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Sierra Leone: Sixth Review Under the Arrangement Under the Extended Credit Facility, Request for Waiver for Nonobservance of a Performance Criterion, Request for a Three-Year Arrangement Under the Extended Credit Facility, and Financing Assurances Review—Staff Report; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Sierra Leone.

In the context of the Sierra Leone, the following documents have been released and are included in this package:

- The staff report for the Sixth Review Under the Arrangement Under the Extended Credit Facility, Request for Waiver for Nonobservance of a Performance Criterion, Request for a Three-Year Arrangement Under the Extended Credit Facility, and Financing Assurances, prepared by a staff team of the IMF, following discussions that ended on March 24, 2010, with the officials of Sierra Leone on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 19, 2010. 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 4, 2010 discussion of the staff report that completed the request and/or review.

- A statement by the Executive Director for Sierra Leone.

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

Letter of Intent sent to the IMF by the authorities of Sierra Leone*
Memorandum of Economic and Financial Policies by the authorities of Sierra Leone*
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

SIERRA LEONE

Staff Report for the Sixth Review Under the Arrangement Under the Extended Credit Facility, Request for Waiver for Nonobservance of a Performance Criterion, Request for a Three-Year Arrangement Under the Extended Credit Facility, and Financing Assurances Review

Prepared by the African Department

(In consultation with other departments)

Approved by Seán Nolan and Dominique Desruelle

May 19, 2010

Fund relations. The Executive Board approved on May 10, 2006 a three-year PRGF arrangement in an amount equivalent to SDR 31.11 million (30 percent of quota). The arrangement was later extended to June 30, 2010. Two augmentations of access in an amount equivalent to SDR 10.4 million each (about 10 percent of quota) were approved by the Executive Board upon the completion of the third and the fourth review in December 2008 and June 2009, respectively. Six disbursements totaling SDR 44.88 million have been made. With the completion of the sixth review, a final disbursement of SDR 7 million will be made available.

Staff team. The mission comprised Mr. Mikkelsen (head), Mr. Million and Ms. Saxena (all AFR) and Mr. Palmason (SPR). It was assisted by Mr. Tjirongo (Resident Representative). Messrs. Itam and Tucker (OED) participated in several meetings.

Discussions. Discussions were held in Freetown March 11–24, 2010 and in Washington D.C, April 21–25, 2010. The mission met with Finance Minister Kamara, Central Bank Governor Sesay, other government officials, and representatives of civil society and donors.

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Abbreviations and Acronyms

ACC	Anti-Corruption Commission
BOP	Balance of payments
BSL	Bank of Sierra Leone
CRF	Consolidated revenue fund
DfID	U.K. Department for International Development
DSA	Debt Sustainability Analysis
DTD	Domestic Taxpayer Department
EC	European Commission
EU	European Union
FAD	Fiscal Affairs Department
FCHI	Free Health Care Initiative
FMR	Financial Management Regulation
FSDP	Financial Sector Development Plan
GBAA	Government Budgeting and Accountability Act
GDP	Gross domestic product
GST	Goods and services tax
HIPC	Highly indebted poor countries
IMF	International Monetary Fund
LTO	Large Taxpayer Office
MDAs	Ministries, departments, and agencies
MDG	Millennium Development Goal
MDRI	Multilateral Debt Relief Initiative
MEFP	Memorandum of Economic and Financial Policies
MOFED	Ministry of Finance and Economic Development
MPC	Monetary Policy Committee
MTEF	Medium Term Expenditure Framework
NEER	Nominal effective exchange rate
NPA	National Power Authority
NPLs	Nonperforming loans
NRA	National Revenue Authority
PC	Performance criterion
PFM	Public financial management
PRGF	Poverty Reduction and Growth Facility
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
PV	Present value
REER	Real effective exchange rate
SDR	Special drawing right
SPF	Strategic Petroleum Fund
TA	Technical assistance
TMU	Technical Memorandum of Understanding

Executive Summary

- **All except one quantitative performance criteria for end-December 2009 were met, but performance on structural benchmarks was mixed.** A key benchmark on introduction of the Goods and Services Tax (GST) was met, while recruitment of budget officers was observed with a delay. Three unmet benchmarks—two on tax administration and one on strengthening banking supervision—have been included in the new program.

- **After being adversely affected by falling global demand last year, economic activity is expected to pick up in 2010.** A recovery in export demand and continued investment in infrastructure should support an increase in real GDP growth to 4.8 percent in 2010 from 4 percent in 2009. Twelve-month inflation rose to 17 percent in February 2010, reflecting a sharp currency depreciation in the second half of 2009 and a jump in the price level in early 2010 related to the implementation of the new GST. Fiscal policy performance during 2009 was broadly satisfactory, with the revenue target being met with a solid margin.

- **The Government of Sierra Leone is requesting a successor three-year ECF arrangement to support their program to raise economic growth by increasing investment in infrastructure and developing an accessible financial sector**. The program will help create fiscal space for accelerated capital and social spending by broadening the tax base, containing non-priority spending, and raising public sector efficiency, especially in project selection and implementation.

- **Fiscal policy in 2010 focuses on improving revenue collection to support capital spending while containing pressures on current expenditures.** Revenues are projected to increase due to higher imports, an increase in royalties on diamonds, the full year effect of the increase in fuel excises in 2009, and moderate efficiency gains accruing from the introduction of a computer-based system in customs clearing and the GST. Capital spending will increase by 1 percentage point of GDP, while a new free health care initiative will raise the wage bill for the public sector by 0.4 percent of GDP. Monetary policy will seek to contain inflationary pressures stemming from the jump in price levels earlier this year and expected higher domestic fuel prices. The Bank of Sierra Leone will pursue this objective through open market operations and net sales of foreign exchange.

- **Structural reforms will complement the macroeconomic program.** The focus for 2010 is on improving tax administration by reducing inefficiencies in tax collection and increasing compliance; strengthening public financial management by enhancing the planning, monitoring and evaluation process for capital projects; deepening the financial sector by establishing a benchmark interest rate and improving access to credit through establishing a credit reference bureau; and establishing a transparent and automatic pricing framework for petroleum products to reduce fiscal risks from increasing international oil prices.

I. Introduction

1. **In the attached letter of intent, the Government of Sierra Leone (GoSL) is requesting a successor three-year Extended Credit Facility (ECF) arrangement.** The new arrangement will support Sierra Leone in its efforts to further raise economic growth and enhance employment and income opportunities, especially for the poor, while maintaining macroeconomic stability.

2. **Continued Fund support is warranted because of substantial development needs and external financing gaps.** Although macroeconomic stability has been achieved in the period after the end of the civil conflict in 2002, Sierra Leone remains a post-conflict country whose growth prospects depend on rebuilding infrastructure and institutions, as well as strengthening policies conducive to a more vibrant private sector (Box 1). The Fund will continue to collaborate closely with Sierra Leone's development partners, particularly those providing budgetary support.[1]

II. Recent Economic Developments and Program Performance

3. **The global economic downturn slowed economic activity in 2009, but achieving single digit inflation remains a challenge (Figure 1 and Table 1).**

- Economic activity continued to decline in the first half of 2009 due to falling global demand and declining foreign inflows from remittances. Despite a pickup in exports of diamonds and agricultural products in the second half of 2009 and an increase in domestic food production, real GDP growth for the year as a whole slowed to 4 percent in 2009 compared with 5.5 percent in 2008.

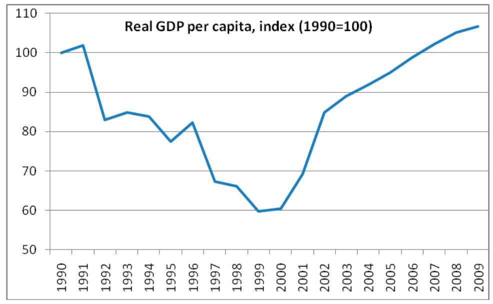
- Although inflation subsided in the first half of 2009, reflecting lower import prices (mainly fuel), the depreciation of the leone in the second half of the year contributed to a pickup in monthly inflation rates. Inflation increased further in the first two months of 2010 due to difficulties in implementing the VAT (called GST in Sierra Leone) and higher domestic fuel prices. As a result, 12-month inflation rose to about 17 percent in February 2010. The replacement of seven existing indirect taxes with the new 15 percent GST was not anticipated to significantly affect prices, but many businesses opted to add the GST to current prices without fully netting out the savings from the abolished indirect taxes.

- The external current account deficit is estimated to have declined to 8.4 percent of GDP in 2009 from 11.7 percent of GDP in 2008, reflecting an increase in official transfers and weak imports. Exports increased by about 4 percent while imports decreased by about 2.5 percent. Gross international reserves (excluding the 2009

[1] The World Bank, the European Union, the African Development Bank, and DfID.

Box 1. Sierra Leone: Recent Program Achievements and Lessons

Despite achieving macroeconomic stability under the ECF-supported program, Sierra Leone remains a post-conflict country whose growth prospects hinge on rebuilding infrastructure and developing a stable and accessible financial sector. The rebuilding efforts that followed the end of the civil conflict eight years ago are far from complete. The country still suffers from lack of infrastructure (roads, electricity, and water) and weak institutions. Despite economic growth in recent years, per capita income remains low (it returned to the pre-conflict level just a few years ago), poverty is pervasive (at 60 percent of the population), and Sierra Leone ranks at the bottom of the UN's Human Development Index.



The new PRSP completed mid-2009 identifies the lack of infrastructure as a serious impediment to growth and presents a strategy to accelerate public investments and promote private sector development. Gross domestic investment is currently at about 15 percent of GDP, significantly lower than the sub-Saharan African average of 22 percent. Also, private sector development is constrained by limited access to financial services. Credit to the private sector, at 9 percent of GDP, is low compared to the sub-Saharan African average of 17 percent.

While macroeconomic policy implementation has been broadly satisfactory during the current Fund-supported program, the timely implementation of structural reforms has been a challenge. Economic growth remained robust despite the global economic crisis and inflation was brought down to single digits. The fiscal policy stance was broadly appropriate despite the challenges for domestic revenue collection due to a volatile tax base and delays in reforming tax administration.

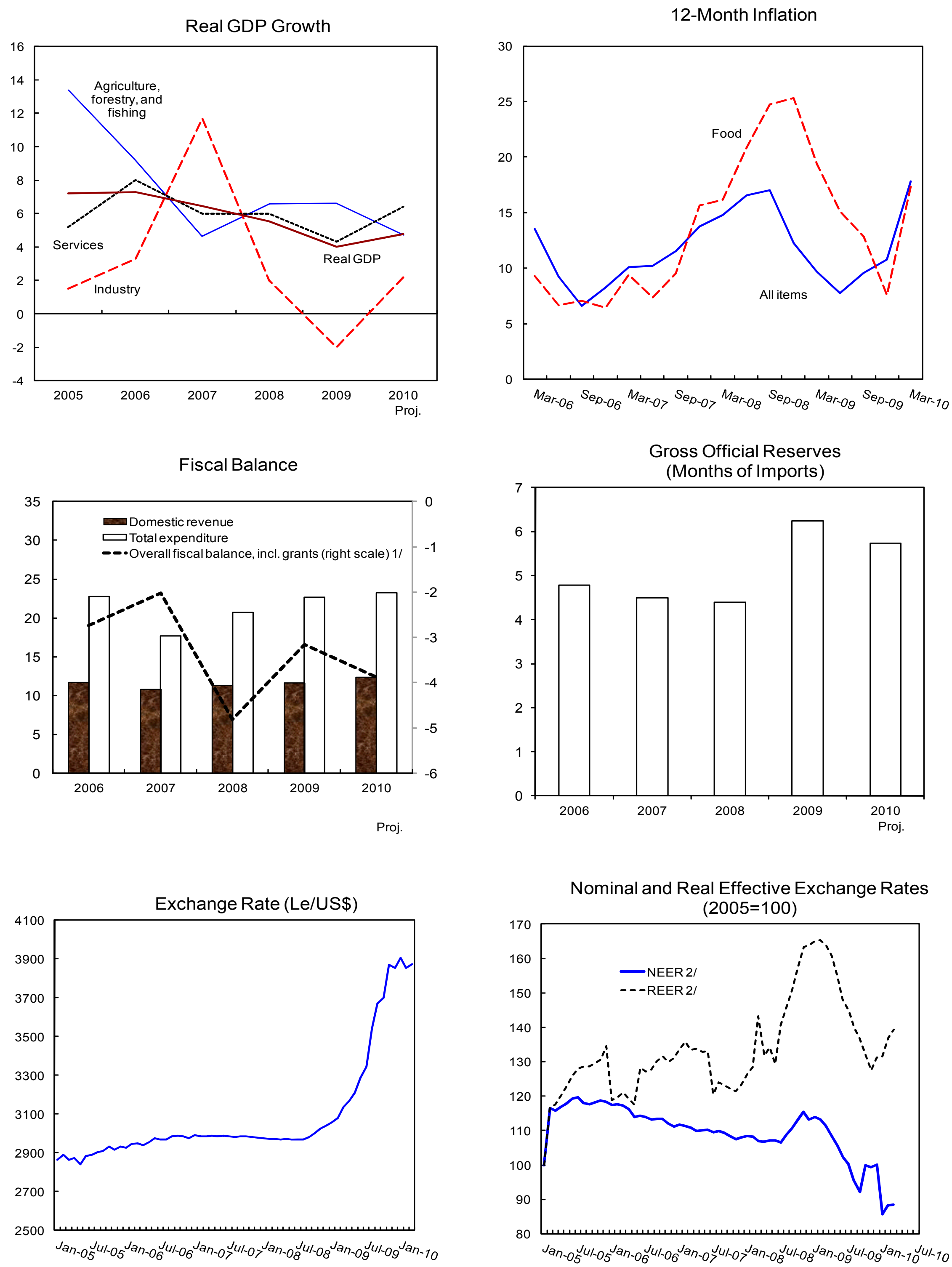
Debt relief from the international community helped decrease public and publicly guaranteed external debt from 142 percent of GDP end-2005 to 32 percent of GDP at end-2007. Nonetheless, under the LIC-DSA framework, Sierra Leone remains at a moderate risk of external debt distress with the external debt trajectory being vulnerable to external shocks. The evolution of external debt hinges on policies aimed at boosting growth and on contracting highly concessional loans.

Although achievements were made on the structural program, including the politically challenging introduction of the GST, progress was generally slower than envisaged in the program. In addition to delays in reforming tax administration, there were shortfalls in implementing measures to improve public financial management and deepen the financial sector, and public enterprise reforms. In most cases, the reason for the shortfalls in the structural program was not lack of political will to change, but rather low capacity in the public administration due to lack of qualified staff and weak institutions.

Looking forward, the priorities are to create fiscal space for investment in infrastructure and to strengthen public administration and financial sector development. The implementation of structural reforms should take into account existing capacity constraints by focusing on the most important measures and setting realistic timetables.

Sierra Leone will qualify as a member with a Longer-Term Program Engagement (LTPE). An Ex Post Assessment (EPA) update is therefore expected to be prepared after the temporary Board suspension of EPAs expires on August 30, 2010.

Figure 1. Sierra Leone: Selected Macroeconomic Indicators, 2006-10
(Percent of GDP, unless indicated otherwise)



Sources: Sierra Leonean authorities; and IMF estimates and projections.
1/ Including grants, but excluding MDRI.
2/ Alternative calculation with weights based on economic importance of the three main currencies (USD, EUR, and GBP.

SDR allocation) stood at US$ 209 million at end-2009, about the same as end-2008, corresponding to 3.9 months of imports. Including the allocated SDRs, reserve coverage was 6.4 months of imports.

- After a long period of stability, the leone depreciated against the US dollar by about 25 percent in 2009, mostly reflecting weaker inflows from exports and remittances. However, the leone has remained stable since end-2009. The REER appreciated at the outset of the global crisis, mainly reflecting a strong depreciation of the British Pound, but this trend reversed during 2009 as the leone depreciated.

4. **Fiscal policy performance during 2009 was broadly satisfactory (Tables 2 and 3).** The domestic revenue target was met by a solid margin as import-based taxes were higher than anticipated. While current expenditures were slightly higher than envisaged, capital expenditures were lower due to a shortfall in externally financed project outlays. Higher budget grants and domestic revenue collections along with lower than programmed expenditures reduced the overall deficit to 3.2 percent of GDP in 2009 from 4.4 percent in the program. However, the domestic primary fiscal deficit, at 4 percent of GDP, was slightly higher than programmed.

5. **Monetary policy was expansionary towards the end of 2009 (Table 4).** Reserve money grew by 20 percent in the fourth quarter after being unchanged in the first three quarters, reflecting government spending ahead of an expected inflow of external budget support and difficulties in rolling over treasury bills despite an increase in interest rates. However, monetary policy was tightened in the first quarter of 2010, where reserve money was kept unchanged, despite the significant jump in the price level related to the introduction of the GST, and currency in circulation declined substantially. Although the pace of credit growth to the private sector remained high in 2009, the quality of the bank's loan portfolio improved as reflected by a decline in the ratio of nonperforming loans (NPLs) to gross loans (Table 9).

6. **All quantitative performance criteria for end-December 2009 were met, except for one (MEFP, Table 1).** The target on domestic primary fiscal balance was exceeded by a moderate margin, reflecting higher budgetary spending ahead of unprogrammed external budget support received very late in the year. This contributed to the higher than anticipated reserve money growth towards the end of 2009. However, during the first quarter of 2010, the domestic primary balance was lower than budgeted due to excess revenue collection, and monetary policy was tightened.

7. **The performance on structural reforms was mixed (MEFP, Table 2).** The continuous structural benchmark on the monthly meeting of the Monetary Policy Committee was met, so was the introduction of the GST on January 1, 2010. The benchmark on recruitment of budget officers was observed but with a delay. The structural benchmark for adoption by the BSL of new off-site surveillance guidelines for banks was not met. Since the

completion of this benchmark requires further technical assistance, which is currently being provided, the measure has been included as a benchmark for 2010. The restructuring of the NRA was delayed partly due to the challenges in implementing the GST; therefore, the benchmarks for the establishment of the Domestic Tax Department (DTD) and the integration of GST administration within the Large Taxpayer Office (LTO) were not met, but they have been included as benchmarks for 2010. While the benchmark for adoption of a new tariff policy framework was not met, electricity tariffs were raised sufficiently in 2009 to insure the financial viability of the publically-owned electricity enterprise. Looking ahead, the GoSL is receiving technical assistance from the World Bank to move to a cost-based formula for electricity pricing.

III. POLICY DISCUSSIONS

A. Medium-Term Macroeconomic Framework

8. **Consistent with the priorities laid out in PRSP II, the key economic objective of the GoSL is to raise growth by accelerating investments in infrastructure and developing an accessible financial sector.** The focus of the next three-year program will be on (i) creating fiscal space for improving basic infrastructure and social services while maintaining macroeconomic stability; (ii) strengthening tax performance and improving public financial management (PFM) systems; and (iii) deepening the financial sector.

9. **The medium-term outlook is favorable for Sierra Leone.** Economic growth will benefit from the recent completion of the Bumbuna power station, investment in basic infrastructure, initiatives to improve the business climate and raise agricultural productivity, and continued macroeconomic stability. This should support a recovery of real GDP growth to 4.8 percent in 2010 and to at least 6 percent in 2012. An expected recovery in export demand for minerals and cash crops should contribute to exchange rate stability. Combined with expanding domestic food production, this should in turn ease inflationary pressures. Monetary and exchange rate policies will aim to bring 12-month inflation down to 8 percent at end-2012 from a projected inflation of 12.5 percent at end-2010.

10. **Fiscal space will be created for accelerated capital and social spending by broadening tax bases, containing non-priority spending, and raising public sector efficiency, especially on project selection and implementation.** Domestic revenue is targeted to increase to at least 13.5 percent of GDP by 2012 due to efficiency gains from the introduction of GST, higher taxation on mining, and improvement in tax administration. The authorities will also minimize discretionary tax exemptions in order to meet revenue targets (MEFP, ¶14). With the emphasis on investment in infrastructure, the composition of expenditure will shift toward capital spending, which is projected to increase from 7 percent of GDP in 2009 to 9 percent of GDP by 2012. Non-wage current expenditures are expected to decline by about 1 percentage point of GDP because of the termination of the emergency power project. However, the wage bill is expected to increase by 0.4 percent in 2011–12

because of higher wages for health sector workers. The overall fiscal deficit is expected at 4-5 percent of GDP while domestic financing is targeted to remain below 2 percent of GDP per year. This will ensure a sustainable fiscal outlook and prevent crowding out of private sector activities.

11. **The GoSL launched a new free health care initiative (FHCI) for children and pregnant women on April 27, 2010.** The aim is to reduce the high infant and maternal mortality rates and achieve the corresponding Millennium Development Goals (MDGs). The FHCI, supported by several key development partners, reinstates the free health care system that has existed for decades but has been undermined with the introduction of user fees charged by local health care staff. The program involves provision of free medical care and essential drugs to children and pregnant women. To this end, the authorities have hired additional health care workers and more than doubled salaries in the sector. The annual additional cost of the initiative is estimated by the GoSL at about US$22 million, or 1.2 percent of GDP, mostly covering purchase of drugs and a higher health sector wage bill. While the drugs are fully funded by donors for now, the salary increase is only partially covered by donor funds, and this contribution will decline to zero over 4 years. The permanent annual impact on budget spending reflects only an increase in the wage bill of about 0.5 percent of GDP, since all drugs are procured outside the budget. While recognizing the need to improve health services in the country, staff stressed the need to carefully assess the fiscal implications, including for the wage bill of the whole public service, to ensure sustainability of the policy. In this respect, staff proposed a more gradual approach to the salary increase in the health sector and stressed the importance of implementing the pay reform, which involves a gradual raise in wages for all public servants partly financed by retrenchments. While recognizing the risks and the need to speed up pay reform for the public sector at large, the authorities argued that the success of the FHCI required a substantial and immediate increase in salaries and noted that the budget impact was limited since DfID offered to pay a significant share of the higher wage bill in the initial years.

12. **Due to limited scope for nonconcessional borrowing, continued budget support is essential.** Significant nonconcessional external borrowing, possibly with the exception of specific high-yielding projects in the energy sector, is not advisable given the moderate risk of debt distress assessment in the LIC-DSA for Sierra Leone prepared in December 2009 (particularly, the PV of external debt-to-exports ratio is close to the 100 percent threshold). The program assumes concessional external budget support amounting to about US$78 million in 2010, of which US$6 million from the World Bank's Crisis Response Window and about US$13.5 million from the European Union's Vulnerability-Flex grant are expected to be committed in the second half of the year. The requested disbursements from the Fund associated with the completion of the review and a new ECF arrangement, amounting to SDR 15.88 million, are projected to close the remaining external financing gap in 2010. For 2011–12, about US$65 million a year is programmed in external budget support

from the World Bank, the European Union, the African Development Bank, and DfID.[2] The program also assumes a buyback of most remaining outstanding external commercial debt in 2012.[3]

13. **Monetary policy will aim to achieve single-digit inflation while maintaining a flexible exchange rate regime.** The BSL and MOFED will improve their coordination to enhance the liquidity management framework. With the development of a benchmark interest rate, the BSL will move towards a monetary policy framework where interest rates increasingly will be used to signal policy intentions—however, money growth targeting will be maintained for now. The BSL will also enhance foreign exchange management by promoting an interbank foreign exchange market and move to a wholesale foreign exchange auction system.

14. **The structural reform program will complement the policies for improving infrastructure to promote higher sustainable private sector-led economic growth (MEFP, ¶17).** The program will focus on: (i) improving tax administration by making revenue collections more efficient and effective to achieve domestic revenue targets; (ii) strengthening PFM to raise efficiency in public spending, particularly for capital spending, by improving the Medium-Term Expenditure Framework process; and (iii) strengthening monetary operations and deepening the financial sector to enhance financial stability and increase intermediation (Box 2). In addition, policies will be implemented to ensure full pass-through of international market prices on fuel to the domestic market price to safeguard budget resources.

B. Policies for 2010

15. **The macroeconomic outlook for 2010 has been revised to reflect recent developments.** Growth is expected to pick-up to 4.8 percent in 2010, aided by global economic recovery, completion of the Bumbuna power station, investment in basic infrastructure, and initiatives to improve the business climate and raise agricultural productivity. The 12-month inflation is projected at 12.5 percent at end-2010 because of the jump in the price level earlier in the year. Import coverage of gross foreign exchange reserves is expected to decline from the current relatively high level as imports recover with economic recovery and expansion in investment.

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[2] This external budget support is included under official transfers and public sector disbursements in the balance of payments (Table 5). In the absence of this financial support, the projected overall balance of payment surplus would turnaround to a deficit of close to US$50 million a year in 2011–12.

[3] The nominal value of the commercial debt, which currently is being assessed with support from the World Bank, could amount to US$250 million. It is assumed that the buyback will be financed by donors consistent with other similar buyback operations.

Box 2: Sierra Leone—Financial Sector Reforms

Financial sector development is vital to promote private sector-led growth and poverty reduction in Sierra Leone. Although progress has been made in recent years, the authorities recognize that further reforms are required. To this end, they have developed a Financial Sector Development Plan (FSDP) that identifies four priority reform areas:

- Build a strong and competitive banking system
- Increase access to finance for businesses and households
- Improve mobilization and investment of long-term funds
- Create an enabling environment through legislative and regulatory reforms

Of several impediments to financial sector development pointed out in the FSDP, the program will focus on key measures to enhance financial stability and increase access to finance.

Enhancing financial stability and reducing vulnerabilities

Enhance BSL capacity to carry out its mandates:

- Amend the BSL and Banking Acts to give operational independence to BSL for effective regulation and supervision of the financial sector
- Expedite the exit of BSL from its involvement in the community banks

Develop supervisory techniques of the BSL:

- Institute supervision of market and country risks
- Make inspection reports more proactive in presenting corrective actions with required time tables
- Adopt new off-site surveillance guidelines

Improve the conduct of monetary policy:

- Establish central bank benchmark policy interest rate
- Complete conversion of non-interest bearing securities held by the BSL into marketable securities

NASSIT, the public pension fund, and its role in developing a long-term debt market:

- Separate NASSIT's social security administration from its investment functions
- Engage NASSIT in developing a long-term bond market consistent with the government's financing needs

Increasing access to finance

Strengthen information infrastructure:

- Establish a credit reporting system (will improve ranking in ease of doing business)
- Adopt and enforce International Financial Reporting Standards (IFRS)

Improve payments and settlement systems:

- Establish Real Time Gross Settlements system (RTGS)

Reinforce legal framework for financial and commercial transactions:

- Introduce a land-titling system to facilitate collateralization of land
- Designate a commercial bench within the judiciary to deal with commercial cases

Fiscal policy

16. **Fiscal policy will focus on improving revenue collections to accelerate capital spending while containing pressures on current expenditures.** Despite higher expected revenues, the overall fiscal deficit is projected to increase from 3.2 percent of GDP in 2009 to 3.9 percent of GDP in 2010 because of higher capital spending and lower budget grants. Domestic revenue is projected to increase by 0.7 percentage points to 12.4 percent of GDP because of higher imports, the full year effect of the increase in fuel excises in 2009, and moderate efficiency gains accruing from the introduction of a computer-based system (ASYCUDA) in custom clearing and the GST. An increase in diamond royalties to 6.5 percent, consistent with the new Mines and Minerals Act, will raise revenue by 0.2 percent of GDP in the second half of the year. The increase in diamond royalties will not apply to production where the fiscal regime is determined by developments agreements.[4]

17. **The 2010 budget envelope raises capital spending and allocations to implement the FHCI.** While nonwage current spending is projected to decline, mainly due to the completion of the emergency power project, capital spending is budgeted to increase to 8.1 percent of GDP in 2010 from 7.1 percent of GDP in 2009. The projects focus on rebuilding basic infrastructure like roads, water, and electricity. The FHCI is expected to increase the wage bill for health care workers by Le 28 billion, or 0.4 percent of GDP, of which about Le 18 billion is funded by DfID.[5] With the increase in inflation, salaries (including allowances) for other public servants are assumed to increase by 15 percent. As a result, the total wage bill is budgeted to increase by 0.3 percentage points of GDP in 2010.

18. **Over the next years, the GoSL intends to implement a pay reform to attract staff of high caliber.** The reform includes (i) realignment of current discrepancies in qualifications and grade placements; (ii) decompression of wage structure; (iii) retrenchment of redundant staff; and (iv) a gradual increase in compensation to competitive levels. The new pay structure will also introduce a performance appraisal system, whereby pay progression and staff promotions will be linked to performance. The implementation of the pay reform during 2010 is intended to be budget neutral (MEFP, ¶18).

19. **The GoSL recently signed a new mining lease agreement with a foreign company.** This agreement grants extensive tax exemptions, contrasting with the new legislation aimed at providing a level playing field for new mining projects in Sierra Leone. The mission raised concerns about the agreement since it undermines the program objective of raising an already low revenue-to-GDP ratio. This policy also risks reducing future budget grants to Sierra Leone, since key developing partners reacted strongly against the agreement. However, while indicating that concessions were necessary to attract investors in this

[4] There is currently only one diamond mine operating under a development agreement.

[5] The increase in health sector salaries is effective from March 1, 2010.

particular case, the GoSL is committed to applying the new fiscal regime for future mining investments (MEFP, ¶23).

20. **The authorities recognize the need to accelerate efforts to improve tax administration and broaden the tax base (MEFP ¶28–29).** In line with the recommendations from a recent FAD mission, measures to make the NRA more efficient include (i) establishing a DTD, as a vehicle for achieving integration of domestic tax collection; (ii) integrating administration of the GST into the LTO; and (iii) enforcing tax legislation to eliminate discretionary duty waivers and tax exemptions and reduce tax evasion.

Monetary and exchange rate policies

21. **The challenge for monetary policy will be to contain inflationary pressures stemming from the jump in price levels earlier this year and higher domestic fuel prices.** Monetary policy will aim at bringing inflation down to 12.5 percent at end-2010. Reserve money is envisaged to grow at 8 percent in 2010—or somewhat lower than nominal GDP reflecting excess liquidity at the beginning of the year—which could accommodate a 32 percent growth in private credit. The BSL will achieve this target through open market operations and net sales of foreign exchange.

22. **The authorities are committed to maintaining a flexible exchange rate to facilitate adjustment to external shocks.** The BSL will continue to sell foreign exchange to sterilize the liquidity created by foreign-financed budget spending and reduce short-term market volatility. Foreign exchange reserve coverage is projected to be maintained at a comfortable level at end-2010 (5.7 months of imports, including the 2009 SDR allocation).

Structural reforms

23. **The authorities are committed to stepping up structural reforms to complement the scaling up of public investment.** Reforms will focus on:

- **Improving tax administration.** The National Revenue Authority (NRA) will establish a DTD and integrate administration of the GST with the LTO to reduce inefficiencies arising from separate tax departments and to enhance tax compliance. In addition, the NRA will step up efforts to improve tax compliance (MEFP, ¶28–29).

- **Strengthening PFM.** The GoSL will strengthen the MTEF by enhancing the planning, monitoring and evaluation process for capital projects and enhance the Macro-Economic Fiscal Framework (MEFF) by developing an integrated macroeconomic forecasting model. Budget execution will continue to be strengthened by the rolling out of IFMIS to MDAs (MEFP, ¶30–32).

- **Strengthening the financial sector.** The BSL will enhance the conduct of its monetary policy by establishing a benchmark interest rate. The independence of the BSL will be strengthened, as will its supervisory role in reducing vulnerabilities (with the adoption of new off-site surveillance guidelines for banks). Access to credit will be enhanced by strengthening information structure through establishing a credit reference bureau and adopting International Financial Reporting Standards (IFRS) (MEFP, ¶33–37).

- **Establishing a transparent and automatic pricing framework for petroleum products** to ensure full pass-though and eliminate the fiscal risk from high international fuel prices (MEFP, ¶38).

IV. Program Risks

24. **Risks to the budget remain in the medium term.** On the expenditure side, the GoSL's decision to implement the FHCI, including a significant permanent increase in wages and salaries for health workers, represents risks for the budget in the medium-term due to uncertainties about the implications of this move on wage pressures elsewhere in the public service. Moreover, the permanent costs of importing drugs, currently covered fully by donors, will over time need to be brought into the budget. To reduce those fiscal risks, efforts are required to improve tax performance through reforming tax administration, increasing collections from the mining sector, and eliminating discretionary tax incentives. Also, timely implementation of the public service pay reform will be important to control the wage bill. On the revenue side, the emphasis on trade-based taxes will continue to make collections vulnerable to external shocks.

V. Program Modalities and Capacity To Repay The Fund

25. **Access is proposed at 30 percent of quota (SDR 31.11 million) phased in seven equal disbursements over three years (Table 7).** This level of access is sufficient to cover remaining external financing gaps during the program period and reflects a moderate decline compared to access under the current ECF (50 percent of quota including augmentations in two rounds). Moreover, the level of access is consistent with maintaining an external debt-to-GDP ratio of about 35 percent in the medium-term and keeping foreign exchange reserve coverage above 5 months of imports. The conclusion of the LIC-DSA, presented in December 2009, that Sierra Leone is at moderate risk of external debt distress and that its debt trajectory remains vulnerable to external shocks further supports the case for a moderate access level. The debt service obligations to the Fund, including the new program disbursements, will remain below 2.5 percent of exports of goods and services in the medium-term (Table 6).

26. **The program will be monitored semiannually.** Quantitative performance criteria are set for June and December 2010 and indicative targets for September 2010. Quantitative

performance criteria are proposed on (i) net domestic assets of the central bank; (ii) net domestic bank financing of the central government; (iii) gross foreign exchange reserves; (iv) new external arrears; (v) short-term external debt by the public sector; and (vi) contracting or guaranteeing of external nonconcessional debt by the public sector with maturities of more than one year (MEFP, Table 3). Indicative targets have been set on domestic central government revenue and poverty-related expenditures. Structural benchmarks have also been set for 2010 (MEFP, Table 4).

27. **The GoSL is making good faith efforts to resolve external arrears to commercial creditors.** The authorities continue to engage these creditors and have made goodwill payments to some of them to avoid litigation. The authorities are pursuing a debt buyback of most remaining commercial debt in 2012 (see paragraph 12) and there are no new developments in Sierra Leone's relations with its commercial creditors that could undermine program implementation. Ongoing efforts to resolve these arrears provide sufficient financing assurances for the Fund-supported program.

28. **A safeguards assessment has been initiated by the Fund, in line with the normal procedure for new programs.** The latest safeguards assessment update was completed in October 2009.

VI. Staff Appraisal

29. **After a period of economic slowdown, the outlook for Sierra Leone appears favorable.** Growth is expected to gradually pickup, aided by global economic recovery, completion of the Bumbuna power station, investment in basic infrastructure, and initiatives to improve the business climate. However, 12-month inflation is expected to remain at low double digits in the second half of 2010 due to the jump in inflation earlier in the year.

30. **A sustainable fiscal policy is critical for macroeconomic stability.** Improving revenue collection and expenditure efficiency will be important to finance the rebuilding efforts of basic infrastructure in Sierra Leone and the recently launched FHCI. While financial support from the development partners will continue to be an important source of financing to achieve the country's development objectives, more efforts will be needed by the GoSL to raise the domestic revenue contribution to the budget in the coming years. To this end, the introduction of the GST and the increase in mining royalties are important steps, but more needs to be done to increase tax compliance and further broaden tax bases. On the spending side, it is important to contain the wage bill by raising compensation to public servants to more competitive levels only in the context of a multiyear pay reform where corresponding savings are achieved through re-grading and retrenchments.

31. **The large increase in the price level during the two first months of 2010 has created a challenge for monetary policy.** Staff welcomes the BSL's resolve to bring inflation down to single digits by 2011 and its initiative to develop a benchmark policy

interest rate to improve the implementation of monetary policy. The BSL should continue to enhance bank supervision and closely monitor developments of nonperforming loans.

32. **Staff supports the authorities' commitment to accelerate structural reforms.** The focus is appropriately on improving tax administration, strengthening public financial management, and deepening the financial sector. The first two reform areas will help create fiscal space for capital and social spending while the latter complements these efforts by encouraging private sector investment and activity.

33. **Staff supports the authorities request for a three-year ECF arrangement,** based on the strength of the macroeconomic program and the GoSL's commitment to sound macroeconomic policies and to implement the agreed structural reform program. Staff also supports the request for a waiver for nonobservance of the performance criterion on domestic primary balance based on corrective actions and recommends completion of the sixth ECF review and the financing assurances review.

Table 1. Sierra Leone: Selected Economic Indicators

	2008	2009	2010 Proj	2011 Proj	2012 Proj
	(Annual percentage change, unless otherwise indicated)				
National account and prices					
GDP at constant prices	5.5	4.0	4.8	5.5	6.0
GDP deflator	11.2	5.7	13.3	9.7	7.6
GDP at market prices	5,826	6,407	7,605	8,798	10,030
(in billions of local currency)					
Consumer prices (end-of-period)	12.2	10.8	12.5	9.5	8.0
Consumer prices (average)	14.8	9.2	15.5	7.8	8.7
External sector					
Terms of trade (deterioration -)	-2.5	-8.3	5.7	4.3	2.8
Exports of goods (US$)	-5.2	3.9	25.9	12.5	11.5
Imports of goods (US$)	24.8	-2.6	14.7	11.9	10.7
Average exchange rate	2,985	3,414	…	…	…
(local currency per U.S. dollar)					
Nominal exchange rate change (depreciation -)	-2.2	-28.2	…	…	…
Real effective exchange rate (depreciation -)	-11.5	-6.7	…	…	…
Gross international reserves, months of imports	4.4	6.4	5.7	5.4	5.1
Money and credit					
Domestic credit to the private sector	56.8	45.4	32.2	18.3	21.2
Base money	10.2	20.6	8.0	15.8	14.0
M2	29.7	29.6	15.2	4.9	14.0
91-day treasury bill rate (in percent)	9.1	14.0	...	...	...
	(Percent of GDP, unless otherwise indicated)				
National accounts					
Gross capital formation	14.8	14.8	16.1	16.6	17.4
Government	6.2	7.1	8.1	8.5	9.0
Private	8.6	7.7	7.9	8.1	8.4
National savings	3.1	6.4	7.1	7.6	8.3
External sector					
Current account balance					
(including official grants)	-11.7	-8.4	-9.0	-9.0	-9.1
(excluding official grants)	-15.7	-13.4	-12.7	-11.6	-11.4
External public debt (including IMF)	31.2	29.8	33.8	33.6	33.1
Central government budget					
Overall balance	-4.7	-3.2	-3.9	-4.7	-3.5
(excluding grants)	-9.2	-11.0	-10.8	-10.6	-10.3
Revenue	11.5	11.7	12.4	12.9	13.7
Grants	4.5	7.8	7.0	5.9	6.9
Total expenditure and net lending	20.7	22.7	23.3	23.6	24.0

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.

Table 2. Sierra Leone: Fiscal Operations of the Central Government
(In billions of leone)

	2008	2009		2010	2011	2012
		Prog.	Act.	Proj.	Proj.	Proj.
Total revenue and grants	934	1,197	1,250	1,475	1,655	2,064
Revenue	670	725	749	946	1,139	1,375
Tax	589	641	660	839	1,015	1,233
Personal Income Tax	110	119	122	148	174	203
Corporate Income Tax	62	61	61	76	90	106
Goods and Services Tax	…	…	…	197	247	328
Imports sales tax 1/	123	113	129	…	…	…
Domestic sales tax 1/	14	17	11	…	…	…
Excises	70	113	107	137	146	157
Import duties	161	148	170	216	263	332
Mining royalties and license	19	21	20	41	66	75
Others	31	48	40	25	29	34
Of which: Five indirect taxes 1/	24	…	29	…	…	…
Non-tax	80	84	89	107	124	142
Grants	265	472	500	529	516	689
Budget support	144	243	315	297	244	353
Project grants	121	229	186	232	273	336
Expenditures and net lending	1,207	1,483	1,452	1,770	2,072	2,411
Current expenditures	848	988	1,000	1,151	1,324	1,508
Wages and salaries	334	400	402	506	594	677
Goods and services	285	332	350	339	401	463
Of which : Emergency Power Project	83	69	59	11	0	0
Subsides and transfer	109	154	145	170	194	221
Interest	120	101	103	136	135	147
Domestic	109	87	89	117	119	126
Foreign	12	15	14	19	17	21
Capital expenditure	359	495	452	619	748	903
Foreign financed	284	410	345	418	545	672
Domestic financed	75	85	107	202	202	231
Net lending	0	0	0	0	0	0
Overall balance						
Including grants	-273	-286	-202	-295	-417	-346
Excluding grants	-538	-758	-703	-824	-933	-1,036
Financing	273	286	202	295	417	346
External financing (net)	143	171	155	162	253	231
Borrowing	163	214	198	213	314	378
Project	163	181	160	185	273	336
Program	0	33	39	28	41	42
Amortization	-20	-43	-43	-51	-61	-147
Domestic financing (net)	158	115	47	133	164	115
Bank	218	151	109	180	162	124
Central bank	120	129	163	157	139	87
Commercial banks	98	23	-54	23	23	37
Nonbank	-60	-36	-62	-47	2	-9
Non bank financial institutions	-34	8	-25	18	14	23
Privatization proceeds	4	10	10	8	20	0
Change in arrears	-46	-54	-59	-74	-31	-32
Floats (checks payable & outstanding commitments	16	0	12	0	0	0
Errors and omissions/financing gap	-28	0	1	0	0	0
Memorandum item:						
Total poverty expenditures	330	337	362	417	456	525
Domestic primary balance, including grants	-133	-247	-254	-270	-253	-216

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.
1/ Replaced by GST on January 1, 2010.

Table 3. Sierra Leone: Fiscal Operations of the Central Government
(In percent of GDP)

	2008	2009		2010	2011	2012
		Prog.	Act.	Proj.	Proj.	Proj.
Total revenue and grants	16.0	18.6	19.5	19.4	18.8	20.6
Revenue	11.5	11.3	11.7	12.4	12.9	13.7
Tax	10.1	9.9	10.3	11.0	11.5	12.3
Personal Income Tax	1.9	1.9	1.9	1.9	2.0	2.0
Corporate Income Tax	1.1	0.9	1.0	1.0	1.0	1.1
Goods and Services Tax	…	…	…	2.6	2.8	3.3
Imports sales tax 1/	2.1	1.8	2.0	…	…	…
Domestic sales tax 1/ ..	0.2	0.3	0.2	…	…	…
Excises	1.2	1.7	1.7	1.8	1.7	1.6
Import duties	2.8	2.3	2.6	2.8	3.0	3.3
Mining royalties and license	0.3	0.3	0.3	0.5	0.7	0.7
Others	0.5	0.8	0.6	0.3	0.3	0.3
Of which: Five indirect taxes 1/	0.4	…	0.4	…	…	…
Non-tax	1.4	1.3	1.4	1.4	1.4	1.4
Grants	4.5	7.3	7.8	7.0	5.9	6.9
Budget support	2.5	3.8	4.9	3.9	2.8	3.5
Project grants	2.1	3.6	2.9	3.1	3.1	3.4
Expenditures and net lending	20.7	23.0	22.7	23.3	23.6	24.0
Current expenditures	14.6	15.3	15.6	15.1	15.1	15.0
Wages and salaries	5.7	6.2	6.3	6.6	6.7	6.7
Goods and services	4.9	5.2	5.5	4.5	4.6	4.6
Of which : Emergency Power Project	1.4	1.1	0.9	0.1	0.0	0.0
Subsides and transfers	1.9	2.4	2.3	2.2	2.2	2.2
Interest	2.1	1.6	1.6	1.8	1.5	1.5
Domestic	1.9	1.4	1.4	1.5	1.3	1.3
Foreign	0.2	0.2	0.2	0.3	0.2	0.2
Capital expenditure	6.2	7.7	7.1	8.1	8.5	9.0
Foreign financed	4.9	6.4	5.4	5.5	6.2	6.7
Domestic financed	1.3	1.3	1.7	2.7	2.3	2.3
Net lending	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance						
Including grants	-4.7	-4.4	-3.2	-3.9	-4.7	-3.5
Excluding grants	-9.2	-11.8	-11.0	-10.8	-10.6	-10.3
Financing	4.7	4.4	3.2	3.9	4.7	3.5
External financing (net)	2.5	2.7	2.4	2.1	2.9	2.3
Borrowing	2.8	3.3	3.1	2.8	3.6	3.8
Project	2.8	2.8	2.5	2.4	3.1	3.4
Program	0.0	0.5	0.6	0.4	0.5	0.4
Amortization	-0.3	-0.7	-0.7	-0.7	-0.7	-1.5
Domestic financing (net)	2.7	1.8	0.7	1.7	1.9	1.1
Bank	3.7	2.3	1.7	2.4	1.8	1.2
Central bank	2.1	2.0	2.5	2.1	1.6	0.9
Commercial banks	1.7	0.4	-0.8	0.3	0.3	0.4
Nonbank	-1.0	-0.6	-1.0	-0.6	0.0	-0.1
Non bank financial institutions	-0.6	0.1	-0.4	0.2	0.2	0.2
Privatization proceeds	0.1	0.2	0.2	0.1	0.2	0.0
Change in arrears	-0.8	-0.8	-0.9	-1.0	-0.4	-0.3
Floats (checks payable & outstanding commitments)	0.3	0.0	0.2	0.0	0.0	0.0
Discrepancy/financing gap	-0.5	0.0	0.0	0.0	0.0	0.0
Memorandum items:						
Total poverty expenditures	5.7	5.2	5.6	5.5	5.2	5.2
Domestic primary balance, including grants	-2.3	-3.8	-4.0	-3.6	-2.9	-2.2
Nominal GDP (in billions of local currency)	5,826	6,442	6,407	7,605	8,798	10,030

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.
1/ Replaced by GST on January 1, 2010.

Table 4. Sierra Leone: Monetary Accounts 1/

(In billions of leone; unless otherwise indicated)

	2008	2009					2010			
		Mar	June	Sept.	Dec		Mar.	June	Sept.	Dec.
					Prog.	Act.	Proj.	Proj.	Proj.	Proj.
I. Monetary Survey										
Net foreign assets	832	802	807	1,309	1,303	1,542	1,483	1,388	1,359	1,370
Net domestic assets	637	713	762	408	307	401	489	673	790	866
Domestic Credit	959	1,020	1,093	1,208	1,237	1,264	1,343	1,536	1,634	1,727
Claims on central government (net)	528	517	572	625	668	631	698	847	894	853
Of which: For budget financing	-3	-15	52	99	148	106	200	297	308	286
Claims on other public sector 2/	17	22	24	27	24	31	36	36	36	36
Claims on private sector	413	481	497	556	545	601	609	653	704	794
Other items (net) 3/	-351	-327	-349	-827	-930	-899	-897	-907	-888	-861
Money and quasi-money (M3)	1,469	1,515	1,569	1,716	1,611	1,942	1,973	2,061	2,149	2,237
Broad money (M2)	1,161	1,224	1,240	1,355	733	1,505	1,528	1,597	1,665	1,733
Foreign exchange deposits	307	292	329	361	878	437	444	464	484	504
II. Bank of Sierra Leone										
Net foreign assets	479	475	439	894	884	1,005	928	832	804	815
Net domestic assets	-12	-20	19	-426	-381	-442	-365	-244	-207	-207
Claims on other depository corporations	4	4	0	9	0	6	6	6	6	6
Claims on central government (net)	136	107	170	192	260	271	329	444	476	470
For budget financing	-320	-343	-257	-220	-192	-157	-72	-9	-13	0
For monetary operations	457	450	426	412	452	428	401	453	489	470
Claims on other public sector 2/	0	0	0	0	0	0	0	0	0	0
Claims on private sector	7	8	10	9	10	7	9	9	9	9
Other items (net) 3/	-164	-143	-161	-645	-651	-732	-726	-721	-715	-710
Reserve money	467	455	458	468	503	563	563	589	597	608
Currency outside banks	383	373	370	395	364	486	418	434	436	465
Commercial bank deposits	84	82	88	73	139	77	145	155	161	143
Memorandum items:										
(Annual percentage change)										
Reserve money	10.2	10.5	6.2	0.9	7.8	20.6	23.7	28.6	27.5	8.0
M3 (Money and quasi-money)	25.7	27.6	22.9	25.6	12.9	32.2	30.2	31.4	25.2	15.2
Credit to the private sector	56.8	62.4	56.2	49.5	31.8	45.4	26.6	31.4	26.6	32.2
Velocity (GDP/M3)	4.0	4.2	4.1	3.7	4.0	3.3	3.9	3.7	3.5	3.4
Money multiplier (M3/Reserve money)	3.1	3.3	3.4	3.7	3.2	3.4	3.5	3.5	3.6	3.7
Credit to the private sector (in percent of GDP)	7.1	7.5	7.8	8.7	8.5	9.4	8.0	8.6	9.3	10.4
Gross Reserves (in US$ millions)	209	203	208	…	334	336	331	328	325	336

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.

1/ End of period
2/ Include public enterprises and the local government.
3/ Including valuation.

Table 5. Sierra Leone: Balance of Payments
(In millions of U.S. dollars; unless otherwise indicated)

	2008	2009		2010	2011	2012
	Act.	Prog.	Prel.	Proj.	Proj.	Proj.
Current account	-227.9	-182.3	-158.3	-171.1	-193.1	-214.5
Trade balance	-202.3	-206.4	-179.8	-174.9	-193.6	-211.5
Exports, f.o.b.	267.7	246.7	278.1	350.2	394.1	439.2
Of which: diamonds	128.6	96.3	100.6	139.1	163.4	188.0
Imports, f.o.b	-470.0	-453.1	-457.9	-525.1	-587.6	-650.7
Of which: oil	-151.5	-100.1	-92.7	-126.9	-140.2	-152.3
Services (net)	-69.0	-43.1	-52.7	-53.5	-60.1	-66.5
Income (net)	-67.6	-40.7	-49.2	-43.6	-28.7	-28.5
Of which: interest on public debt	-3.9	-8.5	-4.2	-4.5	-4.1	-5.0
Transfers	111.1	107.9	123.3	100.9	89.3	92.1
Official transfers	77.7	73.2	93.8	70.8	55.5	54.8
Other transfers	33.4	34.7	29.6	30.0	33.7	37.4
Capital and financial account	203.8	269.1	266.4	130.2	199.5	222.9
Capital account	42.6	71.3	56.8	60.8	69.2	107.5
Of which: project support grants	40.5	69.4	56.8	58.2	66.4	79.4
Financial account	161.2	197.8	209.6	69.4	130.3	115.4
Foreign direct and portfolio investment	-3.4	33.4	33.4	51.1	67.4	81.9
Other investment	164.6	164.4	176.2	18.2	62.9	33.5
Public sector (net)	48.0	53.8	45.9	45.5	65.3	58.3
Disbursements	54.7	64.5	56.8	53.4	76.4	89.4
Amortization	-6.7	-10.7	-10.9	-8.0	-11.0	-31.1
Monetary authorities	0.0	128.1	128.1	0.0	0.0	0.0
Change in net foreign assests of commercial banks	0.3	-19.8	-21.5	0.4	-0.1	2.0
Other, including errors and omissions	116.3	2.3	23.7	-27.7	-2.3	-26.7
Overall balance	-24.0	86.7	108.1	-40.9	6.4	8.5
Financing						
Central bank net reserves (- increase)	24.0	-86.7	-108.1	40.9	-6.4	-8.5
Gross reserve change	6.0	-124.1	-126.9	0.0	-15.0	-15.0
Use of Fund loans	18.0	37.3	18.8	40.9	8.6	6.5
Purchases	18.0	37.3	18.8	43.0	13.6	13.6
Repurchases	0.0	0.0	0.0	-2.1	-5.0	-7.1
Exceptional financing	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:			(Percent of GDP)			
Current account	-11.7	-9.4	-8.4	-9.0	-9.0	-9.1
Trade Balance	-10.4	-9.9	-9.6	-9.2	-9.0	-8.9
Capital and Financial Account	4.5	12.9	12.9	8.3	9.4	10.5
Overall Balance	-1.2	4.5	5.8	-2.1	0.3	0.4
Official aid (grants and loans)	8.9	10.6	10.9	9.6	9.3	10.5
Budget support in US$ (grants and loans)	77.7	83.2	93.4	77.8	65.5	64.8
Gross International Reserves						
(US$ millions)	209	334	336	336	351	366
Months of imports	4.4	6.5	6.4	5.7	5.4	5.1
excluding SDR allocation of 2009	4.4	4.0	3.9	3.5	3.4	3.3
National currency per US dollar	2,984.6	3,322.0	3,410.2	…	…	…

Sources: Sierra Leonean authorities; and Fund staff estimates and projections.

Table 6. Sierra Leone: Indicators of Capacity to Repay the Fund

		Projection								
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fund obligations based on existing credit										
(in millions of SDRs)										
Principal	0.0	1.4	3.3	4.6	4.6	8.1	7.9	6.1	4.7	4.7
Charges and interest[1]	0.1	0.0	0.0	0.2	0.2	0.2	0.1	0.1	0.1	0.0
Fund obligations based on existing and prospective credit										
(in millions of SDRs)										
Principal	0.0	1.4	3.3	4.6	4.6	8.1	10.3	12.1	12.6	14.3
Charges and interest[1]	0.1	0.0	0.0	0.4	0.4	0.4	0.4	0.3	0.3	0.2
Total obligations based on existing and prospective credit										
In millions of SDRs	0.1	1.4	3.3	5.0	5.1	8.5	10.7	12.4	12.8	14.5
In millions of US$	0.2	2.2	5.0	7.7	7.7	13.1	16.4	19.1	19.6	22.3
In percent of exports of goods and services	0.1	0.5	1.1	1.5	1.4	2.1	2.4	2.4	2.3	2.5
In percent of debt service[2]	1.2	14.8	25.0	17.8	33.7	42.5	49.1	55.5	56.0	58.5
In percent of GDP	0.0	0.1	0.2	0.3	0.3	0.5	0.5	0.6	0.6	0.6
In percent of Gross International Reserves	0.1	0.6	1.4	2.1	2.0	3.4	4.2	4.9	4.9	5.5
In percent of quota	0.1	1.4	3.2	4.9	4.9	8.2	10.3	12.0	12.3	14.0
Outstanding Fund credit										
In millions of SDRs	46.7	73.4	79.0	83.2	83.1	75.0	64.7	52.5	40.0	25.7
In millions of US$	72.0	112.5	120.8	127.4	127.3	115.0	99.2	80.6	61.3	39.4
In percent of exports of goods and services	21.7	27.7	26.5	25.1	22.9	18.5	14.5	10.2	7.3	4.4
In percent of debt service	477.5	772.5	601.4	295.1	553.6	373.4	297.6	234.5	175.0	103.5
In percent of GDP	3.8	5.9	5.6	5.4	5.0	4.2	3.3	2.5	1.8	1.1
In percent of Gross International Reserves	21.4	33.4	34.4	34.8	33.6	30.0	25.5	20.5	15.4	9.8
In percent of quota	45.0	70.7	76.2	80.3	80.1	72.3	62.3	50.7	38.6	24.7
Net use of Fund credit (in millions of SDRs)	18.8	45.2	18.6	20.7	13.9	12.5	17.6	22.0	22.5	25.0
Disbursements	18.8	43.0	13.6	13.6	6.8	0.0	0.0	0.0	0.0	0.0
Repayments	0.0	2.1	5.0	7.1	7.1	12.5	17.6	22.0	22.5	25.0
Memorandum items:										
Exports of goods and services (in millions of US$)	332	405	456	508	557	620	683	789	841	891
Debt service (in millions of US$)	15	15	20	43	23	31	33	34	35	38
Nominal GDP (in millions of US$)	1,879	1,906	2,141	2,369	2,564	2,765	2,976	3,179	3,390	3,592
Gross International Reserves (in millions of US$)	336	336	351	366	378	383	388	393	398	403
Quota (millions of SDRs)	104	104	104	104	104	104	104	104	104	104

Sources: IMF staff estimates and projections.

[1] There are no interest payments to the Fund in 2010-11.
[2] Total debt service includes IMF repayments.

Table 7. Sierra Leone: Proposed Schedule of Disbursements Under the new ECF Arrangement

Availability	Disbursements		Conditions for Disbursement
	In millions of SDRs	In percent of quota	
July 2010	4.44	4.28	Effectiveness of the three-year ECF arrangement
December 2010	4.44	4.28	Board completion of the first review based on observance of performance criteria for June 30, 2010
June 2011	4.44	4.28	Board complettion of the second review based on observance of performance criteria for December 31, 2010
December 2011	4.44	4.28	Board completion of the third review based on observance of performance criteria for June 30, 2011
June 2012	4.44	4.28	Board completion of the fourth review based on observance of performance criteria for December 31, 2011
December 2012	4.44	4.28	Board completion of the fifth review based on observance of performance criteria for June 30, 2012
June 2013	4.47	4.32	Board complettion of the sixth review based on observance of performance criteria for December 31, 2012
Total disbursements	**31.11**	**30.00**	

Table 8. Sierra Leone: Millennium Development Goals

	1990	1995	2000	2005	2008
Goal 1: Eradicate extreme poverty and hunger					
Employment to population ratio, 15+, total (%)	*64*	65	65	64	*64*
Employment to population ratio, ages 15-24, total (%)	*39*	41	44	41	*42*
GDP per person employed (annual % growth)	*-20*	-9	1	4	4
Income share held by lowest 20%	1.1	..	..	*6.1*	..
Malnutrition prevalence, weight for age (% of children under 5)	..	..	24.7	28.3	..
Poverty gap at $1.25 a day (PPP) (%)	45	..	..	*20*	..
Poverty headcount ratio at $1.25 a day (PPP) (% of population)	63	..	..	*53*	..
Prevalence of undernourishment (% of population)	*45*	*43*	..	47	..
Vulnerable employment, total (% of total employment)	..	..	..	..	..
Goal 2: Achieve universal primary education					
Literacy rate, youth female (% of females ages 15-24)	..	..	..	*37*	*44*
Literacy rate, youth male (% of males ages 15-24)	..	..	..	*60*	*64*
Persistence to last grade of primary, total (% of cohort)	..	..	..	..	..
Primary completion rate, total (% of relevant age group)	..	..	..	*81*	*81*
Total enrollment, primary (% net)	..	..	..	..	..
Goal 3: Promote gender equality and empower women					
Proportion of seats held by women in national parliaments (%)	..	*6*	9	15	13
Ratio of female to male enrollments in tertiary education	..	..	*40*	..	..
Ratio of female to male primary enrollment	69	..	*71*	*90*	*90*
Ratio of female to male secondary enrollment	*57*	..	*71*	*69*	*69*
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	..	..	..	*23.2*	..
Goal 4: Reduce child mortality					
Immunization, measles (% of children ages 12-23 months)	..	..	37	67	*67*
Mortality rate, infant (per 1,000 live births)	169	166	161	157	*155*
Mortality rate, under-5 (per 1,000)	290	283	274	265	*262*
Goal 5: Improve maternal health					
Adolescent fertility rate (births per 1,000 women ages 15-19)	..	*146*	139	130	*126*
Births attended by skilled health staff (% of total)	..	..	42	43	..
Contraceptive prevalence (% of women ages 15-49)	..	..	4	5	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	2,100	..
Pregnant women receiving prenatal care (%)	..	..	68	81	..
Unmet need for contraception (% of married women ages 15-49)	..	..	..	..	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases					
Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	..	..	61	52	..
Condom use, population ages 15-24, female (% of females ages 15-24)	..	..	..	..	..
Condom use, population ages 15-24, male (% of males ages 15-24)	..	..	..	..	..
Incidence of tuberculosis (per 100,000 people)	207	279	377	509	*574*
Prevalence of HIV, female (% ages 15-24)	..	..	..	*1.3*	*1.3*
Prevalence of HIV, male (% ages 15-24)	..	..	..	*0*	*0*
Prevalence of HIV, total (% of population ages 15-49)	0.2	1.0	1.2	1.6	*1.7*
Tuberculosis cases detected under DOTS (%)	..	29	33	36	*37*
Goal 7: Ensure environmental sustainability					
CO2 emissions (kg per PPP $ of GDP)	0.2	0.3	0.4	0.3	..
CO2 emissions (metric tons per capita)	0.1	0.1	0.1	0.2	..
Forest area (% of land area)	43	41	40	38	..
Improved sanitation facilities (% of population with access)	..	12	12	*11*	*11*
Improved water source (% of population with access)	..	57	57	*53*	*53*
Marine protected areas, (% of surface area)	..	..	..	..	..
Nationally protected areas (% of total land area)	..	..	..	*4.1*	*4.1*
Goal 8: Develop a global partnership for development					
Aid per capita (current US$)	15	51	43	69	*99*
Debt service (PPG and IMF only, % of exports, excluding workers' remittances)	10	62	46	9	*4*
Internet users (per 100 people)	0.0	0.0	0.1	0.2	0.3
Mobile cellular subscriptions (per 100 people)	0	0	0	*14*	18
Telephone lines (per 100 people)	0	0	0	..	..
Other					
Fertility rate, total (births per woman)	5.5	5.5	5.4	5.3	*5.2*
GNI per capita, Atlas method (current US$)	190	200	150	230	320
GNI, Atlas method (current US$) (billions)	0.8	0.8	0.6	1.2	1.8
Gross capital formation (% of GDP)	10.0	5.6	6.9	17.4	19.7
Life expectancy at birth, total (years)	40	39	43	46	48
Literacy rate, adult total (% of people ages 15 and above)	..	..	..	*35*	*38*
Population, total (millions)	4.1	4.0	4.2	5.1	5.6

Source: World Development Indicators database, 2009

Table 9. Sierra Leone: Financial Soundness Indicators of the Banking System, 2005–09

	2005	2006	2007	2008	2009 December
	(Percent, end of period, unless otherwise indicated)				
Capital adequacy					
Regulatory capital ratio [1]	35.7	33.3	35.0	43.5	34.0
Regulatory tier 1 capital ratio [2]	10.3	17.0	16.7	18.7	18.8
Asset quality					
Nonperforming loans to total gross loans	…	…	25.6	17.9	10.6
Nonperforming loans (net of provisions) to regulatory capital	…	…	28.5	4.6	9.5
Earnings and profitability					
Return on assets	8.1	5.8	3.1	2.2	1.6
Return on equity	28.0	17.0	10.3	7.2	4.0
Interest spread [3]	13.4	13.4	15.2	12.1	7.1
Liquidity					
Ratio of net loans to total deposits	27.5	26.5	27.7	33.9	41.5
Liquidity ratio [4]	53.0	58.9	53.3	62.0	53.4
Statutory minimum liquidity ratio [4] [5]	34.0	28.5	25.7	25.0	29.0
Share of foreign exchange deposits in total deposits	30.7	32.4	36.5	32.2	34.5
	(Number of banks not complying)				
Prudential ratios at year-end					
Capital adequacy	0	0	0	0	1
Minimum liquidity ratio	0	0	0	0	1
Minimum capital	0	1	1	1	2
Limit of single large exposure [6]	0	2	1	2	4
Memorandum Item:					
Number of banks	7	8	10	13	14

Source: Bank of Sierra Leone.

[1] Capital requirement over risk-weighted assets (solvency ratio).

[2] Core capital (Tier I) over total assets.

[3] Average lending rate minus average saving deposit rate.

[4] Calculated taking into account both domestic currency and foreign currency deposits. Liquid assets include domestic currency cash in vault, claims on the BSL, claims on discount houses, and government securities.

[5] Effective November 2007, minimum liquidity includes 40 percent of demand deposits and 20 percent of quasi money to be held in either cash or treasury bills.

[6] A single large exposure of an institution is any exposure that is 2 percent or more of its capital base.

APPENDIX I. LETTER OF INTENT

May 18, 2010

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. Strauss-Kahn:

The attached Memorandum of Economic and Financial Policies (MEFP) describes recent economic developments and progress in the implementation of the ECF-supported program during the second half of 2009 and presents our policies for the medium-term under a new ECF-supported program. To support the implementation of the program, the Government of Sierra Leone (GoSL) requests a new three-year arrangement under the ECF in a total amount equivalent to SDR 31.11 million (30 percent of quota). We also request that the first disbursement, in an amount equivalent to SDR 4.44 million, be made available after the approval of the ECF arrangement by the Executive Board of the IMF.

All quantitative performance criteria for end-December 2009 were met, except for one. The target on domestic primary fiscal balance was moderately exceeded, reflecting in part the use of higher external budget support. Higher government spending towards the end of the year and difficulties in rolling over treasury securities led to an expansion of liquidity. However, monetary policy was tightened in the first quarter of 2010, where reserve money was kept unchanged despite a 7 percent jump in the price level related to the introduction of the goods and services tax.

On the structural reform program, the continuous structural benchmark on the monthly meeting of the Monetary Policy Committee was met, so was the introduction of the GST on January 1, 2010. The structural benchmark on recruitment of budget officers was not met on time, but it has now been completed. Two unmet benchmarks on tax administration will be included as structural benchmarks in the new program.

In light of the above, the GoSL requests a waiver related to non-observance of one performance criterion and that the seventh disbursement be made available upon completion of the sixth review under the ECF arrangement.

The GoSL believes that the policies set forth in the attached MEFP and Technical Memorandum of Understanding (TMU) are adequate to achieve the objectives of the new program, but stands ready to take any further measures that become necessary for this purpose, in consultation with the Fund. The GoSL will consult with the Fund in advance of revisions to the policies contained in the MEFP and continue to provide the staff of the IMF the information required to accurately assess Sierra Leone's progress in executing the policies in the MEFP. The first and second review under the new program shall take place in December 2010 and June 2011, respectively. Furthermore, the GoSL will continue to consult with the IMF on its economic and financial policies, in accordance with the IMF's policies on such consultations.

The GoSL agrees, in line with its commitment to transparency and accountability, to the publication of this letter, its attachments, and the related staff report in accordance with the procedures for publication.

Very truly yours,

/s/
Samura M. W. Kamara
Minister of Finance and Economic Development

Attachments

Appendix I—Attachment I
Sierra Leone: Memorandum of Economic and Financial Policies

I. Introduction

1. This memorandum reviews recent economic developments and outlines the macroeconomic policies and structural reforms that the Government of Sierra Leone (GoSL) will pursue under a new three-year Extended Credit Facility (ECF).

II. Recent Economic Developments

2. **Macroeconomic performance in 2009 weakened due to the global recession.** Economic growth continued to decline in the first half of 2009 due to falling global demand and declining foreign inflows from remittances. Despite a pickup in exports of diamonds and cash crops in the second half of 2009 and buoyant domestic food production, real GDP growth is estimated to have slowed down to 4 percent in 2009 compared with 5.5 percent in 2008. Lower fuel and domestic food prices eased inflationary pressures in the first half of 2009. However, the depreciation of the leone in the second half contributed to a rebound in inflation to 10.8 percent in December. During the first two months of 2010, inflation jumped to about 17 percent, reflecting the introduction of GST on January 1 and higher domestic fuel prices.

3. **Fiscal policy performance during 2009 was broadly satisfactory.** The domestic revenue target was met by a solid margin as import duties rose significantly. While current expenditures were slightly higher than envisaged, capital expenditures were lower due to a shortfall in externally financed projects. Higher budget grants and domestic revenue collections along with a moderate increase in expenditures reduced the overall deficit to 3.2 percent of GDP in 2009 from 4.7 percent in 2008 and 4.4 percent in the program. However, the domestic primary fiscal deficit, at 4.0 percent of GDP, was slightly higher than programmed.

4. **Monetary policy became more expansionary towards the end of 2009.** Reserve money grew faster than anticipated in 2009 (about 20 percent) with most of the expansion attributed to the last couple of months of the year. The increase in liquidity was due to significant government spending ahead of expected inflow of external budget support and difficulties in rolling over treasury bills towards the end of the year. The average interest rate on treasury bills increased from 9 percent end-2008 to 14 percent end-2009. However, the pace of credit growth to the private sector remained high in 2009 but the quality of the bank's loan portfolio improved reflected by a decline in the ratio of nonperforming loans (NPLs) to gross loans from 17.9 percent at end-2008 to 10.6 percent at end-2009.

5. **Exchange rate depreciated by about 28 percent against the US dollar in 2009.** This depreciation was mainly caused by a decline in export proceeds and transfers due to the

global economic crisis. However, the exchange rate has stabilized around the levels observed in November-December 2009.

6. **All quantitative performance criteria for end-December 2009 were met, except for one (Table 1).** The target on domestic primary fiscal balance was moderately exceeded, reflecting in part the use of higher external budget support. Higher government spending towards the end of the year and difficulties in rolling over treasury securities led to an expansion of liquidity.

7. **Two of the seven structural benchmarks for the second half of 2009 were met (Table 2).** The continuous structural benchmark on the monthly meeting of the Monetary Policy Committee was observed, so was the introduction of the Goods and Services Tax (GST). The benchmark on recruitment of budget officers was observed but with delay due to late start of the Integrated Public Financial Management Reform Program. The benchmark for adoption by the BSL of new off-site surveillance guidelines for banks was not observed. Completion of this benchmark requires additional technical assistance, which is currently being provided. The restructuring of the NRA was delayed partly due to the challenges in implementing the GST; therefore, the benchmarks for the establishment of the Domestic Tax Department (DTD) and the integration of GST administration within the Large Taxpayer Office (LTO) were not met. Finally, the benchmark for adoption of a new tariff policy framework was not observed due to a change in strategy—the GoSL intends to adopt a cost-based formula for pricing electricity, which will be developed with technical assistance from the World Bank.

III. TAKING STOCK

8. **Since the end of the civil conflict, economic policies in Sierra Leone have focused on rebuilding the economy and laying the basis for long term growth**. The emphasis of the previous ECF-supported program was on strengthening the long-term basis for poverty reduction and development by maintaining macroeconomic stability and improving public services. Macroeconomic performance has been good in recent years: growth remained robust despite the global financial crisis, inflation came down to single digits, domestic revenue performance improved and international reserves increased.

9. **Progress has been made in implementing our structural reform program:**

- To improve the efficiency of revenue collections and broaden the tax base, a tax identification number (TIN) system was introduced, a new and modernized customs law consistent with the WTO agreement was adopted by Cabinet, and a small and medium taxpayer regime was put in place. Moreover, the GST was introduced and replaced seven other taxes to simplify and broaden the tax base.

- For better expenditure control, the rollout of the Integrated Financial Management Information System (IFMIS) now covers more than half of all transactions by the ministries, departments and agencies (MDAs) and the public expenditure tracking surveys (PETS) was integrated into the broader public financial management (PFM).

- Financial sector vulnerabilities were addressed by assessing the bank capitalization and credit quality of all commercial banks and raising the minimum paid-up capital requirement for licensed financial institutions. Credit to private sector has been growing rapidly reflecting financial sector deepening.

10. **While progress has been made over the last decade, significant challenges remain**. Sierra Leone remains a post-conflict country suffering from lack of infrastructure (roads, electricity, and water) and weak institutions. Despite economic growth in recent years, per capita income remains low, poverty is pervasive (at 60 percent of population), and Sierra Leone ranks at the bottom of UN's Human Development Index. Gross domestic investment is currently at about 15 percent of GDP, significantly lower than the sub-Saharan African average of 22 percent. Also, private sector development is constrained by limited access to financial services. While growing, credit to the private sector, at 9 percent of GDP, remains low compared to the sub-Saharan African average of 17 percent.

IV. MEDIUM-TERM CHALLENGES AND POLICIES

11. **The GoSL's key economic objective is to raise growth by increasing investments in infrastructure and developing an accessible financial sector.** In order to reduce poverty significantly and improve the lives of the majority of Sierra Leoneans, an annual growth rate of 6–10 percent is required for a sustained period of time. Consistent with the second Poverty Reduction Strategy Paper (PRSP II), the three-year program will focus on (i) creating fiscal space for improving basic infrastructure and social services while maintaining macroeconomic stability; (ii) strengthening tax performance and improving public financial management (PFM) systems; and (iii) developing the private sector.

12. **The medium term outlook for the Sierra Leonean economy is favorable.** Real GDP growth is expected to recover to 4.8 percent in 2010 and increase to at least 6 percent by 2012, benefiting from the recent completion of the Bumbuna power station, investment in basic infrastructure, and initiatives to improve the business climate and raise agricultural productivity. The global economic recovery will increase export demand for minerals and cash crops, which should contribute to exchange rate stability. Combined with expanding domestic food production, this should ease inflationary pressures. Monetary and exchange rate policies will also aim at returning to single-digit inflation, with inflation projected to decline from 12.5 percent in 2010 to 8 percent in 2012. However, import coverage of gross foreign exchange reserves will decline from the current relatively high level as imports recover with economic recovery and expansion in investment.

13. **Fiscal space will be achieved through several channels.** While pressing for scaling up of donor inflows, fiscal space will be created by broadening tax bases, containing non-

priority spending, and raising public sector efficiency, especially on project selection and implementation.

14. **Domestic revenue is expected to increase over the medium term and expenditure will shift towards capital spending.** Reflecting efficiency gains from the introduction of GST and improvement in tax administration, the aim is to raise domestic revenue above 13.5 percent of GDP by 2012. To achieve this target, the GoSL will fully apply the fiscal regime stipulated in existing tax and customs acts and will resist issuing discretionary tax exemptions. In particular, new investment agreements in the mining sector will adhere to the fiscal regime stipulated in the Mines and Minerals Act 2009 and the Consolidated Income Tax Act 2000. With the emphasis on investment in infrastructure, the composition of expenditure will shift toward capital spending, which is projected to increase from 7 percent of GDP in 2009 to 9 percent of GDP by 2012. Non-wage current expenditures are expected to decline by about 1 percentage point of GDP because of the termination of the emergency power project. Although the wage bill is envisaged to be contained at around 6.7 percent of GDP, adjustments may have to be made in connection with the implementation of the public service pay reform in 2011–12. The GoSL is committed to ensuring that the overall central government deficit remains below 5 percent of GDP in 2010–12.

15. **The GoSL has launched a new free health care initiative for children under five years of age, pregnant women and lactating mothers.** The objective is to reduce the high infant and maternal mortality rates and achieve the Millennium Development Goals 4 and 5. The initiative involves the provision of cost-free medical care and drugs to these vulnerable groups. It provides significant improvements in the compensation to professional health workers to ensure the elimination of user fees in all government hospitals and health centers. While costs initially are largely borne by donors, the permanent additional cost of the initiative is currently estimated at 1.2 percent of GDP. The increase in staffing and wages in the health sector will raise the budgetary wage bill by about Le 28 billion in 2010 (0.4 percent of GDP) and by about Le 35 billion on a permanent basis taking into account the full year effect.

16. **Monetary policy will strive to achieve single-digit inflation**. Improvement in the coordination between the Ministry of Finance and Economic Development (MOFED) and the BSL will enhance the liquidity management framework. Moreover, the monetary policy framework will be strengthened by the introduction of a policy interest rate to guide the market. The BSL will also enhance foreign exchange management and promote an interbank foreign exchange market by moving to a wholesale foreign exchange auction system.

17. **The structural reform program will complement the improvements in infrastructure to promote higher sustainable private sector-led economic growth.** The program will focus on: (i) improving tax administration by making revenue collections more efficient and effective to achieve domestic revenue target; (ii) improving public financial management to raise efficiency in public spending, particularly for capital spending, by

improving Medium-Term Expenditure Framework (MTEF) process and rolling out IFMIS to more MDAs; and (iii) strengthening monetary operations and deepening the financial sector to enhance financial stability. In addition, policies will be implemented to ensure full pass-through of international market prices on fuel to the domestic market price to safeguard budget resources.

18. **To improve working conditions for the public service and to attract staff of high caliber, a multiyear pay reform will be implemented.** The reform will (i) realign current discrepancies in qualifications and grade placements; (ii) decompress the wage structure; (iii) retrench redundant staff; and (iv) gradually raise compensation to competitive levels financed partly from the restructuring and, if necessary, a moderate increase in the total public sector wage bill. The GoSL is seeking assistance from development partners to finance temporary costs for retrenchment and implementation. In contrast to the recent changes in pay conditions to the health sector, the pay reform will target the whole public service. The implementation of the pay reform will be budget neutral in 2010.

19. **Debt sustainability will remain a priority.** We are committed to a conservative strategy of external borrowing on concessional terms. A comprehensive national debt law and procedures manual will be adopted in 2010. In collaboration with the Public Debt Unit of MOFED, government agencies are working on improving the quality of debt data and reporting in order to better monitor commitments, disbursements, and debt service obligations. The Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) will be electronically linked with IFMIS. In order to further improve on debt management, the Government is requesting assistance from the World Bank and the Fund with respect to developing a comprehensive Medium-Term Debt Management Strategy (MTDS).

V. Policies for 2010

A. Fiscal Policy

20. **The overall fiscal deficit is projected to increase in 2010 despite higher domestic revenue.** The overall fiscal deficit is projected to increase from 3.2 percent of GDP in 2009 to 3.9 percent of GDP in 2010. Domestic revenue is projected to increase 0.7 percentage points to 12.4 percent of GDP because of higher imports, the full year effect of the increase in fuel excises by mid-2009, higher royalties on diamonds, and moderate efficiency gains across several tax categories. However, budget support grants are expected to decline by 1 percentage points to 3.9 percent of GDP, partly reflecting an unusually high level of support in 2009 to alleviate the effects of the global economic crisis.

21. **Expenditures will shift from current to capital spending.** Current expenditures are projected to decline from 15.6 percent of GDP in 2009 to 15.1 percent of GDP in 2010, while capital expenditures will increase from 7.1 percent in 2009 to 8.2 percent, mostly due to higher spending on basic infrastructure (roads and water supply projects). Wages and salaries

are envisaged to increase from 6.3 percent of GDP in 2009 to 6.6 percent of GDP because of a more than doubling of salaries to health care workers from March 1 and hiring of about 1,300 new health care professionals. The wage bill for other public servants is expected to increase by about 15 percent, reflecting a 30 percent increase in basic salaries (basic salaries make up about half of the total compensation including various allowances).

22. **The GoSL has adopted a new tax incentive policy to attract new investments in several sectors.** Although relatively few new incentives have been introduced, the new policy consolidates several existing incentives from a number of sector-specific acts into the tax and customs acts and it promotes elimination of discretionary tax incentives and exemptions. To evaluate the costs and benefits of this policy, the GoSL will prepare a policy review by March every year covering the previous calendar year. This review will contain a list of all projects that have benefited from the catalogue of incentives, specify the purpose of the projects, and report foregone revenue. The review will be made publicly available and submitted to the Parliament.

23. **A new Mines and Minerals Act came into effect on January 1, 2010.** Together with the Consolidated Income Tax Act 2000, this new act defines the fiscal terms for mining operations in Sierra Leone. The key fiscal terms comprise royalties of 3–15 percent (depending on mineral type) and a 30 percent corporate tax. This new fiscal regime will apply to all future mining contracts. At present, diamonds produced by Koidu Holdings attract a royalty of 5 percent according to the development agreement. Consistent with the Mines and Minerals Act 2010, the revised royalty rate of 6.5 percent will be applied to all other diamond mining operators in 2010. All royalties will be collected by NRA and deposited into the Consolidated Revenue Fund.

24. **The GoSL has committed to the principles of Extractive Industries Transparency Initiative (EITI).** It launched in March 2010, the first EITI report on payments made by mining companies and revenues received by MDAs from the extractive sector for the fiscal years 2006–07. To enhance the transparency and accountability process, the EITI report and its findings are currently being disseminated to MDAs, mining companies, chiefdom leaders, civil society, and the general public. The next objective is to undertake a validation exercise to enable Sierra Leone become an EITI compliant country. In the medium-term, EITI reports will incorporate the oil, fisheries and timber sub-sectors.

B. Monetary and Exchange Rate Policy

25. **Monetary policy will aim to achieve an inflation rate of 12.5 percent by end-2010.** Monetary policy will be challenged by the first round effects on inflation arising from the introduction of GST and expected higher domestic fuel prices. Reserve money is targeted to grow by 8 percent in 2010. This will still accommodate a robust expansion in credit to the private sector of about 30 percent, with unchanged international reserves. The BSL stands

ready to use its monetary instruments more actively and raise interest rates, if necessary, to achieve the program targets.

26. **Exchange rate flexibility will be maintained.** The BSL will sell foreign exchange only to absorb foreign-financed budget spending and reduce short-term market volatility. The BSL will gradually reduce the amount offered on the foreign exchange auction as the effects from the global economic downturn dissipate.

C. Structural Reforms

27. **The overall pace of our reforms needs to be accelerated to complement the scaling up of public investments**. Policies for 2010 will focus on improving tax administration, strengthening PFM and developing the financial sector. Policies for the two latter areas will be based on the Integrated Public Financial Management Reform Program (IPFMRP) and the Financial Sector Development Plan (FSDP), respectively.

Improving tax administration

28. **The GoSL will step up efforts to improve tax administration and broaden the tax base**. The National Revenue Authority (NRA) will establish a DTD to bring all domestic tax administration under one organization (*Structural Benchmark for September 2010*). The current tax administration suffers from inefficiencies arising from separate tax departments for GST and income and it is not conducive to enhance tax compliance. The NRA will appoint a commissioner, DTD and a deputy commissioner for design and monitoring and bring the Income Tax Department (ITD) and GST departments under the umbrella of the DTD. In addition, the operations (taxpayer services, filing and returns processing, and coordinated audit operations) of GST and the LTO will be integrated (*Structural Benchmark for December 2010*).

29. **The NRA will step up efforts to improve tax collection and compliance.** In the past, penalties on overdue tax were promulgated but rarely imposed, hence compliance has been low. The NRA will work towards increasing compliance by providing information to taxpayers on what they need to pay and then following up through phone calls and letters. The MOFED will also assist the NRA in this endeavor to enforce tax compliance by providing specific product lists when approving duty free exemptions.

Strengthening public financial management

30. **The GoSL will strengthen the Medium-Term Expenditure Framework (MTEF) by enhancing the planning, monitoring and evaluation process for capital projects.** The legal framework governing the entry of projects into the budget and monitoring is insufficient. Given the accelerated capital spending, planning, monitoring and evaluation of projects becomes even more important. With the assistance from the World Bank, GoSL intends to amend the legal framework to require that strategic priorities be set out in

monitorable progress indicators for each MDA and project selection criteria be established such that only viable projects enter into the budget. The necessary legal amendments will be submitted to the Parliament (*Structural Benchmark for September 2010*).

31. **The Macro-Economic Fiscal Framework (MEFF) will be strengthened by developing an integrated macroeconomic forecasting model.** Budget planning is weak in the absence of credible forecasts. In a coordinated effort involving MOFED, the BSL, the SSL and the NRA, work is currently underway to develop a framework for producing fiscal forecasts that will help in preparing future budgets. A full set of forecasts is expected to be completed by June in order to feed into the 2011 budget cycle.

32. **The roll out of IFMIS to MDAs will continue to strengthen budget execution.** So far, IFMIS has been rolled out to 11 key MDAs with 2 additional MDAs in the process, accounting for about 65 percent of expenditures. The MOFED will continue to provide training and support to IFMIS users across MDAs to ensure that activities are properly and adequately captured within the system.

Financial sector measures

33. **The BSL will improve the conduct of monetary policy by establishing a benchmark interest rate** (*Structural Benchmark for September 2010*)**.** The reverse repo rate will be used as the benchmark rate and this rate will be announced after every Monetary Policy Committee meeting. This interest rate will be used to signal the stance of the monetary policy to the market.

34. **The independence of the BSL will be strengthened.** The GoSL commits to ensuring the operational independence of the BSL. To this end, the BSL and Banking Acts will be amended to ensure efficient management of monetary policy and to make the Banking Act consistent with international best practices in line with the Basel core principle. The government will continue to recapitalize the BSL by converting non-negotiable non-interest bearing securities into marketable instruments. In order to minimize the losses from its engagement in community banks, the BSL will expedite its exit.

35. **To develop a long-term capital market,** the MOFED and the BSL will engage market participants, including the commercial banks, NASSIT and other non-bank financial institutions, to develop a long-term bond market consistent with the government's financing need. The GoSL will also strengthen the capital market regulatory structure and governance by enacting the Securities and Exchange Commission's (SEC) Act and implement associated regulations, and deepen the long- term capital market with the privatization and divestiture of slated public enterprises.

36. **The BSL will strengthen its supervisory role to reduce the vulnerabilities arising in the financial sector from NPLs.** To this end, the BSL will adopt new off-site surveillance

guidelines for banks (*Structural Benchmark June 2010*). The BSL will also build capacity to move towards risk-based supervision.

37. **Private sector development is constrained by limited access to financial services.** Lack of financial development is evident in low credit to the private sector. Access to credit will be enhanced by strengthening information structure through establishing a credit reference bureau (*Structural Benchmark for December 2010*). To improve efficiency of transactions in the economy, the BSL will work towards strengthening the payments and settlements system.

Domestic fuel pricing

38. ***The* GoSL will improve the transparency of the pricing framework for petroleum products by implementing an automatic price adjustment mechanism.** The present system of ad-hoc price adjustment poses a fiscal risk to the budget should international fuel prices continue their recent upward trend. To maintain fiscal prudence and depoliticize fuel pricing, the GoSL will adopt an automatic price adjustment mechanism to ensure full pass-through of changes in international prices (*Structural Benchmark for June 2010*). This new mechanism comprises (i) at least monthly domestic retail fuel price adjustments; (ii) a Le 1,000 per gallon cap on retail price changes (up or down) for each monthly adjustment; (iii) adjustment in fuel excises (up or down) to cover for the less than full pass through in the short term implied by the cap. The Strategic Petroleum Stock Fund, which was originally intended for financing a physical stock reserve of fuel and has now been depleted, will be eliminated. This will allow for the removal of the current Le 200 contribution to strategic stocks in the current formula.

D. Economic Statistics

39. **There is a need to strengthen Sierra Leone's capacity to collect and disseminate economic statistics.** Statistics of Sierra Leone (SSL) is seeking technical assistance from the IMF to improve the reporting of national account and price statistics. There is a particular need to improve collection of agriculture output and compute one single reliable consumer price index.

VI. Program Monitoring

40. The program for the first year will be monitored based on quantitative performance criteria for end-June and end–December 2010 (Table 3) and structural benchmarks for 2010 (Table 4).

Table 1. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2009

(Cumulative change from beginning of calendar year to end of month indicated; Le millions, unless otherwise indicated)[1]

	December 2009			
	Perf. criteria *Prog.*[2]	Adjusted *targets*	*Prel.*	Met or Not met
Performance criteria				
Net domestic bank credit to the central government (ceiling)	151,223	179,497	108,994	Met
Unadjusted target (ceiling)		151,223		
Adjustment for the shortfall (excess) in external budget support		-4,381		
Adjustment for the issuance of treasury securities to the private sector		32,655		
Net domestic assets of the central bank (ceiling)	-368,577	-418,135	-429,852	Met
Unadjusted target (ceiling)		-368,577		
Adjustment for the shortfall (excess) in external budget support		-4,381		
Adjustment for exchange rate depreciation (appreciation)		-45,177		
Domestic primary fiscal balance of the central government (floor)	-246,785	-246,785	-254,191	Not met
Subsidies to National Power Authority (ceiling)[3]	0		0	Met
Gross foreign exchange reserves of the central bank, US$ millions (floor)	124	112.58	126.9	Met
Unadjusted target (floor)		124.08		
Adjustment for the shortfall (excess) in external budget support[4]		1.24		
Adjustment for the shortfall in the US$ value of IMF disbursement		-18.29		
Adjustment for the increase (decrease) in BSL short-term foreign currency liabilities		5.55		
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling)[3]	0	0	0	Met
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling)[3]	0	0	0	Met
External payment arrears of the public sector (ceiling)[3]	0	0	0	Met
Total domestic government revenue (floor)	724,790	724,790	749,195	Met
Indicative target				
Poverty-related expenditures (floor)	337,474		361,615	Met
Memorandum items:				
External budgetary assistance[4]	254,789		328,696	
Net credit to government by nonbank sector[5]	7,500		-25,155	
PRGF disbursements (US$ millions)	37		19	
Exchange rate (Leones/US$)	3,543		3,856	

Sources: IMF staff projections and data from the authorities.

[1] The performance criteria and indicative targets shown in this table are defined in the Technical Memorandum of Understanding (TMU).
[2] IMF Country Report No. 10/15.
[3] These apply on a continuous basis.
[4] Including program grants and program loans.
[5] Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the nonfinancial private sector.

Table 2. Sierra Leone: Structural Benchmarks for 2009

Measures	Timing	Macro Rationale	Status
Macroeconomic policy coordination			
Provide to Fund staff the Monetary and Policy Committee (MPC) monthly minutes that include the monthly projections for government revenue and expenditures made available by the Ministry of Finance to the Bank of Sierra Leone to produce a monthly liquidity forecast.	On a continuous basis	To strengthen liquidity management and enhance monetary and fiscal policy coordination.	Met
Tax administration and policy			
• Establish a Domestic Tax Department (DTD) as the vehicle for achieving integration of domestic tax collection and make it functional.	End–December	To improve efficiency of revenue collection efforts.	Not met, but expected to be met by end-September 2010 in the new program.
• Integrate the Goods and Services Tax (GST) administration within the Large Taxpayer Office (LTO).	End–December	To ensure full and efficient implementation of the GST to achieve domestic revenue target.	Not met. Will be met by end-December in the new program.
• Introduce the Goods and Services Tax (GST).	January 1, 2010	To broaden the tax base and improve efficiency of revenue collection.	Met.
Public financial management			
• Recruit and assign budget officers to MDAs that have IFMIS 'rolled out' and ensure their budget committees are fully operational.	End–December	Improve spending efficiency by enhancing public financial management and budget execution.	Not met, but was implemented in March 2010.
Financial supervision			
• Adoption by the BSL of new off-site surveillance guidelines for banks consistent with the requirements of the revised Banking and Other Financial Services Act, and introduction of new reporting requirements based on these guidelines.	End–September	Financial deepening which is vital to achieve the growth objective of the program.	Not met. This measure will be met by end-June in the new program.
Public enterprise reform			
• Adopt a comprehensive tariff policy for the electricity sector that will strengthen the financial position of the National Power Authority.	End-December	To improve financial viability of the public electricity. This will ensure an efficient and sustainable power supply, critical for the growth objectives of the program.	Not met. The World Bank is becoming more involved in the electricity sector and has advised the authorities to conduct a new tariff study before a policy is decided. Also, since tariffs were increased in 2009, likely well above the long-term marginal cost, there is no urgency to adopt a policy to safeguard budget resources.

Table 3. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2010[1]

(Cumulative change from beginning of calendar year to end of month indicated; Le billions, unless otherwise indicated)

	2009	2010		
	Actual Stock	*Jun.*	*Sept.* [2]	*Dec.*
Performance criteria				
Net domestic bank credit to the central government (ceiling)	105.7	191.5	202.7	180.4
Net domestic assets of the central bank (ceiling)	-442.3	198.6	235.5	235.1
Gross foreign exchange reserves of the central bank, US$ millions (floor)	336.4	-8.7	-11.8	0.0
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) [3]	…	0.0	0.0	0.0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) [3]	0.0	0.0	0.0	0.0
External payment arrears of the public sector (ceiling) [3]	…	0.0	0.0	0.0
Indicative target				
Total domestic government revenue (floor)	…	432.8	676.8	946.3
Poverty-related expenditures (floor)	…	252.2	337.9	417.0
Memorandum items:				
External budgetary assistance (US$ million) [4]	…	29.6	52.1	77.8
Net credit to government by nonbank sector [5]	…	44.0	-8.8	-27.1
PRGF disbursements (SDR millions)		11.4	11.4	15.9
Exchange rate (Leones/US$)	…	3,990	3,990	3,990

Sources: IMF staff projections.

[1] The performance criteria and indicative targets are defined in the Technical Memorandum of Understanding (TMU).
[2] Indicative target.
[3] These apply on a continuous basis.
[4] Including grants and loans.
[5] Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the nonfinancial private sector.

Table 4. Sierra Leone: Structural Benchmarks for 2010

Measures	Timing	Macro Rationale
• Adopt a domestic fuel pricing formula that reflects full pass-through of international oil prices.	End–June	To enhance transparency and eliminate risks for the budget in case of external shocks.
• Adoption by the BSL of new off-site surveillance guidelines for banks.	End–June	To enhance the supervisory role of the BSL for financial sector development.
• Establish a Domestic Tax Department (DTD) as the vehicle for achieving integration of domestic tax collection and make it functional, including recruiting Commissioner and Deputy Commissioner.	End-September	To improve efficiency of revenue collection efforts.
• Submit to parliament amendments of the Government Budgeting and Accountability Act (2005) and Financial Management Regulation to ensure that only viable capital projects enter into the budget.	End-September	To improve efficiency of public investments and achieve the program growth targets.
• Establish reverse repo rate as the benchmark interest rate and announce the rate after every Monetary Policy Committee meeting.	Continuous from end-September	To increase the effectiveness of monetary policy and help develop a yield curve.
• Establish a credit reference bureau.	End–December	To improve informational infrastructural and promote credit access for credit-worthy customers.
• Integrate the Goods and Services Tax (GST) administration within the Large Taxpayer Office (LTO).	End-December	To ensure full and efficient implementation of the GST to achieve domestic revenue target

APPENDIX I—ATTACHMENT II
SIERRA LEONE: TECHNICAL MEMORANDUM OF UNDERSTANDING

May 18, 2010

I. INTRODUCTION

1. This memorandum sets out the understandings between the Sierra Leonean authorities and the International Monetary Fund (IMF) regarding the definitions of the quantitative performance criteria (PCs) and structural benchmarks (SBs) for the program supported by the Extended Credit facility (ECF) arrangement, as well as the related reporting requirements. Unless otherwise specified, all quantitative PCs and indicative targets will be evaluated in terms of cumulative flows from the beginning of the period, as specified in Table 3 of the Memorandum of Economic and Financial Policies (MEFP).

2. **Program exchange rates.** For the purpose of the program, foreign currency denominated *transactions* in 2010 will be converted from their U.S. dollar denominated value into Sierra Leonean currency (leones) using a program exchange rate of Le 3,990/US$.

II. QUANTITATIVE PERFORMANCE CRITERIA

A. Gross Foreign Exchange Reserves of the Bank of Sierra Leone (BSL)

3. **Definition**. Unless otherwise noted, gross foreign exchange reserves of the Bank of Sierra Leone (BSL) are defined as reserve assets of the BSL. Reserve assets are defined in the IMF's *Balance of Payments Manual* (5th ed.) and elaborated in the reserve template of the Fund's *International Reserves and Foreign Currency Liquidity: Guidelines for a Data Template*. They exclude foreign assets not readily available to, or controlled by, the monetary authorities.

Adjustment clauses.

4. The floor on the change in gross foreign exchange reserves will be adjusted (a) downward (upward) by the amount in U.S. dollars of the shortfall (excess) in programmed external budgetary assistance[1]—the downward adjustment will be capped at the equivalent of US$20 million; (b) downward (upward) for any shortfall (excess) in the U.S. dollar value of disbursements from the IMF under the ECF arrangement; and (c) upward (downward) for any increase (decrease) in BSL short-term (one year or less in original maturity) foreign currency-denominated liabilities (to residents and nonresidents).

[1] External budgetary assistance is defined as program grants and program loans, excluding HIPC assistance.

B. Net Domestic Assets of the BSL

5. **Definition.** Net domestic assets (NDA) of the BSL are defined as the end-period stock of the reserve money less the end-period stock of net foreign assets calculated at the program exchange rates. Reserve money includes currency issued (equal to currency outside banks plus cash in vaults) and deposits of commercial banks with the BSL. Net foreign assets of the BSL are defined as gross foreign exchange reserves (defined above) minus foreign liabilities. Foreign liabilities are defined as foreign currency-denominated liabilities of the BSL to nonresidents and the outstanding use of Fund credit. For program purposes, foreign liabilities exclude SDR allocation.

6. **Adjustment clauses.** The ceiling on NDA of the BSL will be adjusted upward (downward) by the leone value of the shortfall (excess) in the external budgetary assistance at the test dates—the upward adjustment will be capped at the equivalent of US$20 million.

C. Net Domestic Bank Credit to the Central Government (NCG)

7. **Definition.** NCG refers to the net banking system's claims on the central government as calculated by the BSL. It is defined as follows:

- the net position of the government with commercial banks, including: (a) treasury bills, excluding holdings of treasury bills for monetary operations; (b) treasury bearer bonds; and (c) loan and advances of commercial banks to the government; less government deposits in commercial banks;

- the net position of the government with the BSL, including: (a) treasury bills, excluding holdings of treasury bills for monetary operations; (b) treasury bearer bonds; and (c) ways and means; less (a) central government deposits; and (b) HIPC and MDRI relief deposits.

8. **Adjustment clauses.** The ceiling on NCG will be adjusted (a) upward (downward) by up to the leone value of the shortfall (excess) in external budgetary assistance—the upward adjustment will be capped at the equivalent of US$20 million; (b) downward (upward) by the excess (shortfall) in the leone value of net issues of government securities to the nonbank private sector vis-à-vis the program assumption (as specified in the memorandum items in Table 3 of the MEFP).

9. **Data source**. The data source for the above will be the series "Claims on government (net)", submitted to the IMF staff and reconciled with the monthly monetary survey prepared by the BSL, excluding transactions related to monetary policy operations as defined by BSL.

10. **Definition of Central government.** Central government is defined for the purposes of this memorandum to comprise the central government and those special accounts that are classified as central government in the BSL statement of accounts. The National Social Security and Insurance Trust and public enterprises are excluded from this definition of central government.

D. External Payment Arrears of the Public Sector

11. **Definition.** External payment arrears of the public sector are defined as the stock of new external overdue debt-service payments by the public sector. For the purposes of this PC, the public sector comprises the central government, regional government, all public enterprises and the BSL. The nonaccumulation of external arrears is a performance criterion during the program period. Excluded from this PC are those debts subject to rescheduling. This PC will apply on a continuous basis.

E. New Nonconcessional External Debt Contracted or Guaranteed by the Public Sector with an Original Maturity of One Year or More

12. **Definition**. Those are defined as all forms of new debt with original maturity of one year or more contracted or guaranteed by the public sector (see paragraph 11 for definition of public sector) based on the residency criterion. This PC applies not only to debt as defined in the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274 (00/85), August 24, 2000, Point 9, as revised on August 31, 2009, (Decision No. 14416-(09/91)) but also to commitments contracted or guaranteed for which value has not been received. Excluded from this PC are disbursements from the IMF and those debts subject to rescheduling. For the purposes of this PC, the "public sector" is as defined in ¶11 above. This PC will apply on a continuous basis.

13. Any external debt of which the net present value, calculated with the reference interest rates mentioned hereafter, is greater than 65 percent of the nominal value (grant element of less than 35 percent) is considered nonconcessional, with the exception of IMF lending. For debt with a maturity of more than 15 years, the average of the ten-year commercial interest reference rates (CIRRs) published by the OECD is used to calculate the grant element. The average of the six-month CIRRs is used for debt with shorter maturities. For loans in foreign currencies for which the OECD does not calculate a CIRR, calculation of the grant element should be based on the CIRR in SDRs. The Government will report any new external borrowing and its terms to Fund staff as soon as external debt is contracted or guaranteed by the government.

F. External Short-Term Debt Contracted or Guaranteed by the Public Sector

14. **Definition**. External short-term debt is defined as external debt stock with a maturity of less than one year contracted or guaranteed by the public sector (see paragraph 11 for definition of public sector). Debt is defined in Annex I of this TMU. For this purpose, short-term debt will exclude normal trade credit for imports. For the purposes of this PC, the public sector is as defined in ¶11 above. This PC will apply on a continuous basis.

III. Quantitative Indicative target

A. Domestic Revenue of Central Government

15. **Definition**. The floor on total domestic central government revenue is defined as total central government revenue, as presented in the central government financial operations table, excluding external grants.

B. Poverty-Related Expenditures

16. **Definition**. Poverty-related expenditures refer to those expenditures in the areas identified in Table 2 of the Sierra Leone HIPC Decision Point Document.

IV. Program Monitoring

17. The Sierra Leonean authorities shall maintain a program-monitoring committee composed of senior officials from the MoFED, the BSL, and other relevant agencies. The committee shall be responsible for monitoring performance under the program, recommending policy responses, informing the IMF regularly about the progress of the program, and transmitting the supporting materials necessary for the evaluation of PCs and benchmarks. The committee will provide monthly reports to the IMF on progress in implementing the program's quantitative targets and structural benchmarks.

ANNEX 1: IMPLEMENTATION OF THE REVISED GUIDELINES ON PERFORMANCE Criteria with Respect to Foreign Debt

The term “debt” has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000, which reads as follows: “(a) For the purpose of this guideline, the term “debt” will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers’ credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers’ credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property. (b) Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt”. (c) Excluded from this performance criterion are normal import-related credits, disbursements from the IMF, and those debts subject to rescheduling arrangements.”

Sierra Leone: Summary of Data to be Reported to IMF Staff

Type of Data	Tables	Frequency	Reporting Deadline
Real sector	National accounts	Annual	End of year + 9 months
	Revisions of national accounts	Variable	End of revision + 2 months
	Disaggregated consumer price index	Monthly	End of month + 2 weeks
Public finance	Net government position and details of nonbank financing, including the stock of the float, treasury bills, and bonds, as well as privatization receipts	Monthly	End of month + 6 weeks
	Government flow-of-funds table (Government Financial Operations Table) with supporting documentation (final) and presented on commitment and cash bases	Monthly	End of month + 6 weeks
	Petroleum product prices and tax receipts by categories of petroleum products	Monthly	End of month + 6 weeks
	Stock of outstanding payment commitments with a breakdown between current and capital expenditures	Monthly	End of month + 6 weeks
	Import duty exemptions by end-users and tariff regimes and estimates of corresponding revenue losses	Quarterly	End of quarter + 6 weeks
Monetary and financial data	Monetary survey	Monthly	End of month + 6 weeks
	Balance sheet of the BSL	Monthly	End of month + 6 weeks
	Consolidated balance sheets of commercial banks	Monthly	End of month + 6 weeks
	BSL monitoring sheet of net financing of the financial sector to the government	Monthly	End of month + 6 weeks
	BSL monitoring sheet of treasury bills and bonds holdings	Monthly	End of month + 6 weeks
	Borrowing and lending interest rates	Monthly	End of month + 6 weeks
	Results of foreign exchange and Treasury Bills auctions	Weekly	End of week + 3 days
	Stocks of government securities	Monthly	End of month + 6 weeks
	Banking supervision ratios	Quarterly	End of quarter + 8 weeks

Sierra Leone: Summary of Data to Be Reported to IMF Staff (concluded)

Type of Data	Tables	Frequency	Reporting Deadline
Monetary and financial data			
	Gross official foreign reserves	Weekly	End of week + 1 week
	Foreign exchange cashflow table	Monthly	End of quarter + 4 weeks
	Revised balance of payments data	Monthly	When revisions occur
	Exports and imports of goods (including the volume of key minerals and fuels)	Monthly	End of month + 3 months
External debt	Outstanding external arrears and repayments (if applicable)	Monthly	End of month + 4 weeks
	Details of all new external borrowing and guarantees provided by government on new borrowing, including the associated concessionality calculation (percentage) for each new loan.	Monthly	End of month + 4 weeks
	External debt service payments (separately on principal and interest payment) to each creditor, including and excluding new disbursements in the debt recording system. Also, including and excluding HIPC relief.	Monthly	End of month + 4 weeks
HIPC initiative and MDRI monitoring	Statement of special account at the BSL, that receives resources generated by the HIPC Initiative and tracks their use	Monthly	End of month + 4 weeks
	Statement of special MDRI account at the BSL and the corresponding poverty-reducing spending financed	Monthly	End of month + 4 weeks
	Minutes of the meeting of the Monetary Policy Committee	Monthly	Date of meeting + 2 weeks

INTERNATIONAL MONETARY FUND

SIERRA LEONE

Sixth Review Under the Arrangement Under the Extended Credit Facility, Request for Waiver for Nonobservance of a Performance Criterion, Request for a Three-Year Arrangement Under the Extended Credit Facility, and Financing Assurances Review—Informational Annex

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

May 19, 2010

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Appendix I. Relations with the Fund
(As of April 30, 2010)

I. Membership Status: Joined 9/10/62; Article VIII

II. General Resources Account:	**SDR Million**	**% Quota**
Quota	103.70	100.00
Fund holdings of currency	103.69	99.99
Reserve position	0.02	0.02

III. SDR Department:	**SDR Million**	**% Allocation**
Net cumulative allocation	99.51	100.00
Holdings	120.95	121.55

IV. Outstanding Purchases and Loans:	**SDR Million**	**% Quota**
ECF Arrangements	58.88	56.78

V. Latest Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF	5/10/06	5/9/10	51.88	44.88
ECF	9/26/01	6/25/05	130.84	130.84
ECF	3/28/94	5/04/98	101.90	96.85

VI. Projected Payments to Fund[1]
(SDR million; based on current use of resources and present holdings of SDRs):

	Forthcoming				
	2010	2011	2012	2013	2014
Principal	1.40	3.27	4.62	4.62	8.12
Charges/interest	0.01	0.01	0.13	0.12	0.11
Total	1.41	3.27	4.76	4.74	8.23

VII. Implementation of HIPC Initiative

	Enhanced Framework
Commitment of HIPC Initiative assistance	
Decision point date	March 2002
Assistance committed (NPV terms)	
By all creditors (US$ million)[2]	675.20

[1] When a member has overdue financial obligations outstanding for more than three months, the amount will be shown in this section.

[2] Assistance committed under the original framework is expressed in net present value (NPV) terms at the

Of which: IMF assistance (US$ million)	125.21
(SDR equivalent in millions)	100.00
Completion point date	December 2006
Disbursement of IMF assistance (SDR million)	
Amount disbursed	100.00
Interim assistance	66.03
Completion point balance	33.97
Additional disbursement of interest income [3]	6.58
Total disbursements	106.58

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI):

I. MDRI-eligible debt (SDR Million) [4]	117.34
Financed by: MDRI Trust	76.75
Remaining HIPC resources	40.59

II. Debt Relief by facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGF**	**Total**
December 2006	N/A	117.34	117.34

IX. Safeguards Assessment

Pursuant to IMF policy, the Bank of Sierra Leone was subject to a safeguards assessment with respect to the PRGF arrangement approved on May 10, 2006. The assessment, which was completed on June 12, 2006, proposed recommendations to address new and continuing vulnerabilities in financial reporting, internal audits, and internal controls. An update of the 2006 safeguards assessment report was completed in October 2009.

completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

[3] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim.

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

X. Exchange Rate Arrangement

For customs valuation purposes and for official transactions, the Bank of Sierra Leone (BSL) calculates an official exchange rate every Friday morning as the weighted average of the auction rate, the commercial bank mid-rate, and the bureau mid-rate in the previous week. Commercial banks may buy foreign exchange from and sell it to individual customers and may trade among themselves or with the BSL on a freely negotiable basis. As of May 6, 2010, the BSL mid-rate was Le 3,902.20=US$1.

In March 2008 the exchange rate regime was reclassified as "a conventional peg" to reflect the nominal stability of exchange rate developments under *de facto* management through the auction by the BSL as the only seller of foreign exchange. Effective February 2, 2009, the *de facto* exchange rate arrangement was reclassified from a conventional pegged arrangement to a "stabilized arrangement" retroactively to April 30, 2008, due to a revision of the classification methodology.

With effect December 14, 1995, Sierra Leone has accepted the obligations of Article VIII, Sections 2, 3, and 4. On June 29, 2001, Sierra Leone removed the remaining exchange restriction, in the form of a tax clearance certificate required for payments and transfers of certain types of current international transactions. Sierra Leone continues to maintain an exchange system free of restrictions on the making of payments and transfers for current international transactions.

XI. Article IV Consultation

The Executive Board concluded the 2008 Article IV consultation on December 22, 2008. The next Article IV consultation will be held in accordance with the decision on consultation cycles approved on July 15, 2002.

XII. Technical Assistance

Department	Purpose	Date
FAD	Review of petroleum pricing mechanism	February 2010
	Tax administration	January 2010
	Evaluation of progress in PFM reforms	March 2009
	Assist in designing a simplified regime for small taxpayers	January 2009
	Evaluation of progress on tax administration reform and VAT preparation	September 2008
	Evaluation of progress on PFM reforms	July 2008

Department	Purpose	Date
	Implementation of public financial management reforms	March 2008
	Tax administration reforms for successful VAT implementation	February 2008
MCM	Banking Supervision and Banking Regulation	April 2010
	Needs assessment and monetary operations and foreign exchange auction system	March 2010
	Follow-up assessment on TA needs	June 2009
	Follow-up assessment of banking supervision processes at BSL	March 2009
	Follow-up assessment on progress in strengthening central bank internal auditing	March 2009
	BSL: Internal audit and management of the central bank	October 2008
	Monetary policy, banking supervision, and recapitalization of the BSL	April/May 2008
	Recapitalization of the BSL	February 2008
STA	Assist the authorities in implementing the international standards recommended in the *Monetary and Financial Statistics Manual*	April 2009
	National accounts statistics mission	March 2009
	National accounts statistics mission	September/October 2008
	National accounts statistics mission	January 2008

XII. Resident Representative

Mr. Meshack Tjirongo assumed responsibility for the Fund office in March 2010 as a new resident representative. Mr. Tjirongo covers both The Gambia and Sierra Leone and is stationed in Banjul.

Appendix II. Sierra Leone Joint World Bank-IMF Work Program, 2010

Title	Activities	Provisional Timing of Mission	Expected Delivery Date
	A. Mutual Information on Relevant Work Programs		
World Bank work program	Public Expenditure Review	February 2009	May 2010
	Supplement to Third Governance Reform and Growth Credit (GRGC 3)	May 2010	June 2010
	Fourth Governance Reform and Growth Credit (GRGC 4)	Multiple 2010	October 2010
	IRCBP Supervision	June & Nov. 2010	N/A
	IPFMRP (PFM Project) Supervision	Feb-Mar. & June 2010	N/A
	Decentralized Service Delivery Spn.	Multiple 2010	N/A
IMF work program	2010 Article IV consultation and first PRGF review	September 2010	December 2010
	Technical Assistance		
	FAD:		
	• Tax administration reform	N/A	N/A
	MCM		
	• Bank supervision and Banking regulation	May 2010	June 2010
	STA		
	Monetary and Banking Statistics	September 2010	N/A
	National Accounts and Price Statistics	July 2010	N/A
	B. Agreement on Joint Products and Missions		
Joint products in 2010	DSA		December 2010
	Assisting the authorities with the implementation of their financial sector reform strategy		Continuous

Appendix III. Statistical Issues

1. Data provided to the Fund are affected by serious shortcomings that significantly hamper surveillance. The prolonged civil war resulted in a virtual collapse of statistical systems in the late 1990s. Serious deficiencies still affect balance of payments statistics, national accounts, and social indicators. The authorities are cooperating fully in providing data to the Fund and regularly disseminating economic and financial data to the public. The country participates in the GDDS, but its metadata need to be updated.

2. A major and sustained improvement in the coverage and timeliness of economic data will require greater interagency coordination and restructuring the institutional framework. Statistics Sierra Leone (SSL) continues to face a shortage of budgetary resources which adversely affects compilation of national accounts and price statistics. Since March 2004, and with support from the GDDS Anglophone Africa Project, fourteen national accounts TA missions visited Freetown, the most recent in March 2009. These missions reviewed source data, methodologies, compilation, and dissemination issues and assisted with data development and improvements in methodology. But the impact of TA has been limited by the lack of source data. In this regard, the agriculture survey launched in March 2010 will significantly improve the quality of GDP estimates. Work in this area will continue under a new DfID-funded project, Enhanced Data Dissemination Initiative, slated to start in July 2010.

National accounts

3. The coverage of private sector activities in the national accounts is hampered by an outdated business directory and low response rates to surveys. In particular, small businesses, which represent a very high proportion of business activity, are not adequately captured in national account statistics. The consumer price index (CPI) is used extensively to derive estimates of GDP at constant prices. AFR missions continue to make their own estimates and projections of key national accounts aggregates, as well as making adjustments to historical data using new information.

4. Efforts to reconstruct the national accounts estimates commenced during 2003/04, with the main effort being to prepare new estimates for the period starting in 2001. Because resource constraints significantly hindered the production of final estimates, only preliminary data for 2001–04 were made available. Efforts are underway to prepare revised national accounts based on a 2005 benchmark and using 2005 prices to compile constant price estimates. However, shortages of resources and staff continue to pose major constraints to the statistical development undertaken by SSL.

Prices

5. The SSL compiles the CPI monthly and publishes it with a lag of about three weeks. It has been rebased to 2003 using the 2003 Sierra Leone integrated household survey and continues to cover the capital city and three towns. While a national CPI is being compiled, the authorities continue to publish the old CPI (1992=100). To avoid confusion, the authorities have requested TA to validate the work done in order to adopt a common series. The production of producer price indices remains a medium-term goal planned to start in 2009.

Government finance statistics

6. The budget reporting system was established with assistance from the Fund/UNDP technical assistance project. Monthly data on central government revenue, current expenditure, and financing are provided with appropriate detail. Fiscal data are reported to AFR and plans are underway to resume reporting annual data for publication in the *GFS Yearbook* (the most recent data refer to 2004). Fiscal data only cover the central government. With the current drive towards decentralization and the growing role of the local government, there is an urgent need to compile and monitor data for the whole of general government.

7. There is an urgent need for more timely and accurate data on foreign-financed development projects. Reports on implementation of the development budget and its financing are currently not produced in a format that is suitable for budget analysis because the necessary data are not available. There is also need for quality control of the final data. The authorities are currently considering introduction of a flash reporting system for government expenditure in general and for foreign aid-financed projects. As part of the GDDS regional project for Anglophone African countries, work has been undertaken to reconcile fiscal and monetary data and to improve the coverage and classification of the two data sets.

Monetary statistics

8. The main components of the central bank balance sheet are available daily and weekly; this system provides an early warning system on key financial targets. The full monetary survey is compiled by the BSL with a lag of about six weeks; it has comprehensive coverage of commercial banks.

9. There has been some progress in the compilation of data in line with the *2000 Monetary and Financial Statistics Manual*. The BSL, with assistance from STA, has completed the preparation of a standardized report form (SRF) for the central bank, and started reporting monetary data in the SRF-format to the IMF in April 2010. Work on preparation of the SRF for other financial corporations continues.

10. Reconciliation of fiscal and monetary statistics remains a challenge. In the past, compilation of fiscal data solely on a cash basis and differences in the coverage of the central government explained most of the discrepancies between the datasets. In 2007, a TA mission found limited progress on previous recommendations on the fiscal reporting system for extra budgetary agencies and projects. The coverage of reporting agencies had improved, but there were many obvious errors and omissions in the data and in the BSL database. However, in June 2008 the authorities notified the IMF that the fiscal data have been reconciled with the expanded BSL monetary data.

Balance of payments

11. The BSL is responsible for compiling balance of payments (BOP) statistics. It obtains source data from the SSL, government ministries, the Customs and Excise Department (Customs), and the "Financial Survey of Major Limited Companies," for data on foreign direct investment. Imports and exports of goods estimates are based on data compiled by Customs and are adjusted for coverage, valuation, and timing to accord with BOP definitions. The BSL does not adjust BOP data using supplementary information to take account of unreported data.

12. External transactions are characterized by a large volume of activity in the informal sector, principally diamond smuggling. A considerable portion of imports is financed by these unrecorded exports. As a result, official BOP statistics tend to substantially understate transactions. Staff has been addressing this problem through the use of third-country (principally EU member) import data. STA has been providing technical assistance on BOP issues through the GDDS project to help the authorities implement the *Balance of Payments Manual, Fifth Edition (BPM5)*.

13. Data problems also exist for trade in services, income statistics, current transfers, and the capital and financial accounts. Regarding the last, there are substantial difficulties in tracking financial transactions of the public and private sectors that are routed through commercial banks. While the authorities are producing data on the international investment position, improvements are required in coverage and in valuation adjustments. These difficulties are manifested in reconciling flow data in the BOP and stocks in the international investment position. Estimates of smuggled imports and exports, in particular diamonds, are also not available.

14. Information on official grant and loan receipts is relatively good and is prepared by AFR on the basis of contact with the authorities and donor agencies, but data on private capital flows are very poor. Some information on private banking flows can be derived from the monetary survey. Other private flows, especially those linked to the informal diamond trade, are implicitly included in "errors and omissions."

Sierra Leone: Table of Common Indicators Required for Surveillance

May 2010

	Date of latest observation	Date received	Frequency of Data[4]	Frequency of Reporting[4]	Frequency of publication[4]
Exchange Rates	03/25/10	03/30/10	D	W	W
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	09/09	10/15/09	M	M	M
Reserve/Base Money	03/10	05/06/10	M	M	M
Broad Money	03/10	05/06/10	M	M	M
Central Bank Balance Sheet	03/10	05/06/10	M	M	M
Consolidated Balance Sheet of the Banking System	03/10	05/06/10	M	M	M
Interest Rates[2]	03/10	05/06/10	W	M	W
Consumer Price Index	03/10	04/23/10	M	M	M
Revenue, Expenditure, Balance and Composition of Financing – Central Government	03/10	04/19/10	M	M	N/A
Stocks of Central Government and Central Government-Guaranteed Debt	12/09	03/11/10	Q	Q	N/A
External Current Account Balance	12/09	03/11/10	A	A	A
Exports and Imports of Goods and Services	12/09	03/11/10	A	A	A
GDP/GNP	12/09	03/15/10	A	A	A
Gross External Debt	12/09	03/11/10	A	A	A
International Investment Position[3]	06/09	08/31/09	A	A	A

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[4] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).

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International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Sixth Review Under Sierra-Leone's ECF, and Approves a New three-year ECF

The Executive Board of the International Monetary Fund (IMF) today approved the sixth review of Sierra Leone's performance under the Extended Credit Facility (ECF) arrangement. The approval will enable a final disbursement of SDR 7 million (US$ 10.2 million), bringing total disbursements under the program to SDR 51.88 million (US$ 75.8 million). In completing the review, the Executive Board granted a waiver for the non-observance of the quantitative performance criterion on the domestic primary fiscal balance of the central government.

The Board has also approved a new three-year successor arrangement under the ECF in a total amount equivalent to SDR 31.11 million (US$ 45.5 million), which will take effect on July 1st, 2010, and will enable the first disbursement of an amount equivalent to SDR 4.44 million (US$ 6.5 million). The new arrangement is designed to support the authorities' program to raise economic growth by increasing investment in infrastructure and developing an accessible financial sector. The program will help create fiscal space for accelerated capital and social spending by broadening the tax base, containing non-priority spending, and raising public sector efficiency, especially in project selection and implementation.

The Executive Board originally approved a three-year Poverty Reduction and Growth Facility (PRGF) arrangement in 2006 (see Press Release No.06/94) which was later extended by one year and recently converted to an ECF.

At the conclusion of the Executive Board discussion on Sierra Leone, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair, stated:

"After being adversely affected by falling global demand last year, economic activity is expected to pick up in 2010 due to a recovery in export demand and continued investment in infrastructure. Inflation rose sharply in early 2010, reflecting a jump in the price level related to the implementation of the new goods and services tax and a depreciation of the leone against the U.S. dollar in the second half of 2009. Gross international reserves remain at comfortable levels.

"The policies supported by a new three-year Extended Credit Facility arrangement will raise economic growth by increasing investment in infrastructure and developing an accessible financial sector. For 2010 and in the medium-term, fiscal space for higher capital and social spending will be created by broadening the tax base, containing non-priority spending, and raising public sector efficiency, especially in project selection and implementation. The introduction of the goods and services tax, implementation of the new Mines and Minerals Act, and strengthening of tax administration will improve revenue collection. The establishment of an automatic pricing framework for petroleum products to ensure full pass-through of prices will reduce the fiscal risk from high international fuel prices.

"The government recently launched a new free healthcare initiative for children and pregnant women with the aim of reducing the high infant and maternal mortality rates. This is a welcome initiative but its fiscal implications need to be assessed continuously to ensure sustainability of the policy. To this end, sustained efforts to improve revenue performance and to implement a pay reform covering the entire public sector will be important.

"Monetary policy will seek to maintain low and stable inflation. The authorities are also committed to maintaining the flexible exchange rate regime to facilitate adjustment to external shocks," Mr. Portugal noted.

Annex

Recent Economic Developments

Economic activity in Sierra Leone continued to decline in the first half of 2009 due to falling global demand and declining foreign inflows from remittances. Despite a pickup in exports of diamonds and agricultural products in the second half of 2009 and an increase in domestic food production, real GDP growth for the year as a whole slowed to 4 percent in 2009 compared with 5.5 percent in 2008. Although inflation subsided in the first half of 2009, the depreciation of the leone in the second half of the year combined with higher domestic fuel prices contributed to a pickup in end-2009 inflation rate. In February 2010, inflation jumped to 17 percent from 10.8 percent in December, reflecting largely the difficulties in implementing the new Goods and Services Tax in January and higher domestic fuel prices.

The external current account deficit is estimated to have declined to 8.4 percent of GDP in 2009 from 11.7 percent in 2008, reflecting an increase in official transfers and weak imports. Exports increased by about 4 percent while imports decreased by about 2.5 percent. Gross international reserves corresponded to 6.4 months of imports.

Program Summary

Under the new ECF-supported program, the government aims to raise economic growth in the medium term by accelerating investments in infrastructure and developing an accessible financial sector. The program is designed to:

- create fiscal space to improve basic infrastructure and social services while maintaining macroeconomic stability;
- strengthen tax performance and improve public financial management (PFM) systems; and
- deepen the financial sector to promote private-sector led growth.

The macroeconomic objectives of the government program are to:

- Raise real GDP growth to 6 percent by 2012;
- Increase domestic revenues to at least 13.5 percent of GDP by 2012;
- Bring inflation down to 8 percent by end 2012;
- Maintain the overall budget deficit below 4–5 percent of GDP annually through 2012.

Structural reforms will complement the macroeconomic program. The focus will be on:

- Improving tax administration by making revenue collections more efficient and effective to achieve domestic revenue targets;
- Strengthening PFM to raise efficiency in public spending, particularly for capital spending, by improving the Medium-Term Expenditure Framework process;
- Strengthening monetary operations and deepening the financial sector to enhance financial stability and increase intermediation;
- Implementing policies to ensure full pass-through of international market prices on fuel to the domestic market price to safeguard budget resources.

Sierra Leone: Selected Economic Indicators

	2008	2009	2010 Proj	2011 Proj	2012 Proj
	(Annual percentage change, unless				
National account and prices					
GDP at constant prices	5.5	4.0	4.8	5.5	6.0
GDP deflator	11.2	5.7	13.3	9.7	7.6
GDP at market prices	5,828	6,407	7,605	8,798	10,030
(in billions of local currency)					
Consumer prices (end-of-period)	12.2	10.8	12.5	9.5	8.0
Consumer prices (average)	14.8	9.2	15.6	7.6	8.7
External sector					
Terms of trade (deterioration -)	-2.5	-8.3	5.7	4.3	2.8
Exports of goods (US$)	-5.2	3.9	25.9	12.5	11.5
Imports of goods (US$)	24.8	-2.6	14.7	11.9	10.7
Average exchange rate	2,985	3,410	…	…	…
(local currency per U.S. dollar)					
Nominal exchange rate change	-2.2	-26.7	…	…	…
Real effective exchange rate	-11.6	-3.2	…	…	…
Gross international reserves,	4.4	6.4	5.7	5.4	5.1
Money and credit					
Domestic credit to the private sector	56.8	45.4	32.2	18.3	21.2
Base money	10.2	20.6	8.0	15.8	14.0
M2	29.7	29.6	15.2	4.9	14.0
91-day treasury bill rate (in percent)	9.1	14.0	...	...	...
	(Percent of GDP, unless otherwise indicated)				
National accounts					
Gross capital formation	14.8	19.8	21.6	22.5	23.5
Government	6.2	7.1	8.1	8.5	9.0
Private	8.6	12.7	13.5	14.0	14.5
National savings	3.1	11.3	12.7	13.5	14.4
External sector					
Current account balance					
(including official grants)	-11.7	-8.4	-9.0	-9.0	-9.1
(excluding official grants)	-15.6	-13.4	-12.7	-11.6	-11.4
External public debt (including IMF)	31.2	29.7	33.8	33.6	33.1
Central government budget					
Overall balance	-4.7	-3.2	-3.9	-4.7	-3.4
(excluding grants)	-9.2	-11.0	-10.8	-10.6	-10.3
Revenue	11.5	11.7	12.4	13.0	13.7
Grants	4.5	7.8	7.0	5.9	6.9
Total expenditure and net lending	20.7	22.7	23.3	23.6	24.0

Sources: Sierra Leonean authorities; and IMF staff estimates and projections.

Statemet by Samuel Itam, Executive Director
for Sierra Leone
June 4, 2010

Introduction

1. My Sierra Leonean authorities would like to thank staff for the constructive dialogue with the country and for the candor in identifying the policy challenges and presenting options for maintaining macroeconomic stability and reverting to a high and sustainable growth path. My authorities are particularly grateful to the Executive Board and Management for their continued support since the country emerged from a decade-long civil war. While some progress has been accomplished in transitioning from post-conflict reconstruction to the path of sustained economic growth that is anchored on a strong medium-term fiscal framework and prudent macroeconomic policies, program implementation continues to be severely challenged by the relatively low level of domestic revenues and the limited fiscal space for development financing.

2. Against this backdrop, my authorities' medium-term strategy, clearly articulated in the second generation Poverty Reduction Strategy Paper (PRSP-II), the 'Agenda for Change', aims to stimulate private sector-led economic growth through increased investment in infrastructure, while preserving macroeconomic stability. It is in view of the considerable development need and external financing gap that my authorities request the completion of the sixth review of the current ECF arrangement and the Board's approval of a new ECF arrangement.

Performance under the ECF program

3. My authorities have maintained an unwavering commitment to implementing the ECF program since its commencement in May 2006. In spite of the challenging policy environment posed by the succession of global crises – food, fuel, financial and economic – performance in respect of the quantitative criteria has steadily improved. On the structural front, the authorities have been steadfast in pursuing reforms to complement the sound macroeconomic framework and policies through measures to enhance domestic revenue mobilization, strengthen expenditure controls, and mitigate financial sector vulnerabilities.

4. Program implementation as at end-December 2009 was satisfactory as demonstrated by the observance of all quantitative performance criteria, with the exception of the target on domestic primary fiscal balance which was only marginally exceeded. The breach of this criterion however reflects higher development expenditures on infrastructural projects, consistent with the country's medium term strategy outlined in the PRSP II. In furtherance of the structural agenda, the Goods and Services Tax (GST) was introduced on January 1st, 2010 and has so far exhibited a better-than-anticipated performance. In addition, the authorities proceeded with the recruitment of budget officers to ensure effective monitoring of expenditures and service delivery at the government ministries, departments, and agencies (MDAs) in line with the Integrated Public Financial Management Reform Program. We note, however, that the delays in implementing some structural measures have been due to the lack

of an enabling environment, including the legal and regulatory framework. To this end, the Fund is providing technical assistance on the review of the requisite banking legislations to support the establishment of new off-site surveillance guidelines for banks, while the National Revenue Authority (NRA) is now working towards establishing the Domestic Tax Department (DTD) and integrating the GST administration within the Large Taxpayer Office (LTO). These unfinished structural measures have been frontloaded in the proposed ECF program, and my authorities have expressed a strong commitment to their timely implementation.

Recent economic developments

5. Aided by a strong medium-term fiscal framework and sound macroeconomic policies, economic performance during 2006 – 2008 was impressive, with real GDP growth averaging 6.4 percent. The authorities' relative success in restraining monetary growth has helped to contain inflation, while there was a gradual build up of gross international reserves to 4.5 months of import coverage over the period. Economic performance was however undermined by the emergence of the global food and fuel crises, culminating in the widening of the external current account deficit.

6. Macroeconomic performance in 2009 was weakened by the global economic and financial crisis resulting in a deceleration of real GDP growth to 4.0 percent, compared with 5.5 percent the preceding year. The significant contraction in mineral output and exports and the decline in inward remittances initiated a marked depreciation in the exchange rate of the Leone. The easing of monetary policy towards the close of 2009 to support investment in infrastructural development resulted in monetary expansion, which, coupled with the sharp depreciation of the exchange rate, heightened inflationary pressures. Consequently, inflation reverted to double digits by the last quarter of 2009, after remaining at single digit for most of the year.

Outlook and policies for 2010 and the medium term

7. As global demand gradually recovers and domestic production and export pick up, the authorities' policy focus has shifted once again towards the consolidation of macroeconomic stability with high and sustainable economic growth. To this end, real GDP growth is expected to increase to 4.8 percent in 2010. The outlook for inflation in 2010 will be challenged by the price shock from the introduction of the GST in January 2010, the potential increase in the pump price of petroleum products with the planned elimination of subsidies, and the lingering effect of the monetary expansion in 2009. However, the Bank of Sierra Leone was successful in tightening liquidity during the first quarter of 2010, with contraction in reserve money, thereby offsetting some of the inflationary pressures.

8. My authorities medium-term agenda will be defined by priorities set out in the PRSP II that emphasize increased allocation of resources to the development of basic infrastructure and the efficient provision of social services, within a stable macroeconomic environment. In this regard, they seek to gradually increase real output growth to at least 6 percent by 2012 as investment in basic infrastructure, including electricity and agricultural productivity, are realized. The medium-term outlook envisages single digit inflation, declining from 12.5 percent in 2010 to 8 percent in 2012. With the pressure on the exchange rate subsiding, the country is expected to maintain a comfortable gross foreign reserves position above 5 months of import coverage in 2010 and over the medium term.

Fiscal policy

9. My authorities are committed to maintaining fiscal sustainability over the medium term by pursuing prudent fiscal management, while creating much needed fiscal space to support their development priorities. Cognizant of the fiscal challenges, my authorities will seek to intensify effort at mobilizing domestic revenues, by harnessing efficiency gains in tax collection from the introduction of the goods and services tax (GST) and the installation of the ASYCUDA++ software at the Customs Department. In addition, they undertake to implement the tax and customs acts while minimizing revenue leakages, including discretionary tax exemptions. To maximize receipts from the mining sector, my authorities will ensure that all new contracts are in compliance with the terms of the Mines and Minerals Act of 2009. These measures are expected to raise additional revenues of 1.1 percent of GDP by 2012.

10. On expenditures, my authorities will focus on containing non-statutory recurrent outlays. To achieve this, they intend to further strengthen public expenditure management by proceeding with the process of rolling out the integrated financial management information system (IFMIS) to all government ministries, departments and agencies (MDAs).

11. As highlighted by staff, the medium-term expenditure outlook is subject to severe upside risks from the recently launched free health care initiative (FHCI) which seeks to provide universal coverage of health care at the point of access for pregnant women, lactating mothers, and under-five children. It should however be noted that Sierra Leone has consistently ranked at the bottom of the United Nations' Human Development Index, recording one of the highest infant and maternal mortality rates in the world, and, as such, the launching of this initiative provides a bold but measured attempt by the authorities to reverse the deplorable health situation and put the country on track to achieving the Millennium Development Goals (MDGs). My authorities acknowledge the immeasurable support from their development partners, especially the UK Department for International Development (DFID), in providing initial financing for the program. While the authorities are determined to work towards creating the necessary fiscal space going forward, they solicit the continued support of their development partners to ensure the sustainability of the program.

Monetary and exchange rate policies

12. My authorities are committed to achieving low and stable rate of inflation over the medium term. In this regard, the central bank's monetary policy framework is being revised to enhance the potency of monetary instruments in sterilizing domestic liquidity, and to promote development of the inter-bank market. A benchmark policy rate, to be determined periodically by the Monetary Policy Committee (MPC), is being considered to better signal the direction of monetary policy to the market.

13. My authorities consider that the current flexible exchange rate regime has served the country well, facilitating a smooth adjustment to pressures created by the global financial and economic crisis. Exchange rate flexibility will be maintained over the medium term, with interventions in the foreign exchange market limited to smoothening out market volatility. The foreign exchange auction will nonetheless continue to complement monetary operations in mopping up excess liquidity.

Structural reforms

14. My authorities consider the implementation of far-reaching structural reforms as critical to achieving the medium-term objective of high and sustainable economic growth. To this end, they reiterate their commitment to pursuing timely implementation of the unfinished reform measures that have been frontloaded in the proposed ECF-supported program.

15. In addition, my authorities are seeking to expeditiously implement the country's Financial Sector Development Plan (FSDP) which aims not only at deepening the financial sector and promoting financial intermediation, but also at strengthening the supervisory and legislative framework of the financial system in order to ensure financial stability. With technical assistance from the Fund and other development partners, the Bank of Sierra Leone is in the process of revising key banking legislations, including the Banking Act, the Other Financial Services Act, and Anti-Money Laundering and Countering the Financing of Terrorism Act. The authorities are also committed to operationalizing a credit reference bureau to safeguard the credit portfolio of the banking system.

16. Furthermore, my authorities recognize the need to strengthen public financial management with a view to improving budget credibility and predictability, and enhancing control and transparency of fiscal management. In this regard, they are implementing the recently designed integrated public financial management reform program (IPFMRP) to strengthen macro-fiscal coordination and support improved service delivery. As an important first step, the process of revising the underlying legal and regulatory framework, including the Government Budgeting and Accountability Act (2005) and the Financial Management Regulations (2007) have commenced.

17. Finally, the authorities plan to formulate a comprehensive national debt law and develop a procedures manual to improve public debt management in line with international best practices. The emerging framework for public sector borrowing and debt management is expected to clearly define the procedures and authority required to borrow both domestically and externally, as well as regulate the process for issuing Government guarantees and monitoring contingent liabilities which have in the past posed significant risks to the external debt outlook. Similarly, the authorities are establishing a wide area network among the key debt management institutions and, subsequently, link the Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) into IFMIS.

Conclusion

18. The ECF-supported program has been implemented against the backdrop of a difficult external environment characterized by a succession of global crises. However, the unflinching commitment of the authorities to program implementation has culminated in the steady improvement in performance. As at end-December 2009, all quantitative performance criteria were observed, with the exception of the target on domestic primary fiscal balance, which was slightly breached on account of higher development expenditures. My authorities are nonetheless mindful of the enormous challenge of raising domestic revenues to a significantly higher level to support priority spending.

19. Going forward, my authorities will seek to promote private sector-led economic growth through increased investment in infrastructure and improved service delivery, consistent with the PRSP II. In this regard, the structural agenda outlined under the proposed ECF-supported program will be swiftly pursued to complement the strong medium-term fiscal framework. Given the huge external financing gap and the need for implementing sound macroeconomic policies, my authorities consider the Fund's and other development partners' assistance critical to achieving their development objectives. Against this backdrop, my authorities solicit the Executive Board's support in completing the sixth and final review of the current ECF arrangement and request approval of the new three-year ECF arrangement.