11			
Enforcing Contracts	151	152	-1			
Closing a Business	151	151	0			

<sup>1</sup> Out of 175 economies. High ranking represents high cost of doing businesses.

Sources: International Finance Corporation, see <http://www.doingbusiness.org> for more details.

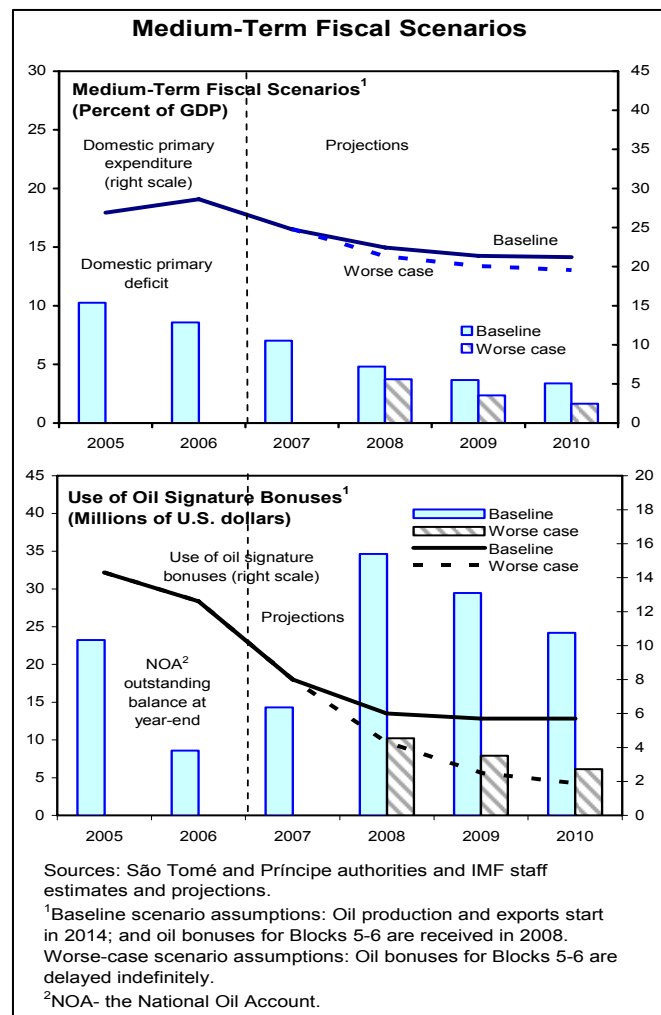
19. **On financial sector reform, the BCSTP plans to further enhance banking supervision, strengthen internal financial management, and implement the AML/CFT**

law (MEFP, ¶23). Although the country is small, the number of banks, most of them foreign owned, has increased in recent years. There is a need to develop the regulatory framework and strengthen the BCSTP's capacity for supervision and enforcement. Work is underway to enhance prudential regulations. The BCSTP has prepared the regulations for implementing the AML/CFT law; these will be issued once the NA approves the law, which is expected in June 2007.

#### IV. PREPARING FOR FURTHER ADJUSTMENT OVER THE MEDIUM TERM

20. **São Tomé and Príncipe's medium-term outlook depends critically on the prospects for oil export earnings and revenue.** Taking into account recent developments in oil exploration, the staff developed scenarios to emphasize the need to prepare for adjustment beyond 2007. The updated baseline scenario assumes that oil production and exports start in 2014—two years later than previously assumed. In a worse case scenario, oil bonuses for Blocks 5-6 (US\$26 million), assumed for 2008 under the baseline, would be delayed indefinitely and there would be no oil production.<sup>6</sup> These scenarios help illustrate the impact of adverse developments on available oil resources and the magnitude of fiscal adjustment needed over the medium term.

21. **The authorities agreed that prudent fiscal management is necessary in view of recent developments in oil exploration.** While stressing the importance of mobilizing and absorbing more foreign aid, they were committed to adjusting the medium-term fiscal and external financing strategies, including the use of the remaining oil signature bonuses, after careful review of oil revenue prospects.



<sup>6</sup> The agreement for Blocks 5-6 is currently at a standstill due to disagreements among the stakeholders. See CR/07/173 on the implications of no oil production.

## V. PROGRAM MONITORING AND RISKS

**22. Board consideration of the fourth review is conditional upon a prior action to remedy the nonobservance of the structural performance criterion for end-March 2007.**

Completion of the fifth program review is conditional on observance of the end-June 2007 performance criteria (LOI, ¶6; MEFP ¶28). To facilitate implementation of public financial management reform, two new structural benchmarks related to the sixth disbursement (fifth review) are proposed for end-June and end-September 2007, respectively. Quantitative performance criteria for end-December 2007 related to the seventh disbursement (sixth review) are also proposed (Table I.1).

**23. There are risks to the program,** primarily the risk of less fiscal revenue, social pressures for more spending after HIPC debt relief, weak capacity in monetary policy implementation, and unfavorable developments in oil prospects. The authorities' policy commitments would help contain these risks.

## VI. STAFF APPRAISAL

**24. São Tomé and Príncipe has made commendable progress in macroeconomic stabilization.** The concerted efforts of the government and the central bank to address the fiscal imbalances and inflationary pressures since mid-2006 have yielded encouraging results: real GDP growth accelerated in 2006; inflation reversed a multi-year rising trend and began to decline—albeit still remaining high; the domestic primary fiscal deficit was significantly reduced; and international reserves of the central bank exceeded the program target for the end of 2006.

**25. A significant reduction in inflation remains a serious challenge.** Achieving this objective of the 2007 program will require continued fiscal consolidation and a proactive monetary policy to contain liquidity growth. Given the downside risks on the revenue side, the authorities must stand ready to reduce nonwage, nonessential spending to offset any revenue losses in the event of adverse developments, and tighten expenditure control and budget execution through public financial management reform. Close cooperation between the fiscal and monetary authorities is crucial to ensure timely sterilization of budgetary use of oil bonuses.

**26. To sustain economic growth and broaden its base, structural reforms need to be accelerated.** Staff strongly support the authorities' efforts to remove distortions in the tax and regulatory systems. Sharply reducing the cost of investing and doing business in São Tomé and Príncipe will help attract not only private investment but also donor funding. Aside from developing the financial sector, the authorities need to work with development partners to reform the utilities sector and upgrade infrastructure, which are critically important for private sector-led growth.

**27. A prudent fiscal strategy is needed.** Staff call on the authorities to prepare for further fiscal adjustment over the medium term, based on a careful review of oil prospects.



After HIPC and MDRI debt relief, the authorities should rely primarily on non-debt-creating capital inflows and maintain a prudent policy on borrowing to ensure debt sustainability.

28. **Staff recommend completion of the fourth review** and approval of a waiver for the nonobservance of the end-March 2007 structural performance criterion based on the prior action for Board consideration of this review.

Table 1. São Tomé and Príncipe: Selected Economic Indicators, 2005–10<sup>1</sup>

	2005	2006			2007			2008	2009	2010
		CR/07/102 <sup>2</sup>	CR/07/102	Est.	CR/07/102 <sup>2</sup>	CR/07/102	Rev. Prog.			
(Annual percentage changes, unless otherwise specified)										
<b>National income and prices</b>										
GDP at constant prices	5.4	8.0	8.0	7.0	7.0	7.0	6.0	6.0	6.0	6.5
Consumer prices										
End of period	17.2	25.0	25.0	24.6	13.5	13.5	13.5	9.5	7.0	6.0
Period average	16.3	21.4	21.4	23.1	18.6	18.6	16.6	11.4	8.2	6.5
<b>External trade</b>										
Exports, f.o.b.	-6.4	-4.6	-4.6	13.4	3.3	3.3	18.9	5.6	4.0	1.6
Imports, c.i.f.	15.7	51.9	51.9	69.4	9.6	9.6	0.9	7.7	6.5	7.0
Exchange rate (dobras per US\$; end of period) <sup>3</sup>	11,748	...	...	12,945	...	...	...	...	...	...
Real effective exchange rate (depreciation = -)	6.5	...	...	2.9	...	...	...	...	...	...
<b>Money and credit</b> (end of period)										
Base money	76.6	27.9	27.9	32.0	21.6	21.6	21.0	16.6	14.3	12.6
Broad money (M3)	45.9	29.4	29.4	39.3	25.3	25.3	25.0	17.6	15.3	13.6
Velocity (GDP to average broad money)	3.3	...	...	3.0	...	...	3.0	3.0	3.0	3.0
Central bank reference interest rate (percent)	18.2	28.0	28.0	28.0	...	...	...	...	...	...
Bank lending rate	30.0	...	...	31.0	...	...	...	...	...	...
Bank deposit rate	10.6	...	...	12.0	...	...	...	...	...	...
(Percent of GDP, unless otherwise specified)										
<b>Government finance</b>										
Total revenue, grants and oil signature bonuses <sup>4</sup>	81.9	54.6	35.2	37.4	262.4	169.3	164.5	47.1	29.1	28.2
Of which: tax revenue	15.1	26.1	16.8	17.5	25.1	16.2	15.8	15.8	15.8	15.8
nontax revenue	2.3	...	3.3	3.7	...	3.3	3.2	2.9	2.9	2.9
grants	17.2	22.6	14.6	16.2	201.4	129.9	125.4	11.4	10.3	9.5
oil signature bonuses	47.2	0.8	0.5	0.0	30.8	19.9	20.2	16.9	0.0	0.0
Total expenditure and net lending	44.5	75.0	48.3	51.3	65.4	42.2	39.6	37.8	36.0	35.0
Of which: noninterest current expenditure	23.6	39.8	25.6	25.3	34.1	22.0	20.0	18.3	17.4	17.4
capital and HIPC-related social expenditures	18.0	30.2	19.4	22.4	28.5	18.4	18.0	18.1	17.4	16.5
Domestic primary balance <sup>5</sup>	-10.3	-15.3	-9.8	-8.6	-12.9	-8.3	-7.0	-4.8	-3.7	-3.4
Overall balance (commitment basis)	37.4	-20.4	-13.1	-14.0	197.0	127.1	124.9	9.3	-6.9	-6.8
<b>External sector</b>										
Current account balance										
Including official transfers	-20.0	-58.6	-37.5	-45.9	-61.6	-39.3	-41.3	-42.0	-41.2	-40.9
Excluding official transfers	-39.4	-91.0	-58.2	-65.0	-86.5	-55.1	-55.9	-55.0	-53.0	-51.7
NPV of external debt	172.9	...	...	162.2	...	...	16.3	16.7	16.3	15.7
External debt service (percent of exports) <sup>6</sup>										
Before HIPC and MDRI debt relief	57.2	40.1	40.1	47.9	38.3	38.3	37.3	37.3	36.5	34.9
After HIPC and MDRI debt relief	48.1	19.0	19.0	24.6	5.9	5.9	4.7	5.1	4.7	4.2
Export of goods and services (US\$ millions)	21.0	22.5	22.5	23.6	23.9	23.9	24.5	26.4	28.5	31.0
Gross foreign reserves <sup>7</sup>										
Months of imports of goods and nonfactor services	4.1	4.4	4.4	4.5	4.4	4.4	4.0	4.0	4.0	4.0
Millions of U.S. dollar	26.6	29.3	29.3	33.3	31.2	31.2	31.7	33.2	35.1	37.0
National Oil Account (US\$ millions)	23.5	8.5	8.5	8.6	14.5	14.5	14.3	34.6	29.5	24.2
<b>Memorandum Item</b>										
<b>GDP</b>										
Billions of dobras	1,189	983	1,526	1,526	1,261	1,954	1,954	2,297	2,650	3,011
Millions of US dollars	114	79	123	123	90	142	142	154	168	184

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

<sup>1</sup> Based on 2001 census and survey-based GDP series unless otherwise specified.<sup>2</sup> Based on 1996 census and survey-based GDP.<sup>3</sup> Central bank buying rate.<sup>4</sup> Includes HIPC and MDRI debt relief, and oil signature bonuses.<sup>5</sup> Excluding oil revenue, grants, interest earned, and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays.<sup>6</sup> In percent of exports of goods and nonfactor services. The difference between debt service before and after HIPC relief is larger than debt service saving in cash terms because this table is on an accrual basis.<sup>7</sup> Gross reserves exclude the National Oil Account and guarantee deposits placed at the BCSTP by financial institutions waiting for operating licenses.



Table 2. São Tomé and Príncipe—Financial Operations of the Central Government, 2005–2010 (concluded)

	2005	2006		2007		2008	2009	2010
		Prog.	Est.	CR/07/102	Rev. prog.	Projections		
	(In percent of GDP) <sup>1</sup>							
<b>Total revenue and grants</b>	<b>81.9</b>	<b>35.2</b>	<b>37.4</b>	<b>169.2</b>	<b>164.5</b>	<b>47.1</b>	<b>29.1</b>	<b>28.2</b>
Total revenue	17.4	20.1	21.2	19.4	19.0	18.7	18.7	18.7
Tax revenue	15.1	16.8	17.5	16.2	15.8	15.8	15.8	15.8
Nontax revenue	2.3	3.3	3.7	3.3	3.2	2.9	2.9	2.9
Grants	17.2	14.6	16.2	129.9	125.4	11.4	10.3	9.5
Project grants	12.8	11.6	12.9	11.2	11.4	10.1	9.2	8.5
Nonproject grants	1.5	0.2	0.2	1.1	0.8	0.7	0.6	0.5
HIPC Initiative-related grants <sup>2</sup>	3.0	2.8	3.1	117.6	113.2	0.6	0.5	0.5
Oil signature bonuses	47.2	0.5	0.0	19.9	20.2	16.9	0.0	0.0
<b>Total expenditure</b>	<b>44.5</b>	<b>48.3</b>	<b>51.3</b>	<b>42.2</b>	<b>39.6</b>	<b>37.8</b>	<b>36.0</b>	<b>35.0</b>
Current expenditure <sup>3</sup>	26.5	28.8	28.9	23.8	21.6	19.6	18.6	18.5
Of which: personnel costs	8.7	8.7	8.7	8.2	8.2	8.2	8.2	8.2
interest on external debt due	2.7	2.9	3.4	1.7	1.5	1.3	1.2	1.1
goods and services	5.6	5.6	5.9	5.1	4.2	3.3	2.4	2.3
transfers	7.0	7.5	7.1	6.5	4.7	4.4	4.4	4.4
Of which: JDA	2.8	2.5	2.5	...	2.2	...	...	...
Capital expenditure	15.7	17.1	20.1	14.3	15.0	15.6	14.9	14.0
Financed by the Treasury	1.7	1.9	3.3	1.7	2.3	2.1	1.9	1.8
Financed by external sources	14.0	15.2	16.8	12.6	12.7	13.6	13.0	12.2
HIPC Initiative-related social expenditure	2.3	2.3	2.3	4.1	3.0	2.5	2.5	2.5
<b>Domestic primary balance <sup>4</sup></b>	<b>-10.3</b>	<b>-9.8</b>	<b>-8.6</b>	<b>-8.3</b>	<b>-7.0</b>	<b>-4.8</b>	<b>-3.7</b>	<b>-3.4</b>
<b>Overall fiscal balance (commitment basis)</b>	<b>37.4</b>	<b>-13.1</b>	<b>-14.0</b>	<b>127.1</b>	<b>124.9</b>	<b>9.3</b>	<b>-6.9</b>	<b>-6.8</b>
Net change in arrears (reduction = -)	-11.3	0.8	1.4	0.0	0.0	0.0	0.0	0.0
External arrears <sup>5</sup>	-4.4	1.6	1.4	0.0	0.0	0.0	0.0	0.0
Domestic arrears	-6.9	-0.8	0.0	0.0	0.0	0.0	0.0	0.0
<b>Overall fiscal balance (cash basis)</b>	<b>26.1</b>	<b>-12.3</b>	<b>-12.6</b>	<b>127.1</b>	<b>124.9</b>	<b>9.3</b>	<b>-6.9</b>	<b>-6.8</b>
<b>Financing</b>	<b>-26.1</b>	<b>12.3</b>	<b>12.6</b>	<b>-127.1</b>	<b>-124.9</b>	<b>-10.1</b>	<b>5.5</b>	<b>5.3</b>
Net external	-3.0	-0.9	2.0	-123.2	-120.7	3.0	2.8	2.5
Disbursements (projects)	1.1	3.5	6.5	1.4	1.4	1.2	1.1	1.0
Program financing (loans)	0.0	0.0	1.6	1.1	1.1	1.3	1.2	1.1
Net short-term loans	0.0	0.0	0.0	-10.3	-10.6	0.0	0.0	0.0
Scheduled amortization <sup>2</sup>	-7.8	-4.5	-6.0	-116.6	-113.8	-0.6	-0.5	-0.5
Change in arrears (principal) <sup>6</sup>	-8.6	0.0	0.0	-7.2	-7.2	0.0	0.0	0.0
Bilateral rescheduling <sup>7</sup>	12.3	0.0	0.0	8.5	8.4	1.0	1.0	0.9
Net domestic	-23.1	13.2	10.6	-3.9	-4.2	-13.1	2.8	2.7
Net bank credit to the government	-23.3	13.2	10.6	-3.9	-4.2	-13.1	2.8	2.7
Banking system credit (excluding National Oil Account) <sup>8</sup>	-1.2	1.2	-1.5	0.2	0.3	0.0	0.0	0.0
National Oil Account	-22.1	12.0	12.1	-4.1	-4.5	-13.1	2.8	2.7
Nonbank financing (including earmarked funds and residual)	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.9	1.4	1.5
<b>Memorandum items:</b>								
Overall balance (commitment basis, incl. grants, excl. oil bonuses)	-9.9	-13.6	-14.0	107.2	104.8	-7.7	-6.9	-6.8
Domestic primary spending	26.9	29.2	28.6	27.2	24.8	22.4	21.4	21.3
MDRI debt relief (flow in US\$ million)	0.0	0.0	0.0	1.1	1.1	1.2	1.2	1.3
National Oil Account ( US\$ million, excl. transfers to budget)	23.5	8.5	8.5	...	14.3	34.6	29.5	24.2

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

<sup>1</sup> Based on 2001 census and survey-based GDP series.

<sup>2</sup> For 2007, includes IDA and AfDB MDRI relief as a stock of debt reduction.

<sup>3</sup> For 2007, assumes the repayment of three US\$5 million loans disbursed by Nigeria in 2002–04, upon receipt of oil signature bonuses for Blocks 2–4 in Joint Development Zone.

<sup>4</sup> Excluding oil revenue, grants, interest earned, scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays.

<sup>5</sup> For 2006, refers to a temporary accumulation of technical arrears with bilateral creditors, pending reconciliation of debt records.

<sup>6</sup> For 2005, reflects impact of Paris Club rescheduling in the last quarter of 2005.

<sup>7</sup> For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.

<sup>8</sup> Net of valuation changes. For 2007, includes IMF MDRI relief as a stock of debt reduction.

Table 3. São Tomé and Príncipe: Summary Accounts of the Central Bank, 2005–07

	2005		2006		2007			
	Dec.	Jun.	Dec.	Rev. Prog. CR/07/102	Actual	Actual	Jun.	Sep.
		Actual				Actual	Rev. Prog.	Dec.
<b>Net foreign assets</b>								
Net international reserves	597.8	561.1	504.9	619.5	691.3	671.8	695.4	681.7
Gross reserves <sup>1,2</sup>	577.0	517.0	465.0	528.7	625.5	612.6	635.0	629.3
Of which: National Oil Account (NOA)	595.2	544.5	493.7	557.2	654.9	643.0	666.0	660.9
Of which: guarantee deposits	276.1	104.0	110.9	111.1	189.8	195.9	199.9	205.4
Short-term liabilities <sup>1</sup>	6.5	15.0	0.0	15.5	0.0	0.0	0.0	0.0
Other foreign assets	-18.2	-27.4	-28.7	-28.5	-29.4	-30.3	-31.0	-31.6
Other liabilities <sup>3</sup>	58.3	90.8	95.7	143.3	96.3	99.4	101.4	103.5
	-37.4	-46.8	-55.8	-52.4	-30.5	-40.2	-41.1	-51.0
<b>Net domestic assets</b>								
Net domestic credit	-387.2	-301.9	-235.4	-341.5	-409.3	-369.3	-370.4	-345.3
Net credit to government	-234.9	-122.8	-50.9	-121.3	-245.1	-211.7	-212.3	-174.3
Claims <sup>3</sup>	-247.9	-135.6	-63.0	-108.3	-257.5	-224.5	-225.6	-188.0
Of which: use of SDRs/Poverty Reduction and Growth Facility	87.8	98.7	108.5	105.6	84.0	94.2	95.3	105.5
Deposits <sup>2</sup>	47.8	58.1	67.7	64.5	42.9	53.1	54.2	64.4
Ordinary	-335.7	-234.4	-171.5	-213.9	-341.6	-318.7	-320.9	-293.5
Of which: HIPC Initiative resources	-15.5	-40.6	-27.2	-33.9	-43.2	-40.0	-36.7	-28.5
Counterpart funds	-22.6	-16.7	-3.5	-12.2	-21.5	-18.2	-15.0	-6.7
Foreign currency <sup>2</sup>	-297.6	-171.1	-121.7	-157.4	-275.7	-256.1	-261.5	-242.4
Of which: NOA <sup>2</sup>	-276.1	-104.0	-110.9	-111.1	-189.8	-195.9	-199.9	-205.4
Rediscount to commercial banks	5.2	3.9	2.5	2.5	2.6	2.7	2.7	2.8
Guarantee deposits from financial institutions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other claims	7.8	9.0	9.6	9.5	9.8	10.2	10.5	10.8
Central Bank certificates of deposit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other items (net)	-152.3	-179.1	-184.5	-220.2	-164.2	-157.6	-158.1	-171.0
<b>Base Money</b>	210.6	259.2	269.5	278.0	282.0	302.5	325.0	336.4
Currency issued	81.1	90.5	103.6	102.7	108.8	105.6	112.4	124.3
Bank reserves	129.5	168.8	165.9	175.3	173.2	196.9	212.6	212.1
Of which: domestic currency	29.9	58.9	83.7	64.9	64.4	68.7	95.8	78.5
foreign currency	99.6	109.9	82.2	110.4	108.7	128.3	116.9	133.6
<b>Memorandum items:</b>								
Gross international reserves (US\$ millions) <sup>1,2</sup>	50.7	43.7	37.8	43.0	49.0	46.6	47.3	46.0
Excluding NOA and guarantee deposits	26.6	34.1	29.3	33.3	34.8	32.4	33.1	31.7
Net international reserves (US\$ millions) <sup>2</sup>	49.1	41.5	35.6	40.8	46.8	44.4	45.1	43.8
National Oil Account (US\$ millions) <sup>2</sup>	23.5	9.5	8.5	8.6	14.2	14.2	14.2	14.3
Net international reserves (US\$ millions; excl. NOA)	25.6	31.9	27.1	32.3	32.6	30.2	30.9	29.5
Commercial banks reserves in foreign currency	8.5	8.8	6.2	8.5	8.1	9.3	8.3	9.3
Net international reserves (US\$ millions)								
Excluding NOA and banks reserves in foreign currency	17.1	23.1	20.9	23.7	24.5	20.9	22.6	20.2
Base money (annual percent change)	76.6	116.8	27.9	32.0	5.1	16.7	19.0	21.0
Currency issued (annual percent change)	20.8	76.3	27.7	26.6	5.1	16.7	19.0	21.0

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

<sup>1</sup> Includes guarantee deposits by prospective financial institutions waiting for operating licenses.<sup>2</sup> Oil signature bonuses for Blocks 5 and 6 in JDZ, totalling US\$26.1 million, originally assumed for 2007, are now projected for 2008.<sup>3</sup> Includes prospective disbursements under PRGF arrangement and MDRI assistance from the IMF as debt reduction totalling SDR1.6 million assumed in the first quarter of 2007.

Table 4. São Tomé and Príncipe: Monetary Survey, 2005-07

	2005		2006		2007			
	Actual	Rev. Prog. CR/07/102	Dec.	Est.	Jun.	Mar.	Rev. Prog.	
							Jun.	Dec.
<b>Net foreign assets<sup>1</sup></b>	<b>824.9</b>	<b>-392.4</b>	<b>795.1</b>	<b>699.3</b>	<b>939.6</b>	<b>928.2</b>	<b>957.1</b>	<b>948.9</b>
Central bank <sup>1</sup>	597.8	-14.9	561.1	504.9	691.3	671.8	695.4	681.7
Commercial banks	227.1	-254.4	234.0	194.4	248.3	256.4	261.7	267.1
<b>Net domestic assets<sup>1</sup></b>	<b>-392.4</b>	<b>-198.9</b>	<b>-198.9</b>	<b>-139.7</b>	<b>-311.8</b>	<b>-277.4</b>	<b>-246.3</b>	<b>-195.7</b>
Net domestic credit <sup>1</sup>	-14.9	149.7	149.7	234.4	112.0	139.4	170.6	233.6
Net credit to government <sup>1</sup>	-254.4	-142.2	-142.2	-69.4	-264.7	-231.9	-233.3	-195.7
Of which: valuation changes				-16.7	-6.9	-13.1	-17.4	-20.6
Claims	87.8	98.7	98.7	108.5	84.0	94.2	95.3	105.5
Deposits	-342.2	-241.0	-241.0	-177.8	-348.8	-326.2	-328.6	-301.2
Budgetary deposits	-22.0	-47.2	-47.2	-33.5	-50.5	-47.4	-44.4	-36.2
Counterpart funds	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6
Foreign currency deposits	-297.6	-171.1	-171.1	-121.7	-275.7	-256.1	-261.5	-242.4
Of which: National Oil Account	-276.1	-104.0	-104.0	-110.9	-189.8	-195.9	-199.9	-205.4
Credit to the economy	239.5	291.9	291.9	303.8	376.7	371.4	403.9	429.3
Of which: credit in foreign currency	142.8	205.5	205.5	202.9	0.0	0.0	0.0	0.0
Other items (net)	-377.5	-348.6	-348.6	-374.1	-423.8	-416.8	-416.9	-429.4
<b>Broad money (M3)</b>	<b>432.6</b>	<b>596.2</b>	<b>596.2</b>	<b>559.6</b>	<b>627.8</b>	<b>650.8</b>	<b>710.8</b>	<b>753.1</b>
Local currency	198.6	226.5	226.5	202.5	270.5	280.4	306.2	324.5
Money	180.4	204.2	204.2	185.1	244.4	253.3	276.7	293.2
Currency outside banks	72.5	81.1	81.1	89.8	91.2	94.5	103.3	109.4
Demand deposits	107.8	123.1	123.1	95.3	153.2	158.8	173.5	183.8
Time deposits	18.2	22.3	22.3	17.4	26.1	27.0	29.5	31.3
Foreign currency deposits	234.0	369.7	369.7	357.1	357.3	370.4	404.6	428.7
Net foreign assets	177.8	-6.9	-6.9	-29.0	13.2	11.3	16.1	14.8
Net domestic assets	-131.9	44.7	44.7	58.4	-9.0	-3.3	1.9	10.2
Of which: net credit to government	-97.9	25.9	25.9	42.8	-24.8	-19.4	-19.6	-13.3
credit to the economy	23.9	17.7	17.7	14.9	3.9	3.0	8.4	12.6
Broad money (M3)	45.9	37.8	37.8	29.4	4.2	8.0	18.0	25.0
<b>Memorandum items:</b>								
Velocity (ratio of GDP to average broad money) <sup>2</sup>	3.3	...	...	...	...	...	...	3.0
Money multiplier (M3/M0)	2.1	2.3	2.3	2.1	2.2	2.2	2.2	2.2
Base money (12-month growth rate)	76.6	116.8	116.8	27.9	5.1	16.7	19.0	21.0
Credit to the economy (12-month growth rate)	42.0	52.1	52.1	26.8	47.6	27.2	29.6	21.4
M3 (12-month growth rate)	45.9	108.4	108.4	29.4	11.7	9.2	20.6	25.0

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

<sup>1</sup> Includes MDRI assistance from the Fund as debt reduction totaling SDR1.6 million assumed for 2007.<sup>2</sup> Based on 2001 census and survey-based GDP series.

Table 5. São Tomé and Príncipe: Balance of Payments, 2005–10

	2005	2006		2007	2008	2009	2010
		CR/07/102	Est.				
( Millions of U.S. dollars )							
<b>Trade balance</b>	<b>-38.2</b>	<b>-60.0</b>	<b>-66.7</b>	<b>-66.6</b>	<b>-71.8</b>	<b>-76.6</b>	<b>-82.2</b>
Exports, f.o.b.	3.4	3.2	3.8	4.5	4.8	5.0	5.1
<i>Of which</i> : cocoa	3.0	3.0	2.5	2.9	2.9	3.0	3.0
Imports, f.o.b.	-41.6	-63.2	-70.5	-71.1	-76.6	-81.6	-87.3
<i>Of which</i> : food	-14.8	-16.4	-17.0	-19.6	-21.3	-23.3	-25.4
petroleum products	-9.8	-11.9	-15.0	-15.0	-17.0	-17.9	-19.0
Services and income (net)	-8.0	-13.4	-15.1	-14.3	-14.7	-14.6	-14.8
Exports of nonfactor services	17.7	19.3	19.8	20.0	21.6	23.5	25.9
<i>Of which</i> : travel and tourism	13.6	14.9	13.8	14.7	15.9	17.3	19.1
Imports of nonfactor services	-22.7	-30.0	-31.8	-32.3	-34.4	-36.6	-39.1
Factor services (net)	-3.0	-2.7	-3.1	-1.9	-1.8	-1.5	-1.6
Interest due	-3.2	-3.5	-3.8	-2.1	-2.1	-2.0	-2.0
National Oil Account (NOA) interest earnings	0.2	0.8	0.8	0.1	0.2	0.5	0.4
Private transfers (net)	1.5	1.6	1.6	1.7	1.7	1.8	1.9
Official transfers (net)	22.7	25.6	23.6	20.7	20.1	19.9	20.0
<i>Of which</i> : project grants	15.5	18.7	15.9	16.1	15.6	15.6	15.7
HIPC Initiative-related grants	3.2	3.4	3.8	0.0	0.0	0.0	0.0
<b>Current account balance</b>							
Including official transfers	-22.1	-46.2	-56.6	-58.5	-64.7	-69.4	-75.2
Excluding official transfers	-44.7	-71.8	-80.2	-79.2	-84.8	-89.4	-95.1
<b>Capital and financial account balance</b>	<b>53.1</b>	<b>30.4</b>	<b>37.3</b>	<b>60.0</b>	<b>84.2</b>	<b>64.5</b>	<b>70.1</b>
Capital transfer <sup>1</sup>	0.0	0.0	0.0	162.7	0.0	0.0	0.0
Financial account	53.1	30.4	37.3	-102.7	84.2	64.5	70.1
Public sector (net)	29.7	-5.6	-7.3	-162.3	25.4	-0.1	-0.1
Project loans	1.3	4.4	4.4	1.9	1.9	1.9	1.9
Program loans	0.0	0.0	0.0	1.5	2.0	2.0	2.0
Oil signature bonuses	49.2	0.0	0.0	28.6	26.1	0.0	0.0
Amortization	-8.9	-5.5	-7.4	-176.4	-0.9	-0.9	-0.9
Other investments	-11.9	-4.5	-4.3	-17.9	-3.7	-3.1	-3.1
<i>Of which</i> : Nigerian and Angolan advances (net)	0.0	0.0	0.0	-15.0	0.0	0.0	0.0
transfers to JDA	-11.4	-3.8	-3.1	-3.1	-3.1	-3.1	-3.1
Private sector (net)	23.3	36.0	44.7	59.6	58.8	64.6	70.2
Direct foreign investment	5.2	29.4	29.4	28.4	30.4	32.4	34.8
Commercial banks	-8.5	4.2	0.8	0.0	5.0	5.0	5.0
Short-term private capital	26.5	2.4	14.5	31.2	23.4	27.2	30.4
<b>Errors and omissions</b>	<b>1.5</b>	<b>0.0</b>	<b>8.1</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
<b>Overall balance</b>	<b>32.5</b>	<b>-15.8</b>	<b>-11.2</b>	<b>1.5</b>	<b>19.6</b>	<b>-4.9</b>	<b>-5.0</b>
Financing	-32.5	15.8	11.2	-1.5	-19.6	4.9	5.0
Change in official reserves, excl. NOA (increase = -)	-8.7	-1.6	-6.6	2.7	-1.5	-2.0	-1.8
Use of Fund resources (net)	0.5	0.7	1.2	-0.2	0.6	0.0	0.0
Purchases	0.5	...	1.2	1.9	0.6	0.0	0.0
Repurchases (incl. MDRI repayment)	0.5	...	0.0	-2.1	0.0	0.0	0.0
National Oil Account (increase = -)	-23.3	14.8	14.9	-5.7	-20.3	5.2	5.3
Change in arrears (net; decrease = -) <sup>2</sup>	-14.6	1.9	1.7	-10.2	0.0	0.0	0.0
Debt relief <sup>1</sup>	13.5	0.0	0.0	11.9	1.6	1.6	1.6
<b>Memorandum items:</b>							
		(Unit specified)					
Current account balance (percent of GDP) <sup>3</sup>							
Before official transfers	-39.4	-58.2	-65.0	-55.9	-55.0	-53.0	-51.7
After official transfers	-20.0	-37.5	-45.9	-41.3	-42.0	-41.2	-40.9
Debt service ratio (percent of exports) <sup>4</sup>							
Before HIPC and MDRI relief	57.2	40.1	47.9	37.3	37.3	36.5	34.9
After HIPC and MDRI relief	48.1	19.0	24.6	4.7	5.1	4.7	4.2
Gross reserves <sup>5</sup>							
Millions of US dollars	26.6	29.3	33.3	31.7	33.2	35.1	37.0
Months of imports of goods and nonfactor services	4.1	4.4	4.5	4.0	4.0	4.0	4.0

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

<sup>1</sup> Include HIPC and MDRI debt relief delivered at the completion point in 2007.

<sup>2</sup> For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears

<sup>3</sup> Based on 2001 census and survey-based GDP series.

<sup>4</sup> In percent of exports of goods and nonfactor services. The difference between debt service before and after HIPC relief is larger than debt service saving in cash terms because this table is on an accrual basis.

<sup>5</sup> Gross reserves exclude the National Oil Account and guarantee deposits placed at the central bank by financial institutions pending operating licenses; imports exclude oil sector-related imports of capital goods and services.

**Table 6. São Tomé and Príncipe: External Financing Requirements and Sources, 2005–07**  
(Millions of U.S. dollars)

	2005	2006 Est.	2007 Proj.
<b>Gross financing requirements</b>	<b>-88.9</b>	<b>-96.9</b>	<b>-283.0</b>
Current account, excluding official transfers	-44.7	-80.2	-79.2
Exports, f.o.b.	3.4	3.8	4.5
Imports, f.o.b.	-41.6	-70.5	-71.1
Services and income (net)	-8.0	-15.1	-14.3
Private transfers	1.5	1.6	1.7
Financial account	-20.9	-11.8	-196.4
Scheduled amortization <sup>1</sup>	-8.9	-7.4	-176.4
IMF repayments <sup>2</sup>	-0.1	0.0	-2.1
Other public sector investment (net)	-11.9	-4.3	-17.9
Change in external reserves (increase = -)	-8.7	-6.6	2.7
Change in arrears (net)	-14.6	1.7	-10.2
<b>Available funding</b>	<b>88.9</b>	<b>96.9</b>	<b>283.0</b>
National Oil Fund (net)	25.9	14.9	22.9
Oil signature bonuses	49.2	0.0	28.6
Saving (accumulation of oil reserve fund = -)	-23.3	14.9	-5.7
Expected disbursements	23.4	28.0	186.8
Multilateral HIPC interim assistance	3.2	3.8	0.0
Capital transfers <sup>1,2</sup>	0.0	0.0	162.7
Grants <sup>3</sup>	18.9	19.7	20.7
Concessional loans	1.3	4.4	3.4
Project loans	1.3	4.4	1.9
Program loans	0.0	0.0	1.5
Private sector (net)	25.3	52.8	59.6
IMF <sup>4</sup>	0.6	1.2	1.9
Financing gap	13.7	0.0	11.9
HIPC debt relief (bilateral creditors) <sup>2</sup>	0.2	0.0	1.7
Reschedulable arrears (bilateral creditors) <sup>5</sup>	13.5	0.0	10.2
Residual financing gap	0.0	0.0	0.0

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

<sup>1</sup> Include HIPC and MDRI debt relief delivered at the completion point in 2007.

<sup>2</sup> Include MDRI assistance from the IMF as a stock of debt reduction.

<sup>3</sup> Includes aid in kind received from Nigeria.

<sup>4</sup> Includes projected disbursements under the PRGF.

<sup>5</sup> In 2005, includes the new Paris Club rescheduling agreement. For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.



**Table 7. São Tomé and Príncipe: Performance Criteria and Actual for 2006**  
(Billions of dobras, unless otherwise specified)

	2006			
	Sep. 30 Base (stocks)	Perf. Criteria	Dec. 31 Perf. Criteria (with adjustors)	Actual
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	...	-150.0	-150.0	-131.0
2. Ceiling on changes in net bank financing of the government (cumulative from end–September 2006; billions of dobras at program exchange rate) <sup>1,2,3</sup>	-126.8	62.1	63.0	14.4
3. Ceiling on changes in net domestic assets of the central bank (cumulative from end–September 2006; billions of dobras at program exchange rate) <sup>1,2,3</sup>	-289.8	73.1	74.0	-36.1
4. Floor on changes in the net international reserves of the central bank (cumulative from end–September 2006; US\$ millions) <sup>3,4</sup>	41.8	-6.4	-6.7	-1.0
5. Ceiling on central government's outstanding external payment arrears (stock, US\$ millions) <sup>5</sup>	...	0.0	0.0	0.0
6. Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (cumulative flows from January 2005, € millions) <sup>6,7</sup>	...	1.6	1.6	1.4
7. Ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP (stock, US\$ millions) <sup>8</sup>	...	1.0	1.0	0.0
<b>Memorandum items:</b>				
Base money (ceiling; billions of dobras)	273.2	269.5	269.5	278.0
Currency issued (ceiling; billions of dobras)	94.4	103.6	103.6	102.7
Oil signature bonuses including accrued interest on NOA (US\$ millions, cumulative from beginning of year)	0.5	0.6	0.6	...
Net external debt service payments (cumulative from beginning of the year, billions of dobras at program exchange rate)	-35.4	-46.1	-69.5	...
Official external program support (cumulative from beginning of the year, billions of dobras at program exchange rate) <sup>9</sup>	7.8	2.8	25.6	...

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

<sup>1</sup> The ceiling was adjusted by cumulative deviations of actual from projected net payments in external debt service; and by deviations in external program support and oil bonuses, including accrued interest on the National Oil Account (NOA). The downward adjustment of higher than programmed external program support did not take place to the extent that the additional support was used to accommodate higher capital outlays of the government, up to US\$1 million.

<sup>2</sup> The ceiling could be adjusted by the amount of accumulated domestic arrears. However, since no domestic arrears accumulated in 2006, no adjustment was made.

<sup>3</sup> Includes the National Oil Account (NOA) at the Central Bank.

<sup>4</sup> The floor on net international reserves was adjusted by the cumulative deviation in external debt service and by deviations for oil bonuses, including accrued interest on NOA. The upward adjustment of higher than programmed external program support did not take place to the extent that the additional support was used to accommodate higher capital outlays of the government, up to US\$1 million.

<sup>5</sup> This is a continuous performance criterion.

<sup>6</sup> This performance criterion applied not only to debt as defined in point No. 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24, 2000), but also to commitments contracted or guaranteed for which value has not been received.

<sup>7</sup> With a grant element of less than 50 percent. Includes a US\$2 million loan received from Angola to finance a social inclusion project.

<sup>8</sup> Debt is defined as in point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24, 2000). Excludes US\$15 million in loans from Nigeria during 2002–04, which are to be repaid from signature bonuses in 2007.

<sup>9</sup> Official external program support, as defined in the TMU, valued at the program exchange rate of 12,549 dobras per U.S. dollar.

Table 8. São Tomé and Príncipe: Millennium Development Goals

	1990	1994	1997	2000	2003	2004
<b>Goal 1. Eradicate extreme poverty and hunger</b>						
<b>Target 1:</b> 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)	..	..	..	..	..	..
<b>Target 2:</b> 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)	..	..	..	..	..	..
<b>Goal 2. Achieve universal primary education</b>						
<b>Target 3:</b> Ensure that, by 2015, children will be able to complete a full course of primary schooling.						
6. Net primary enrolment ratio (percent of relevant age group)	..	..	85.5	97.1	..	..
7. Percentage of cohort reaching grade 5	..	..	..	61.5	..	..
8. Youth literacy rate (percent age 15–24)	..	..	..	..	..	..
<b>Goal 3. Promote gender equality and empower women</b>						
<b>Target 4:</b> 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)	12.0	..	7.0	9.0	9.0	9.0
<b>Goal 4. Reduce child mortality</b>						
<b>Target 5:</b> Reduce by two-thirds, between 1990 and 2015, the under-5 mortality rate.						
13. Under-5 mortality rate (per 1,000)	118.0	118.0	..	118.0	118.0	118.0
14. Infant mortality rate (per 1,000 live births)	75.0	75.0	..	75.0	75.0	75.0
15. Immunization against measles (percent of children under 12 months)	71.0	65.0	60.0	69.0	87.0	87.0
<b>Goal 5. Improve maternal health</b>						
<b>Target 6:</b> Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.						
16. Maternal mortality ratio (modelled estimate, per 100,000 live births)	..	..	..	..	..	..
17. Proportion of births attended by skilled health personnel	..	..	..	58.5	..	79.8
<b>Goal 6. Combat HIV/AIDS, malaria, and other diseases</b>						
<b>Target 7:</b> Halt by 2015, and begin to reverse, the spread of HIV/AIDS.						
18. HIV prevalence among females (percent ages 15–24)	..	..	..	..	..	1.3
19. Contraceptive prevalence rate (percent of women ages 15–49)	..	..	..	29.0	..	..
20. Number of children orphaned by HIV/AIDS	..	..	..	..	..	..
<b>Target 8:</b> 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	..	..	..	80.0	..	..
23. Incidence of tuberculosis (per 100,000 people)	136.1	126.6	120.0	113.7	107.8	107.8
24. Tuberculosis cases detected under DOTS (percent)	..	..	..	..	..	..

Continued

Table 8. São Tomé and Príncipe: Millennium Development Goals (concluded)

	1990	1994	1997	2000	2003	2004
<b>Goal 7. Ensure environmental sustainability</b>						
<b>Target 9:</b> 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)	..	..	..	..	..	..
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	0.6	..	..
29. Proportion of population using solid fuels	..	..	..	..	..	..
<b>Target 10:</b> Halve, by 2015, the proportion of people without access to safe drinking water.						
30. Access to improved water source (percent of population)	..	..	..	..	79.0	..
<b>Target 11:</b> Achieve by 2020 significant improvement for at least 100 million slum dwellers. <sup>1</sup>						
31. Access to improved sanitation (percent of population)	..	..	..	..	24.0	..
32. Access to secure tenure (percent of population)	..	..	..	..	..	..
<b>Goal 8. Develop a Global Partnership for Development</b>						
<b>Target 16:</b> Develop and implement strategies for productive work for youth.						
45. Unemployment rate of population ages 15–24 (total)						
Female	..	..	..	..	..	..
Male	..	..	..	..	..	..
<b>Target 17:</b> Provide access to affordable essential drugs						
46. Proportion of population with access to affordable essential drugs.	..	..	..	..	..	..
<b>Target 18:</b> Make available new technologies, especially information and communications.						
47. Fixed line and mobile telephones (per 1,000 people)	19.2	19.8	31.2	31.0	77.6	77.6
48. Personal computers (per 1,000 people)	..	..	..	..	..	..

Sources: World Development Indicators database.

<sup>1</sup> Targets 33–44 are excluded because they cannot be measured on a country-specific basis. They are related to official development assistance, market access, and the HIPC Initiative.

Table 9. São Tomé and Príncipe: Schedule of Disbursements Under the PRGF Arrangement, 2005–08

SDR Millions	Percent of Quota	Date Available	Disbursement Conditions
0.423	5.7	Aug. 2005	Board approval of arrangement
0.423	5.7	Mar. 2006	Observance of PCs for end-September 2005 and completion of the first review
0.423	5.7	Aug. 2006	Observance of PCs for end-December 2005 and completion of the second review
0.423	5.7	Jan. 2007	Observance of PCs for end-June 2006 and completion of the third review
0.423	5.7	Jun. 2007	Observance of PCs for end-December 2006 and completion of the fourth review
0.423	5.7	Dec. 2007	Observance of PCs for end-June 2007 and completion of the fifth review
0.422	5.7	Jun. 2008	Observance of PCs for end-December 2007 and completion of the sixth review

Source: IMF.

Table 10. São Tomé and Príncipe: Indicators of Fund Credit, 2007–10  
(Millions of SDRs, unless otherwise indicated)

	2007	2008	2009	2010
	Projections			
Fund credit outstanding <sup>1</sup>				
Millions of SDRs	2.91	3.34	3.25	2.96
Millions of U.S. dollars	4.32	4.98	4.85	4.42
Percent of quota	39.32	45.14	43.92	40.00
IMF obligations				
Total charges and interest	0.06	0.08	0.08	0.07
Existing drawings	0.03	0.04	0.04	0.03
Prospective drawings	0.03	0.04	0.04	0.04
Total repayment/repurchases	0.00	0.00	0.09	0.29
Existing drawings	0.00	0.00	0.09	0.29
Prospective drawings	0.00	0.00	0.00	0.00
Fund credit as a percent of				
Export of goods and nonfactor services	17.64	18.90	17.00	14.26
Gross official reserves	13.62	15.01	13.80	11.95
<b>Memorandum items:</b>				
Export of goods and nonfactor services (US\$ millions)	24.5	26.4	28.5	31.0
Gross official reserves (US\$ millions)	31.7	33.2	35.1	37.0

Sources: IMF staff estimates and projections.

<sup>1</sup> Includes prospective PRGF disbursements, totalling SDR1.268 million.

**APPENDIX I**

São Tomé, May 6, 2007

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

Dear Mr. de Rato:

1. The attached Memorandum of Economic and Financial Policies (MEFP) sets out the objectives and policies that the government of São Tomé and Príncipe intends to pursue for the remainder of 2007. They are consistent with the government's Poverty Reduction Strategy (PRS) and the objectives of the three-year arrangement under the IMF's Poverty Reduction and Growth Facility (PRGF). Our economic adjustment and reform efforts are being supported by the international community, notably through debt relief under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI).
2. The government of São Tomé and Príncipe has made substantial progress in macroeconomic stabilization and structural reforms over the past year. Economic growth accelerated in 2006. Inflation has begun declining, reflecting our renewed fiscal consolidation efforts since mid-2006 to redress the expenditure overruns in the first half of the year and a more active use of monetary policy by the Central Bank of São Tomé and Príncipe to curb liquidity growth. We have moved forward to strengthen public finance management and laid the basis for tax reform and actions against money laundering. As a result, all PRGF quantitative performance criteria (as revised in the third program review) and structural benchmarks for end-December 2006 program were met.
3. Looking ahead, our policies for 2007 aim to consolidate the recent stabilization gains, ensure sound management of oil-related and debt relief resources, and lay the groundwork for sustained private sector-led growth. Our program envisages a further reduction of the domestic primary fiscal deficit relative to GDP, combined with a prudent use of oil bonuses, a strengthening of monetary and exchange rate policies to lower inflation, and an acceleration of structural reforms. These are key conditions for sustained growth, which in turn is key for poverty reduction.
4. In support of our objectives and policies, the government hereby requests the completion of the fourth review and the disbursement of the fifth loan under the PRGF arrangement in an amount equivalent to SDR 0.423 million (5.7 percent of quota). The government requests a waiver for the nonobservance of the end-March 2007 structural

performance criterion on issuing a decree to establish the new public accounting plan. This decree has been delayed as we are running into difficulties in obtaining timely technical assistance from a donor-financed consultant. This decree will be issued prior to the Executive Board consideration of the fourth review of our program.

5. The government will provide the IMF with such information as the IMF may request regarding progress in implementing the economic and financial policies and achieving the objectives of the program.

6. The fifth and sixth reviews related to the sixth and seventh disbursements under the PRGF arrangement based on the end-June and end-December 2007 performance criteria are expected for November 2007 and May 2008, respectively.

7. The government believes that the policies and measures set forth in the MEFP are adequate to achieve the objectives of the 2007 program supported by the PRGF arrangement but will take further measures to that end if deemed necessary. During the implementation of the arrangement, the government will consult with the Managing Director of the IMF on the adoption of any measures that may be appropriate, at the initiative of the government or whenever the Managing Director requests such a consultation.

8. The government intends to make the contents of this Letter of Intent and those of the attached MEFP and Technical Memorandum of Understanding (TMU), as well as the staff report on the fourth PRGF review, available to the public and authorizes the IMF to arrange for them to be posted on the IMF website, subsequent to Board completion of the fourth review.

Yours truly,

/s/

/s/

Mrs. Maria dos Santos Tebús Torres  
Deputy Prime Minister and Minister of  
Planning and Finance

Mr. Alindo Afonso de Carvalho  
Governor of the Central Bank of São Tomé  
and Príncipe

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

## APPENDIX I, ATTACHMENT I

### São Tomé and Príncipe:

#### Memorandum of Economic and Financial Policies

May 2007

#### I. INTRODUCTION

1. This Memorandum of Economic and Financial Policies (MEFP) supplements that of December 2006 and our Letter of Intent dated December 27, 2006. It describes (i) performance under the PRGF arrangement through December 2006; (ii) economic developments in 2006 and early 2007, and (iii) the government's economic program for the remainder of this year. The policies set forth in this Memorandum should help achieve the medium-term objectives set out in our PRSP, including efficient use of debt relief resources provided under the Enhanced Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI). Our government is committed to creating the conditions for sustained economic growth, which is essential for reducing poverty.

#### II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

2. **Economic activity picked up in 2006; real GDP grew at an estimated 7 percent.** Growth in the construction, commerce, and services sectors has been particularly strong, boosted by private investment and capital inflows associated with tourism and oil-related projects.

3. **Inflation had begun declining to 17 percent (year-on-year) by the end of March 2007, from 26 percent in August 2006.** This deceleration reflected corrective fiscal measures implemented since mid-2006 and a more active use of monetary policy to curb liquidity growth, which has slowed depreciation of the dobra. The dobra depreciated by 10 percent against the U.S. dollar in the 12 months through December 2006.

4. **Fiscal performance was broadly on the program path through December 2006.** Efforts to strengthen tax administration, the 28 percent increase in petroleum prices in June 2006, and the higher volume of oil imports helped boost tax revenue. Improved control of expenditure commitments on both the wage bill and nonwage current items helped offset the expenditure overruns in the first half of 2006. These measures brought the domestic primary deficit below the performance criteria for end-2006 (Table I.1); it reached 8.6 percent of GDP in 2006, down from 10.3 percent of GDP in 2005.

5. **Monetary aggregates have decelerated markedly since June 2006 as the Central Bank of São Tomé and Príncipe (BCSTP) tightened monetary policy.** The BCSTP raised its reference interest rate by 4 percentage points, to 28 percent, in September 2006 and has since kept the real interest rate positive. More important, it stepped up sales of foreign



exchange to sterilize budgetary use of oil bonuses and foreign inflows. As a result, base money growth (12-month change) declined from 117 percent in June to 32 percent in December 2006 and further to 15 percent in March 2007. By containing its net credit to the government, the BCSTP maintained net international reserves (NIR) above the program's performance criteria for end-December 2006.

6. **The BCSTP has resumed foreign exchange auctions since December 2006 to enhance the functioning of the foreign exchange markets.** These auctions have helped reduce the spread between official and commercial bank exchange rates, while the central bank has continued direct sales to the government and the fuel importer, ENCO, for lumpy transactions. The BCSTP has continued to adjust its exchange rate to market conditions daily by calculating it as the sum of 40 percent of the previous day's selling rate quoted by commercial banks for transactions with the public and 60 percent of its own previous day's selling rate. As a result, the exchange rate of the dobras has remained market determined.

7. **Progress has been made in structural reforms, as envisaged under the program.** All structural benchmarks through December 2006 were met (Table I.2). In October 2006 Legislation for anti-money laundering and the financing of terrorism was submitted to the National Assembly (NA), which granted general approval of the law in January 2007. To improve public debt management, the Commonwealth Secretariat Debt Recording and Management System was introduced in November 2006. Important steps have been taken in public financial management reform—the President promulgated the law establishing the legal and institutional framework for the integrated government financial administration system (SAFE), and a pilot budget preparation and execution program (SAFINHO) was implemented in January 2007. The government has submitted to the NA a new Investment Code, which should improve the investment climate.

### III. ECONOMIC POLICIES FOR THE REST OF 2007

8. **Our macroeconomic framework for 2007 aims to significantly reduce inflation by continued fiscal consolidation and a tight and proactive monetary policy.** Achieving the objectives of our program, particularly reducing annual inflation to 10–15 percent by the end of 2007, will require vigorous and timely implementation of agreed policy measures and close cooperation between fiscal and monetary authorities. We will continue to make every effort to speed up structural reforms, notably in the areas of public expenditure management and the investment climate, to achieve sustained, private sector-led growth.

#### A. Fiscal Policy

9. **The government plans to further reduce the domestic primary deficit to about 7 percent of GDP in 2007 (compared with 8.6 percent in 2006) while increasing pro-poor spending.** Fiscal consolidation under the 2007 budget, which the NA approved on March 15, 2007, would come mainly from containing nonessential spending and the wage bill, because the impact of the envisaged direct tax reform, which aims to reduce distortions,

would be largely neutral in 2007. The domestic primary deficit would be financed mainly by the use of part of the oil bonuses (equivalent to 5.4 percent of GDP).

**10. On the revenue side the government is stepping up its efforts to implement the agreed measures:**

- **We remain committed to the petroleum pricing and taxation reforms** that were delayed due to planning and procedural issues. In the new pricing structure, ENCO will apply a uniform margin across products to eliminate cross subsidies. The new tax structure, with fewer exemptions and the move to a specific tax, is designed to safeguard petroleum tax revenue in percent of GDP. These reforms are to be introduced by end-June 2007.
- **The NA has postponed its consideration of our proposal to increase the excise tax on services (excluding water and electricity) from 5 percent to 7 percent** and to increase excises on some imported goods, including alcoholic beverages and tobacco. These measures have been delayed because the NA prefers to consider them in conjunction with our proposed cut in the corporate income tax rate. We will work with the NA to seek approval of the excise tax changes.
- **We expect the NA to adopt the direct tax reform laws by end-June 2007.** This package of legislation includes a reduction in the corporate income tax rate from 45 to 25 percent, a new personal income tax code, and a new urban property tax code, all to be implemented in 2008.
- **We have started implementing the action plan to recover tax arrears.** The NA has now adopted the tax administration and procedural codes, which will help strengthen arrears collection. We have lowered ENCO's indirect tax arrears from dobras 24 billion at end-October 2006 to dobras 11 billion at end-2006. Efforts will be made to reduce outstanding income tax arrears, which were estimated at dobras 67 billion at end-October 2006.

**11. On the expenditure side the following measures are planned for 2007:**

- **The wage bill** will be contained at dobras 161 billion, causing a decline in the wage bill-to-GDP ratio to 8.2 percent (from 8.7 percent projected for 2006). We will closely monitor all the components of salaries and strictly limit the payments of bonuses and emoluments pending the outcome of a study of salary structure and components. Based on this study, the completion of which is expected by end-June 2007, the government intends to adopt a revised salary structure with adequate incentives for public servants as a first step in its civil service reform strategy.
- **Nonwage current expenditure** will be contained by strict application of the budget circulars that require prior authorization by the Minister of Planning and Finance of

all expenditure commitments (*compromisos*) by budgetary units (except for spending within monthly budget allocations for wages, fuel, food, medicines, basic office supplies, and telecommunications). Payments for utilities (electricity and water) will closely follow consumption while continuing to avoid arrears.

- **Propoor spending will further increase.** We plan to achieve this goal by containing nonessential primary spending through systematic application of the execution mechanisms contained in the new Organic Budget Law. While aligning allocations with the PRSP priorities set out in the Priority Actions Plan for 2006–08, we will strictly monitor the use of HIPC and MDRI resources.

12. **The government intends to take additional measures, if needed, to ensure achievement of program objectives.** The delays in implementing the excise and petroleum pricing and taxation reforms discussed above could have an adverse impact on fiscal revenue of *dobras* 10 billion, 0.5 percent of GDP. To offset such revenue losses, the government will reduce nonwage, nonessential spending. Expenditure management will be tightened in the event of further delays or unexpected large declines in oil import prices, to keep domestic financing of the budget below the program ceilings.

13. **The 2007 fiscal plan remains fully financed.** It assumes the use of US\$8 million from the National Oil Account (NOA) and project support from Taiwan-Province of China and the World Bank (consistent with its 2006–09 Country Assistance Strategy). In seeking donor support for its Priority Actions Plan for 2006–08, the government presented a revised list of needs in infrastructure, education, and good governance to the December 2006 Round Table in São Tomé. Receipt of oil signature bonuses from Blocks 2–4 (projected at US\$13.6 million after repayment of oil-related debt of US\$15 million to Nigeria) and any additional bonuses (possibly up to US\$26 million for Blocks 5-6) will be deposited in the NOA for future budgetary use, consistent with the Oil Revenue Management Law (ORML).

14. **The government will build on progress under the pilot program SAFINHO to enhance the monitoring and execution of the 2007 budget, including the use of debt relief resources, while moving progressively to introduce the full system of integrated public finance management (eSAFE).** A decree will be issued as a prior action for the IMF Executive Board consideration of the fourth review to establish the new public finance accounting plan and the related manual of accounting procedures. With assistance from FAD and the World Bank, we will put in place other elements of the eSAFE to make it fully functional for the 2008 budget. We have set additional benchmarks for end-June and end-September 2007 (Table 2) to facilitate reform in this critical area.

15. **Our medium-term fiscal and external financing strategies depend critically on our capacity to mobilize and absorb aid inflows for development and on the prospects of oil export earnings and revenue.** The government will carefully review the impact of developments in commercially extractable reserves on the macroeconomic framework. We

are committed to adjusting the medium-term fiscal and financing strategies, including the use of NOA resources if oil production and exports are seriously delayed, beyond the previous projection of 2012. The government will reassess its oil-related outlays, including its contribution to the Joint Development Authority (JDA), taking into account updated oil revenue prospects, disbursements of signature bonuses, and the execution of the JDA budget.

## **B. Monetary and Exchange Rate Policies**

16. **The monetary program for 2007 aims to reduce inflation through strict control of base money growth, in the context of a flexible exchange rate regime.** Although base money is an indicative target, it serves as the anchor for the program, playing a central role in restoring price stability. Every effort thus needs to be made to ensure 12-month base money growth declines, from 32 percent at end-2006 to 21 percent by end-2007. Achieving this will require the BCSTP to use monetary instruments, primarily foreign exchange sales, proactively, consistent with the NIR target, to mop up liquidity.

17. **Close cooperation between the Treasury and the BCSTP is essential for improving the latter's liquidity forecast and ensuring timely action to offset the monetary impact of budgetary use of oil bonuses and HIPC and MDRI savings.** To facilitate information-sharing and coordination, Ministry of Finance and BCSTP officials will meet at least once a month to discuss the budget's cash outlays (in both domestic and foreign currency), which will help inform the BCSTP's foreign exchange market operations.<sup>7</sup> Because public expenditure is a major component of aggregate demand and affects domestic prices and the exchange rate, if meeting the program's NIR target is at risk, the government will support monetary tightening by curtailing nonwage expenditures.

18. **The BCSTP is committed to further developing the foreign exchange market.** With IMF technical assistance, the BCSTP expects to make further progress toward accepting the obligations of Article VIII, Sections 2(a), 3, and 4, of the IMF's Articles of Agreement. With a view to ensuring a fuller and faster market determination of the exchange rate, the BCSTP will (i) continue implementing the current policies of holding frequent foreign exchange auctions, better matching supply with demand by using information on bank net open positions, and enforcing limits on them; (ii) encourage ENCO's bankers to purchase relatively small amounts of foreign exchange at each auction, in advance of payment requirements, to help spread out ENCO's demand for foreign exchange and progressively bring it into the auction; (iii) remove the remaining multiple currency practices by applying either the official exchange rate, if it is less than 2 percent below the market (commercial bank) rate, or a rate at the 2 percent limit in BCSTP's direct sales to ENCO and the government; (iv) eliminate the exchange restriction on transfers abroad of dividends

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<sup>7</sup> This working group could include the Director of Budget, Director of Treasury, Director of Monetary and Exchange Policy, and Director of Exchange Operations.

when the new Investment Code becomes effective, which is expected by June 2007. The BCSTP is committed to maintaining the exchange system free of restrictions on current international transactions.

19. **The BCSTP will continue to develop a communication strategy to inform the market on its monetary and exchange policies.** The Governor of the BCSTP has been meeting at regular preannounced intervals with the banking community and the media to communicate the BCSTP's views on inflation and its monetary objectives. In addition, summary data on monetary and macroeconomic aggregates have been posted weekly on the BCSTP website.

20. **The BCSTP has posted audited financial statements for 2005 on its website and will continue to do the same every year.** Its budget execution and profit and loss account on a cash basis will be reported at least quarterly as part of the program's monetary data. The BCSTP will continue to contain the cost of its office building project, taking into consideration contractual obligations and the impact on its current and future financial situation, in consultation with the government.

### C. Structural Reforms in 2007

21. **We will take further steps to ensure transparent management of current and prospective oil resources.** The NA has approved the legislation establishing the Petroleum Oversight Committee for auditing and supervising petroleum receipts and expenditures under ORML. The ORML Handbook has been prepared and is expected to be published soon. We are also implementing the Extractive Industries Transparency Initiative (EITI) process, as expressed at the third EITI conference in Oslo in October 2006. To improve implementation, we will integrate overlapping elements of the ORML and EITI.

22. **To promote private sector-led growth, the cost of investing and doing business in São Tomé and Príncipe must be reduced.** In consultation with the private sector, we have prepared for the NA's consideration draft legislation to reduce red tape and other regulatory impediments to starting a business. Once it is approved, the time needed for starting a business will be reduced from over 140 days to less than 3. We believe this and our other efforts to improve the investment climate will help attract private investment and improve the "doing business indicators" ("cost of starting a business" and "days to start a business") of the International Financial Corporation. Progress in these areas would facilitate our discussion with the U.S. Millennium Challenge Corporation for grant financing of our development projects.

23. **Regarding financial sector reform, the BCSTP intends to further enhance banking supervision, strengthen its internal management in line with the IMF safeguards assessment conducted in 2004, and implement the anti-money laundering law:**

- The BCSTP is strengthening its capacity to supervise licensing of new banks and assess bank foreign currency positions and operating risks. To further strengthen on- and off-site inspections, the BCSTP will by end-June 2007 issue new prudential regulations on credit classification, liquidity, transactions with related parties, and limits on bank net open foreign currency positions.
- The BCSTP has prepared regulations for implementing the AML/CFT law. Once the NA gives final approval of the AML/CFT law, these regulations will be issued, enabling the establishment of a Central Risk Unit within the BCSTP and imposing “know-your-client” rules on banks.
- Regarding safeguards assessment, the BCSTP has adopted investment guidelines for foreign reserves. It intends to develop annual audit plans based on a risk analysis of operations and review the role of the Audit Board to fully align its responsibilities with those of an independent audit committee.

#### **D. External Debt and Debt Relief**

24. **The government will work with the Paris Club and other bilateral official creditors for their full delivery of HIPC relief.** A meeting with Paris Club creditors is expected to take place in May 2007 on completion point debt relief. Regarding bilateral agreements using the September 2005 Paris Club terms of reference, the government has contacted its creditors and signed agreements with Germany, France, and Spain.

25. **On debt management, the government is conscious of the importance of ensuring debt sustainability after HIPC and MDRI debt relief.** To improve its capacity to manage external debt, we have put in place a debt recording and management system obtained from the Commonwealth Secretariat (CS-DRMS). Technical problems with the CS-DRMS software have been resolved, the Debt Office of the Ministry of Finance is transferring debt records to the new system, and a technical consultant from the Commonwealth Secretariat (with financial support from the World Bank) is expected to assist the Debt Office in the second half of 2007.

#### **E. Statistical Issues and Capacity Building**

26. **The National Institute of Statistics, notwithstanding limited capacity and funding, has made significant progress in improving our national accounts statistics.** It has revised GDP in recent years based on the 2001 population and business census. With improved coverage and updated sectoral weights, the new GDP series reflects more accurately our recent economic developments. The government is aware of the remaining weaknesses in national accounts, balance of payments, and government financial operations statistics (TOFE), for which we will seek further technical assistance from the IMF. To strengthen policy implementation and our capacity building, the government has contacted

the EU for support for a Resident Economic Advisor with technical backstopping from the IMF.

#### **F. Program Monitoring**

27. **The revised Technical Memorandum of Understanding (TMU) sets out the modalities of program monitoring.** This includes definitions of performance criteria and indicative targets; application of adjusters for deviations from programmed amounts of oil signature bonuses, budget support, and net external debt service payments; and data sources and frequency of data reporting.

28. **Table I.1 (attached) shows the proposed quantitative performance criteria for end-December 2007 (6<sup>th</sup> review of the program).** To facilitate implementation of the public financial management reform, structural benchmarks are proposed for end-June and end-September 2007 for the fifth review (Table I.2). The nonaccumulation of external payment arrears (as defined in the attached updated TMU) is a continuous performance criterion, as are the 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 and Indicative Targets for 2006–07  
(Billions of dobras, unless otherwise specified)

	2006				2007			
	Sep. 30	Perf. Criteria	Perf. Criteria	Dec. 31	Mar. 31	Jun. 30	Sep. 30	Dec. 31
	Base (stocks)		Actual	(with adjusters)	Ind. Target CR/07/102	Perf. Criteria CR/07/102	Ind. Target Proposed	Perf. Criteria Proposed
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	...	-150.0	-131.0	-150.0	-27.3	-97.0	-115.0	-136.6
2. Ceiling on changes in net bank financing of the government (cumulative from end–September 2006; billions of dobras at program exchange rate) <sup>1,2,3</sup>	-126.8	62.1	14.4	63.0	-118.7	-32.4	-73.9	-33.8
3. Ceiling on changes in net domestic assets of the central bank (cumulative from end–September 2006; billions of dobras at program exchange rate) <sup>1,2,3</sup>	-289.8	73.1	-36.1	74.0	-79.0	-19.6	-7.8	26.3
4. Floor on changes in the net international reserves of the central bank (cumulative from end–September 2006; US\$ millions) <sup>3,4</sup>	41.8	-6.4	-1.0	-6.7	4.6	1.9	2.5	1.0
5. Ceiling on central government's outstanding external payment arrears (stock, US\$ millions) <sup>5</sup>	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0
6. Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (cumulative flows from January 2005, € millions) <sup>6,7</sup>	...	1.6	1.4	1.6	1.6	1.6	1.6	1.6
7. Ceiling on the outstanding stock of external debt with original maturity of up to and including one year owed or guaranteed by the central government or the BCSTP (stock, US\$ millions) <sup>8</sup>	...	1.0	0.0	1.0	1.0	1.0	1.0	1.0
<b>Memoandum items:</b>								
Base money (ceiling; billions of dobras)	273.2	269.5	278.0	269.5	282.0	302.5	325.0	336.4
Currency issued (ceiling; billions of dobras)	94.4	103.6	102.7	103.6	108.8	105.0	112.4	124.3
Oil signature bonuses including accrued interest on NOA (US\$ millions, cumulative from beginning of year)	0.5	0.6	...	0.6	28.7	28.8	28.9	29.0
Net external debt service payments (cumulative from beginning of the year, billions of dobras at program exchange rate) <sup>9</sup>	-35.4	-46.1	...	-69.5	-205.8	-211.0	-216.6	-220.4
Official external program support (cumulative from beginning of the year, billions of dobras at program exchange rate) <sup>10</sup>	7.8	2.8	...	25.6	0.0	0.0	31.4	41.8

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

<sup>1</sup> The ceiling will be adjusted downward or upward by cumulative deviations in the same direction of actual from projected net payments in external debt service; and by deviations in the opposite direction in external program support and oil bonuses, including accrued interest on the National Oil Account (NOA). 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.

<sup>2</sup> The ceiling will be adjusted downward by the amount of accumulated domestic arrears.

<sup>3</sup> Includes the National Oil Account (NOA) at the Central Bank.

<sup>4</sup> The floor on net international reserves will be adjusted upward or downward by the cumulative deviation in the opposite direction in external debt service (including repayments to Nigeria), and by deviations in the same direction for oil bonuses, including accrued interest on NOA. 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.

<sup>5</sup> This is a continuous performance criterion.

<sup>6</sup> 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* (August 24, 2000), but also to commitments contracted or guaranteed for which value has not been received.

<sup>7</sup> With a grant element of less than 50 percent. Includes a US\$2 million loan received from Angola to finance a social inclusion project.

<sup>8</sup> Debt is defined as in point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* (August 24, 2000). Excludes US\$15 million in loans from Nigeria during 2002–04, which are to be repaid from signature bonuses in 2007.

<sup>9</sup> Includes US\$15 million repayment to Nigeria.

<sup>10</sup> Official external program support, as defined in the TMU, valued at the program exchange rate of 12,549 dobras per U.S. dollar (valued at projected average exchange rate of 13,935 dobras per U.S. dollar in fiscal table).



Table I.2. São Tomé and Príncipe: Structural Performance Criteria and Benchmarks, December 2006–December 2007

Action	Benchmark	Status
<b>Prior action</b>		
Adopt decree establishing the new public accounting plan and the related manual of accounting procedures, consistent with the organic public finance law and the public financial management system (SAFE).		An inter-ministerial commission was established to prepare for the decree. The decree was adopted on May 31, 2007.
<b>December 31, 2006</b>		
Implement the Commonwealth Secretariat debt recording management system (CS-DRMS) to improve the government's capacity to manage external debt.		Met, CS-DRMS installed in November 2006.
Submit to the National Assembly legislation criminalizing money laundering and the financing of terrorism.		Met, draft AML/CFT legislation submitted to the NA in October 2006.
<b>March 31, 2007</b>		
Adopt decree establishing the new public accounting plan and the related manual of accounting procedures, consistent with the organic public finance law and the public financial management system (SAFE).	Performance criteria	Delayed due to difficulties in obtaining timely technical assistance from a donor-financed consultant.
Publish the Handbook of the Oil Resource Management Law (ORML) by posting it on the government website. (planned for January 2007)		Delayed, Handbook prepared for web posting.
Issue regulations to implement the law against money laundering and the financing of terrorism (AML/CFT), notably for the Central Risk Unit within the BCSTP and "know-your-client" rules for banks.		Regulations prepared, pending NA approval of the AML/CFT law.
<b>June 30, 2007</b>		
Issue new prudential regulations on credit classification, liquidity, transactions with related parties, and limits on net open foreign currency positions.	Performance criteria	Regulations being prepared.
Produce the monthly budget execution report (TOFE) using upgraded SAFINHO.		SAFINHO in place, IT platform needs upgrading.
Finalize the installation of prepaid electricity metering systems (3,000).		Over 200 installed as of mid-February, 2007.
<b>September 31, 2007</b>		
Prepare the 2008 budget in line with the new organic budget (SAFE) law.		
<b>December 31, 2007</b>		
Implement the fully integrated computerized public financial management system (eSAFE) with new nomenclature, unified current and investment budgets, and incorporating public accounting (including of patrimony/debt).		
Adopt Petroleum Sector Strategy for development of the Exclusive Exploitation Zone (EEZ).		

## APPENDIX I, ATTACHMENT II

### SÃO TOMÉ AND PRÍNCIPE

#### TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This technical memorandum of understanding (TMU) contains definitions and adjuster mechanisms that are intended to clarify the measurement of variables in Table I.1, Quantitative Performance Criteria, PRGF Arrangement, 2006–07, which is 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 end-September 2006.

#### **Provision of Data to the Fund**

2. Data with respect to all variables subject to performance criteria and indicative targets 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 the appropriate way of measuring and reporting. Performance criteria included in the program, as defined below, refer to domestic primary balance of the central government, net bank financing of the central government, net domestic assets and net international reserves of the central bank, external payments arrears, nonconcessional medium and long-term external debt, and short-term external debt.

#### **Definitions**

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

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

5. **Domestic primary expenditure** comprises all government spending assessed on a commitment basis (base “compromiso”), excluding: (i) foreign-financed capital expenditure; (ii) foreign-financed expenditure under the overseas scholarship program that is externally-financed; and (iii) scheduled interest payments. Reporting of government domestic

expenditure will be based on the state budget execution prepared every month by the Directorate of Budget and the Directorate of Treasury in the Ministry of Planning and Finance.

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

a. **Propoor current spending:** These cover the following ministries and expenditure categories (by budget code) as described in the matrix below.

Code	Description of expenditure	Ministry of Education	Ministry of Health	Ministry of Labour
01.00.00	Despesa com Pessoal	x	x	x
02.01.05	Outros bens duradouros	x	x	
02.02.02	Combustiveis e lubrificantes	x	x	x
02.02.04	Alimentacao	x		
02.02.05	Medicamentos	x	x	
02.02.06	Roupas e clasados	x	x	x
02.02.09	Outros bens nao duradouros	x	x	
02.03.01.01	Agua e energia	x	x	x
02.03.02	Conservacao de bens	x	x	
02.03.06	Comunicacoes	x	x	x
04.02.01	Instituicoes particulares	x		x
04.03.01	Particulares (Junta de Saude)	x		x
04.04.02	Outras transferencias para exterior		x	
06.01.00	Ensino e formacao		x	
06.04.01	Custos recorrentes de projectos	x		
06.04.04.02	Outros Diversos	x	x	

Expenditures on fuels and lubricants (“combustíveis e lubrificantes”) that are effected for administrative purposes are excluded. Likewise, food (“alimentação”) and clothing and shoes (“roupas e calçados”) supplied to administrative staff are excluded.

For 2007 onward, the definition of propoor current spending will be based on the new budget nomenclature.

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

7. The **domestic primary balance** is defined as the difference between government domestic revenue and domestic primary expenditure. This balance for end-September 2006 was assessed at dobras –109.6 billion, broken down as follows:

Government domestic revenue:	Db 217.3 billion
Less: government primary expenditure (as defined in paragraph 5)	Db 326.9 billion
Equals: domestic primary balance:	Db -109.6 billion

8. **Domestic arrears** are defined as the difference between expenditure on a commitment basis and cash payments.

9. **The program exchange rate** for the purposes of this TMU will be Db 12,548.5 per U.S. dollar. The exchange rate of the dobra against the euro will be 15,952.93 and against the SDR will be 18,526.31.

10. **Net bank financing of the central government (NCG)** is defined as 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),<sup>8</sup> less all deposits held by the central government with DMBs, as they are reported monthly by the BCSTP to the IMF staff. All foreign exchange–denominated accounts will be converted to dobras at the program exchange rate. At end-September 2006, outstanding net bank financing of the government was assessed at dobras –126.8 billion, broken down as follows:

BCSTP credit, including use of IMF resources:	Db 105.8 billion
Less: government deposits with BCSTP:	Db 226.3 billion
<i>Of which:</i>	
National Oil Account (NOA)	Db 106.0 billion
Treasury foreign currency–denominated accounts	Db 43.9 billion
Treasury local currency–denominated accounts	Db 28.7 billion
Account for HIPC relief <sup>9</sup>	Db 20.3 billion
Account for MDRI relief <sup>10</sup>	Db 0.0 billion
Counterpart deposits	Db 22.6 billion
PRGF disbursement account	Db 4.7 billion

<sup>8</sup> Deposit money banks (DMBs) refers to other depository corporations, as defined in the *Monetary and Financial Statistics Manual*.

<sup>9</sup> Pending the use of HIPC debt relief for propoor spending.

<sup>10</sup> Pending the use of MDRI relief for propoor spending.

Equals: Net credit to government by the BCSTP:	Db –120.5 billion
Plus: DMBs credit:	Db 0.0 billion
Less: government deposits with DMBs (including counterpart funds):	Db 6.3 billion
Equals: Net bank financing of the government:	Db 126.8 billion

11. **Base money** is defined as the sum of currency issued—which consists of currency outside banks and cash in vaults—and bank reserves, at the program exchange rate. Bank reserves refer to reserves of commercial banks held with the central bank and include reserves in excess of the reserve requirements. At end-September 2006 base money was assessed at dobras 273.2 billion, calculated as follows:

Currency issued:	Db 94.4 billion
<i>Of which:</i> Cash in vaults:	Db 13.7 billion
Currency outside banks:	Db 80.7 billion
Plus: Bank reserves:	Db 178.7 billion
<i>Of which:</i> in dobras	Db 80.5 billion
in foreign currency	Db 98.2 billion
Equals: Base money:	Db 273.2 billion
<i>Of which:</i> in dobras	Db 175.0 billion

12. **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-September 2006 NIR was assessed at dobras 524.6 billion, calculated as follows:

Net international reserves:	Db 524.6 billion
<i>Of which:</i> gross reserves:	Db 552.3 billion
<i>Of which:</i> National Oil Account (NOA)	Db 106.0 billion
short-term liabilities:	Db –27.6 billion
Plus: Other foreign assets:	Db 91.9 billion

Plus: Medium and long- term liabilities: Db -53.6 billion

Equals: Net foreign assets: Db 563.0 billion

*Memorandum item:*

Net international reserves minus National Oil Account (NOA)  
minus bank foreign currency deposits with the central bank Db 320.4 billion

13. **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 at programmed exchange rates. All foreign-denominated accounts will be converted to dobras at the program exchange rate. At end-September 2006, net domestic assets were assessed at dobras -70.0 billion, calculated as follows:

Base money: Db 273.2 billion

Less: Net foreign assets: Db 563.0 billion

Equals: Net domestic assets of the BCSTP: Db -289.8 billion

14. **Treasury deficit** of the BCSTP is defined as revenue (excluding unrealized valuation changes) minus costs minus investment.

15. The performance criterion on **short-term external debt** refers to the outstanding stock of external debt with an original maturity of one year or less (including overdraft positions) and owed or guaranteed by the government or the BCSTP.<sup>11</sup> At end-September 2006 the stock of short-term external debt stood at US\$16.0 million.<sup>12</sup>

16. 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 or the BCSTP.<sup>13 14</sup> Debt rescheduling and restructuring are

<sup>11</sup> 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).

<sup>12</sup> This amount includes three nonconcessional loans from Nigeria totaling US\$15 million, which were previously classified under nonconcessional medium-term external debt. They were reclassified as short-term debt after a joint World Bank-IMF debt sustainability analysis mission in April 2006.

<sup>13</sup> 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.

<sup>14</sup> 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 10-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 date of initial 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

(continued)

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 will consult with IMF staff before contracting obligations if it is uncertain as to whether those obligations are within the performance criterion limits.

17. 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, except for arrears pending rescheduling arrangements. The latter will be considered technical arrears. Debt would be deemed to be in arrears when it has not been paid by the time it is due, unless an arrear has been otherwise contractually defined. The performance criterion relating to external arrears does not apply to those pending the signing of bilateral agreements in the context of debt-rescheduling with the Paris Club and other bilateral creditors.

18. **Net external debt service payments** are defined as debt service due less interim HIPC debt relief (including multilateral and bilateral relief) and the accumulation of any new external payment arrears, including technical arrears.

19. **Official external program support** is defined as grants and loans, including in-kind aid when the products are sold by the government and receipts are freely usable by the budget, and other exceptional financing provided by foreign official entities and incorporated into the budget. Amounts assumed in the program consistent with this definition are shown in the memorandum item entitled “official external program support” of Table I.1.

### Use of Adjusters

20. **Deviations in receipts of oil signature bonuses, including accrued interest on NOA, in official external program support, and in net external debt service payments**, from amounts projected for the program (see Table I.1) will trigger adjustments for net bank financing of the central government, net domestic assets of the BCSTP, and net international reserves, as indicated below. These deviations will be calculated cumulatively from end-September 2006 (see Table I.1).

21. **Ceilings on net bank financing (NCG) of the central government and net domestic assets (NDA) of the BCSTP:** Monthly differences between actual and projected receipts of oil signature bonuses, official external program support, and net external debt service payments in foreign exchange will be converted to dobras at the program exchange rate and aggregated from end-September 2006 to the test date. The ceilings on NCG and NDA will be adjusted downward by the positive sum, and upward by the negative sum, of the deviations of actual from projected receipts of oil signature bonuses, including accrued

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loan is less than 50 percent (in other words, a grant element of at least 50 percent). For currencies with no available reference interest rates, the SDR rate will be used. This performance criterion does not apply to Fund resources.

interest on NOA; actual from projected official external program support; and projected from actual net external debt service payments. In the case of a negative sum of deviations (i.e., a shortfall), these ceilings will be increased by 100 percent of any cumulative shortfall. In case of a positive sum (i.e., a surplus), the downward adjustment to NCG and NDA 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 program exchange rates.

22. **Floor on net international reserves (NIR) of the BCSTP:** The quarterly difference between actual and projected receipts of oil signature bonuses, including accrued interest on NOA; official external program support; and net external debt service payments will be converted to dobras at the program exchange rate and aggregated from end-September 2006 to the test date. The floor on NIR will be adjusted upward by the positive sum and downward by the negative sum of the deviations of actual from projected receipts of oil signature bonuses, including accrued interest on NOA; actual from projected official external program support; and projected from actual net external debt service payments. In the case of a negative sum of deviations (i.e., a shortfall), this floor will be decreased by 100 percent of any cumulative shortfall. In case of a positive sum (i.e., a surplus), the downward adjustment to NIR 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 at program exchange rates. In addition, the NIR floor will be lowered by the amount that disbursements under the PRGF arrangement are lower than expected.

### **Data reporting**

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

#### **i. Fiscal data**

The Directorate of Budget at the Ministry of Planning and Finance will provide to IMF staff, within two months after the end of each month or quarter, except for the public investment program (PIP), which will be provided three months after each quarter:

- Monthly data on central government operations for revenues, expenditure, and financing, including detailed description of net earmarked resources (“recursos consignados”)
- Monthly data on net credit to the government by the BCSTP, recorded account by account in a format fully compatible with the monetary accounts of the BCSTP
- Monthly detailed data on tax and nontax revenues
- Monthly detailed data on current and domestically financed capital expenditure on commitment (“compromiso”) and cash payments (“caixa”)
- Monthly data on domestic arrears by type
- Quarterly data on official external program support (nonproject)



- Quarterly data on the execution of the public investment program (PIP) by project and sources of financing
- Quarterly data on project grant and loan disbursement (HIPC and non-HIPC)
- Quarterly data on bilateral HIPC debt relief
- Quarterly data on project loan disbursements
- Latest outstanding petroleum price structures and submission of new pricing structures (within a week of any changes)

## **ii. Monetary data**

The BCSTP will provide to IMF staff, within three weeks from the end of each month, the monetary accounts of the BCSTP; other monetary data will be provided within six weeks after the end of each month for monthly data, within two months after the end of each quarter for quarterly data, and within two months after the end of each year for annual data. Daily data will be provided every week no later than the Wednesday following the end of the week, and weekly data will be provided no later than two weeks after the end of the week. The BCSTP will provide

- Daily data on exchange rates
- Daily data on interest rates
- Daily liquidity management table, including base money and currency in circulation (see attachment)
- Daily net international reserve position
- Weekly balance sheet data of BCSTP (in BCSTP and IMF formats)
- 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 (*Orçamento cambial*)
- Quarterly table on bank prudential ratios and financial soundness indicators
- Quarterly data on the BCSTP's financial position (profit and loss statement, treasury deficit, budget execution)

## **iii. External debt data**

The Debt Management Unit at the Ministry of Planning and Finance will provide to IMF staff, within two months after the end of each month

- Monthly data on amortization and interest of external debt by creditor: scheduled, subject to debt relief or rescheduling, and paid

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

#### **iv. National accounts and trade statistics**

The following data will be provided to IMF staff

- Monthly consumer price index data, provided by the National Institute of Statistics within one month after the end of each month
- Monthly data on imports (value and import taxes collected and arrears) and commodity export values), provided by Customs, within two months after the end of each month
- Monthly data on petroleum shipments and consumption (volumes and cif prices, by product)



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International Monetary Fund  
Washington, D.C. 20431 USA

### **IMF Executive Board Completes Fourth Review of São Tomé and Príncipe's Three-Year PRGF Arrangement and Approves US\$600,000 Disbursement**

The Executive Board of the International Monetary Fund (IMF) has completed today the fourth review of São Tomé and Príncipe's economic performance under a three-year Poverty Reduction and Growth Facility (PRGF) arrangement. The completion of the review enables the release of an amount equivalent to SDR 432,000 (about US\$600,000), which would bring total disbursements under the arrangement to SDR 2.12 million (about US\$3.1 million).

In completing the review, the Executive Board approved a waiver for the nonobservance of an end-March 2007 structural performance criterion on the adoption of a decree establishing a new public accounting plan.

The Executive Board approved the three-year arrangement on August 1, 2005 (see Press Release No. 05/187), for a total amount of SDR 2.96 million (about US\$4.26 million) to support the government's economic program for 2005-07.

In commenting on the Executive Board's discussion on São Tomé and Príncipe, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair, stated:

“São Tomé and Príncipe has made significant progress in macroeconomic stabilization. Real GDP growth accelerated in 2006. Inflation has been declining since August. The primary fiscal deficit was significantly reduced; and international reserves exceeded the targets under the PRGF-supported program, owing to concerted efforts by the government and the central bank.

“The authorities are determined to consolidate the recent stabilization gains and further reduce inflation under their 2007 economic program. To safeguard the program's fiscal objectives, they will need to press ahead with tax reforms to broaden the tax base and to curtail non-essential spending in the event of revenue shortfalls, while preserving priority expenditures. Close cooperation between the fiscal and monetary authorities is essential for the implementation of a pro-active monetary policy to effectively contain liquidity growth.

“On structural reforms, the authorities have given high priority to improving public financial management to increase the efficiency and transparency in the use of public resources, including oil bonuses and debt relief savings. It will be important to move forcefully in regulatory reform to reduce the cost of investing and doing business in the country. Promoting private sector-led growth will also require progress in financial sector reform, particularly in strengthening banking supervision and further developing the foreign exchange market, and in upgrading the country’s infrastructure.

“São Tomé and Príncipe’s medium-term outlook depends importantly on the prospects of oil exports and revenue. The authorities need to manage fiscal adjustment beyond 2007 based on a careful review of oil prospects, while preserving priority expenditures. Prudent debt management will be important for maintaining long-term debt sustainability,” Mr. Portugal said.

**Statement by Laurean W. Rutayisire, Executive Director for the Democratic  
Republic of São Tomé and Príncipe  
June 25, 2007**

On behalf of my Saotomean authorities, I would like to thank the Board, Management and Staff for their continued support and useful advice to São Tomé and Príncipe. My authorities are particularly thankful for the debt relief provided under the HIPC Initiative and MDRI after reaching the Completion point three months ago.

### **I. Recent developments**

Economic activity in São Tomé and Príncipe has been buoyant in 2006 fueled by high capital inflows. Growth is expected to have reached 7 percent in real terms in 2006. Owing to sound policy implementation, inflation continued to decline from its peak of 26 percent in August 2006 to 17 percent in March 2007.

**In the fiscal sector**, domestic revenues increased sharply owing to higher fuel import duties and excise taxes resulting from a rise in petroleum prices and a higher volume of imports. Together with continued expenditure restraint, this led to a domestic primary fiscal deficit narrowing to 8.6 percent of GDP in 2006, down from 10.3 percent in 2005 and well below the program target of 9.8 percent. This improved situation, in turn, resulted in a lower use of oil signature bonuses.

Regarding fiscal-related reforms, my authorities started implementing the action plan to recover tax arrears. The recent adoption by the National Assembly (NA) of the tax administration and procedural codes will help strengthen arrears collection. However, the NA has postponed its consideration of draft law to increase the excise tax on services and on some imported goods, including alcoholic beverages and tobacco, as it prefers to consider them in conjunction with the proposed cut in the corporate income tax rate. The implementation of the system of integrated public finance management (SAFE) progresses steadily with the adoption of a new organic budget law in early 2007. The pilot public management system (SAFINHO) was introduced in January 2007 as scheduled following the adoption of the 2007 budget. However, the decree establishing the public accounting plan has been adopted later than programmed due to difficulties in securing timely external assistance.

**In the monetary sector**, continued tightening by Central Bank of São Tomé and Príncipe (BCSTP) along with fiscal consolidation since mid-2006 resulted in a sharp deceleration of monetary aggregates and decline in inflation. In particular, as increases in the reference interest rate had limited effect on mopping up excessive liquidity and reducing monetary aggregates, the BCSTP resumed sales of foreign exchange since December 2006 with the objective to sterilizing budgetary use of oil bonuses and capital inflows. As a result, base money declined from 117 percent in June 2006 to 15 percent in March 2007 and the spread between official and commercial bank exchange rate narrowed. The lower financing of the budget contributed to maintain the net international reserves (NIR) above the program target for end-December 2006.

Significant progress has been made regarding the strengthening of the central bank's operations. In particular, the central bank has prepared regulations for implementing the legislation criminalizing money laundering activities and the financing of terrorism (AML/CFT) that was submitted to the NA in October 2006. Once the NA gives final approval of the law, these regulations will be issued, enabling the establishment of a Central Risk Unit within the BCSTP and imposing the "know-your-client" rules. Efforts have been made to improve transparency and communication. Regular meetings gather the Governor of the BCSTP, the banking community and the media, with weekly disclosure of monetary and macroeconomic data on the central bank website. The audited financial statements for 2005 have been also posted and the central bank intends to continue to do so in the future.

On other **structural reforms**, significant measures have been taken to strengthen governance in the oil sector and reduce the cost of doing business. The NA approved the legislation establishing the Petroleum Oversight Committee for auditing and supervising petroleum receipts and expenditures under the Oil Revenue Management Law (ORML). The ORML Handbook has been prepared and is expected to be published soon. My authorities are also implementing the EITI process, as acknowledged at the third EITI conference in Oslo in October 2006. To improve its implementation, they will integrate overlapping elements of the ORML and EITI. In order to promote private sector-led growth, my authorities have prepared, in consultation with the private sector, a draft legislation that will significantly reduce red tape and other regulatory impediments to starting a business. It is expected that once this legislation is approved, the time needed for starting a business will be reduced from 140 days to less than 3 days.

As regards **debt issues**, my authorities signed a bilateral agreement with Spain, bringing to three the number of bilateral agreements under the September 2005 Paris Club terms of reference. My authorities remain resolved to ensure debt sustainability. A meeting with Paris Club creditors took place in late May 2007 on completion point of debt relief. To this end, they have put in place a debt recording and management system obtained from the Commonwealth Secretariat (CS-DRMS) since November 2006. The Debt Office within the Ministry of Finance will be assisted by a consultant from the Commonwealth Secretariat in the second half of 2007.

Overall, performance under the program has been satisfactory with all quantitative performance criteria and structural benchmarks for end-December 2006 met. However, the structural performance criterion for end-March 2007 on the public accounting plan was met with delay, as explained above. As this delay is beyond their control, my authorities are requesting a waiver for the non-observance of this performance criterion. In light of their satisfactory performance, my authorities are requesting Board approval for the completion of the fourth review under the PRGF.

## **II. Financial policies for the remainder of 2007 and beyond**

My authorities remain strongly committed to macroeconomic stabilization. Their financial policies for 2007 and beyond aim essentially to further reduce inflation, while maintaining their poverty reduction efforts. To this end, they will maintain their prudent policy stance initiated one year ago, and pursue the implementation of their reform agenda to lay the ground for private sector-led growth.

### **Fiscal policy**

For the remainder of 2007, fiscal policy aims to reduce the domestic primary deficit to 7 percent of GDP, while increasing pro-poor spending, consistent with the PRSP and the Priority Actions Plan for 2006-08. This will be achieved through continued expenditure restraint, as the impact of the envisaged direct tax reform, which aims to reduce distortions, would be largely neutral in 2007. Specifically, the wage bill will be contained at 8.2 percent of GDP (from 8.7 percent projected for 2006). My authorities intend to complete the study of the salary structure and components in June 2007, with the view of devising a new and more realistic one. Likewise, non-wage current expenditure will also be contained by strict application of the budget circulars that require prior authorization by the Minister of Finance for all expenditure commitments. As regards poverty reduction spending, my authorities will continue to strictly monitor the use of HIPC and MDRI resources.

On the revenue side, my authorities will continue to work closely with the NA to ensure a timely approval of the tax reform package. They will also introduce the petroleum pricing and taxation reforms by end-June 2007. These reforms aim to safeguard petroleum tax revenue in percent of GDP. Should there be any delay in the approval of the tax reform package or in the petroleum reforms, my authorities stand ready to further contain as much as possible public spending. To finance the fiscal program, it is envisaged a withdrawal of US\$8 million from the National Oil Account (NOA).

In light of the uncertainty regarding future receipts of oil bonuses and the beginning of oil production, my authorities are committed to adjusting the medium-term fiscal and financing strategies if necessary to maintain fiscal sustainability. In particular, receipt of future oil signature bonuses in the course of the year will be deposited in the NOA for future budgetary use, consistent with the (ORML). They stand ready to revise downward oil-related outlays, including its contribution to the Joint Development Authority (JDA).

As regard financial management, my authorities will build on progress under the pilot system SAFINHO to enhance the monitoring and execution of the 2007 budget. With the assistance from Fund FAD and the World Bank, the elements of SAFE will be put in place progressively so that it is fully functional for the 2008 budget.

### **Monetary, exchange rate and financial sector policies**

For 2007, the monetary program aims at further reduction of inflation through strict control of base money growth, in the context of a flexible exchange rate regime. To this end, the BCSTP will continue to use proactively foreign exchange sales along with other

monetary instruments, consistent with the NIR target to mop up liquidity. To ensure the effectiveness of the monetary policy, the BCSTP and the Ministry of Finance will strengthen their cooperation through regular meetings of senior officials from both institutions. Such meetings are expected to facilitate information-sharing and improve coordination between both institutions, regarding especially foreign exchange-related fiscal and monetary operations.

The BCSTP will continue to strengthen its operations and its internal management in line with the IMF safeguards assessment conducted in 2004. In particular, the central bank is committed to further developing the foreign exchange market, in order to comply with the obligations of Article VIII, Sections 2(a), 3, and 4, of the IMF's Articles of Agreement, as set out in paragraph 18 of their Memorandum of Economic and Financial Policies (MEFP). The central bank will also continue to develop a communication strategy to inform the market on its monetary and exchange rate policies. Regarding safeguards assessment, the BCSTP intends to develop annual audit plans based on a risk analysis of operations and review the role of the Audit Board to fully align its responsibilities with those of an independent audit committee.

Regarding the financial sector reform, the BCSTP intends to further enhance banking supervision, and implement the AML/CFT law. As regards banking supervision, the central bank will issue by end-June 2007 new prudential regulations to strengthen on- and off-site inspections.

### **Structural reforms**

My authorities will continue to implement the EITI process and the institutional framework for the oil revenue management, as provided for in the ORML. They are hopeful that the draft legislation to reduce impediments to start a business, together with the completion of abovementioned reforms in the fiscal, monetary and financial sectors will significantly improve the business climate and will contribute to the development of the private sector.

### **Conclusion**

São Tomé and Príncipe continued to maintain a satisfactory implementation of its economic program supported by the PRGF, thus demonstrating continuous commitment to macroeconomic stabilization and reform. In particular, significant measures have been implemented in key areas such as taxation, public finance management, oil revenue governance, central bank operations and business climate. My authorities remain committed to sound policy implementation. Given uncertainty surrounding oil reserves especially during the current transition period to the oil era, São Tomé and Príncipe still needs external support to make further progress towards its objectives of sustained growth and poverty reduction. I therefore call on the international community to continue providing such support.