International Monetary Fund

Republic of Congo
and the IMF

Press Release:
IMF Executive Board Completes Third Review Under the ECF Arrangement with the Republic of Congo and Approves US$1.78 Million Disbursement
August 31, 2010

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Republic of Congo: Letter of Intent, and Technical Memorandum of Understanding

May 19, 2010

The following item is a Letter of Intent of the government of Republic of Congo, which describes the policies that Republic of Congo intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Republic of Congo, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

SUPPLEMENTAL LETTER OF INTENT

Brazzaville, May 19, 2010

The Minister of Finance, Budget
and Public Portfolio

To:

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, DC 20431
United States of America

Dear Managing Director:

The Fund's Executive Board completed the second review of Congo's Extended Credit Facility (ECF) arrangement in November 2009 and determined that it had reached the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative in January 2010. The Congolese authorities are grateful for this support and are determined to maintain the momentum of economic reform, to further consolidate macroeconomic stability and accelerate growth to reduce poverty durably. In this regard, we believe the program objectives elaborated in our Memorandum of Economic and Financial Policies of November 2009 remain relevant and achievable. These objectives include an increase in real non-oil GDP growth this year, maintaining a low level of inflation, and continued fiscal adjustment toward long-term sustainability.

The implementation of our Fund-supported program continues to be satisfactory and we observed all the quantitative performance criteria at end-December 2009. Indeed, the target on the basic non-oil primary fiscal balance was observed by a significant margin, despite the adverse (but waning) impact of the global financial crisis. We attribute this strong performance to prudent budget management and the emerging benefits of public financial management and tax and customs administration reforms, and some tax policy changes. While performance on structural areas has been broadly favorable, we did not meet two structural benchmarks. The first unobserved structural benchmark concerns the transfer of oil receipts to the treasury within 45 days. As you know, one of the HIPC completion point triggers entailed aligning oil commercialization with best international practice. In this context, we took on board the recommendations made by the World Bank to integrate within the parent company (SNPC) the subsidiary charged with crude oil commercialization. This operational change resulted in a delay in some cases past the 45 days, but progress is being made in regularizing the payment transfer.

The second benchmark that we did not meet is completion of the strategic study of the oil sector. This study is progressing, although not on the timeline we envisaged earlier, owing to the complexity of certain issues, including the legal terms and conditions of oil contracts and the tax regime. To ensure this study effectively guides policies in this critical sector, we have solicited technical assistance from an international expert to buttress the analysis. The study should be completed by end-September.

For 2010 and beyond, we will continue to monitor our program through quantitative performance criteria, which focus on consolidation of the fiscal position. As envisaged earlier, we will target a basic non-oil primary fiscal deficit of CFAF 638 billion, equivalent to a reduction of about 3 percent of non-oil GDP (Table 1). We propose to strengthen the monitoring of the use of the government's financial resources through a[n indicative target] on net domestic financing of the banking sector to the government (ceiling). HIPC debt relief has led to a significant improvement in the government's external position and we will continue to maintain a prudent external borrowing policy, to preserve external sustainability. Nonetheless, we do have some margin to maneuver and we can now accommodate foreign financing on less concessional terms. Consequently, we propose to reduce the program's grant element on new medium- or long-term external debt to 35 percent, from 50 percent. This would help increase the range of potential projects that we could consider with the assistance of our development partners, without jeopardizing debt sustainability. Indeed, an updated debt sustainability analysis demonstrates that moderate external borrowing on these terms will not lead to a deterioration of the external debt indicators over the medium to long term.

With the help of Fund technical assistance, we are making progress in using a functional classification to enhance the monitoring of poverty-related spending. Once this work is completed, we will adopt an indicative target on such spending, consistent with the framework under the ECF.

In coordination with our CEMAC partners, we continue to place great importance on addressing the weaknesses in the regional central bank (BEAC). The BEAC authorities remain committed to strengthening governance. Initial measures have been taken to safeguard Fund resources. An external audit of all budgetary and accounting processes at BEAC headquarters is ongoing and expected to be completed in the coming months. We remain committed to working with the BEAC to resolve these issues as quickly as possible.

During the implementation of the program, we will consult with Fund staff on the adoption of any measures that may be necessary to achieve its objectives, at the initiative of the government, or whenever the Fund staff requests such a consultation. The government intends to make the contents of this letter and those of the attached Technical Memorandum of Understanding (Attachment I), as well as the staff report accompanying its request for completion of the third review of the program, available to the public and authorizes the Fund to arrange for them to be posted on the Fund's website, subsequent to Executive Board approval of its request.

The fourth review under the ECF arrangement based on performance through end-June 2010 is expected to be completed before end-October 2010.

Sincerely yours,

/s

Gilbert Ondongo
Minister of Finance, Budget, and Public Portfolio

Attachment

Table 1. Republic of Congo: Quantitative Targets, 2009–10
(Billions of CFA francs; cumulative from January; unless otherwise indicated)

	End-Dec. 2009		End-Mar. 2010	End-Jun. 2010	End-Sep. 2010	End-Dec. 2010
	Perf. Criteria	Prel.	Indicative Target	Perf. Criteria	Indicative Target	Perf. Criteria
Quantitative targets						
Basic Non-oil primary fiscal balance (floor)	-637	-614	-181	-363	-500	-638
New medium or long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) [1, 2, 3]	0	0	0	0	0	0
New external debt (including leasing) with an original maturity of less than one year (ceiling) [2]	0	0	0	0	0	0
New oil-collateralized external debt contracted by or on behalf of the central government (ceiling) [2]	0	0	0	0	0	0
New nonconcessional external debt with a maturity of more than 1 year contracted or guaranteed by SNPC (ceiling) [2]	0	0	0	0	0	0
New external arrears on nonreschedulable debt (ceiling) [2]	0	0	0	0	0	0
New domestic arrears [2]	0	0	0	0	0	0
Memorandum items						
Oil revenue	1070	934	516	1,060	1,618	2,187
Non-oil primary revenue	372	373	106	211	317	422
Net domestic financing of the government (ceiling, indicative target)	…	…	-295	-618	-999	-1,352
Pro-poor spending	405	401	125	249	352	455

[1] Excluding rescheduling arrangements and disbursements from the IMF; the minimum grant element is set to 35 percent.

[2] Continuous.

[3] The zero ceiling on nonconcessional external debt does not apply to forthcoming external loans from the European Investment Bank and the Central African States Development Bank, as specified in paragraph 11 of the Technical Memorandum of Understanding.

Table 2. Republic of Congo: Structural Benchmarks under the ECF Arrangement, 2010–11

Measures	Timing/status
Public financial management and domestic revenue mobilization	
Have no recourse to emergency payment and cash advance procedures except in situations stated in the organic budget law.	Continuous
Support implementation of the new procurement code by ensuring that 80 percent of public contracts) having a total value of over CFAF 250 million are open to competitive bidding.	Continuous
Undertake audits to assess the arrears (wages, pensions) and liabilities of public enterprises liquidated or under restructuring. These audits will cover the period 2000-08.	End-June 2010
Governance and natural resource management	
Support implementation of the new oil commercialization action plan by ensuring that oil is marketed in line with the recommendations made by the international consultant, who is advising the state-owned oil enterprise (SNPC) on international best practice. These recommendations will include the introduction of competitive tenders for oil sales.	Continuous
Have an internationally reputable audit firm certify oil revenue quarterly, using the same specifications as for the 2003 certification and with no restrictions on access to the information; and publish the certification reports on the website of the Ministry of Economy, Finance and Budget (www.mefb-cg.org). Also, the government will post on the website not only the audit but for each report, a note addressing comments by the auditors.	Continuous
Repatriate to the Treasury the proceeds of oil shipments commercialized by private companies and SNPC on behalf of the government within 45 days after the actual shipment date, based on actual quantities, prices, and shipment dates.	Continuous
Finalize the strategic study of the oil sector—assisted by Congo's development partners—which will include a critical assessment of the institutions and enterprises, including CORAF.	End-September 2010
Public enterprises	
Ensure regular and timely adjustment of petroleum-product prices in line with the pricing mechanism adopted in May 2009, to avoid the need for budget subsidies or subsidies to the state-owned oil refinery, CORAF.	Quarterly

ATTACHMENT I

Technical Memorandum of Understanding

Brazzaville, May 19, 2010

1. This technical memorandum of understanding (TMU) describes the definitions that are intended to clarify the measurement of the quantitative performance criteria and indicators in Table 1 of the Supplemental Letter of Intent (May 19, 2010) and the Memorandum of Economic and Financial Policies (MEFP, dated November 5, 2009) covering 2008–11. All quantitative performance criteria and indicators will be evaluated in terms of cumulative flows from December 31, 2009. Also, the TMU specifies the periodicity and deadlines for transmission of data to the staff of the IMF for program monitoring purposes.

I. DEFINITIONS AND COMPUTATION

A. Government

2. Unless otherwise indicated, **government** is defined as the central government of the Republic of Congo and does not include local governments, the central bank, and any public entity with autonomous legal personality (i.e., wholly- or partially-owned state enterprises) not currently covered by the government's consolidated financial operations table (tableau des opérations financières de l'Etat—TOFE).

B. Basic Primary Fiscal Balance

3. The scope of the government's **financial operations table** (TOFE) includes the general budget and the special accounts of the Treasury (including the forestry and road funds) and the government debt management agency (Caisse Congolaise d'Amortissement, CCA).

4. The government's **non-oil basic primary fiscal balance** is defined as total non-oil revenue excluding grants and investment income (on the government's accounts in the central and commercial banks), minus total expenditure (including net lending), which is to exclude transfers to Hydro Congo, interest payments on debt, externally-financed capital expenditure, and capital expenditure financed by debt services savings under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative. It is calculated from the budget execution outturn reported every month in the TOFE prepared by the Ministry in charge of finance.

5. The government's **total revenue** is reported in the TOFE on a cash basis. It includes all revenue collected by the Treasury (from tax and customs receipts, oil, services and forestry), whether they result from past, current, or future obligations. Receipts also include those recorded on a gross basis, in special accounts.

6. **Oil revenue** is defined as the government's net proceeds from the sale of oil, including the provision for diversified investments, royalties paid by oil companies, and the government's share of excess and profit oil. It excludes all forms of prepayment and pre-financing. The oil revenue projections take account of the 45 day lag between the date of shipment and the date of receipt of the sale proceeds by the Treasury.

7. **Expenditures** are recorded on a payment order basis**.** They include current expenditure, domestically-financed capital expenditure, foreign-financed capital expenditure, and net lending. Current expenditures include expenditures on wages, goods and services, common charges, interests on debt (domestic and external), transfers and subsidies, and other current expenditures. Subsidies to the state-owned oil refinery, CORAF, are estimated on the basis of the enterprises income statement.

8. Pro-poor spending is defined in the budget on the basis of the functional classification.

C. Net domestic financing of the central government

9. Net domestic financing (NDF) of the central government is defined as the change in the government's net position (claims minus deposits at the BEAC and commercial banks) in the banking system, which is elaborated in the table of Position Nette due Gouvernement table (PNG). NDF also includes the change in the stock of Treasury bills and bonds issued by the Congolese Treasury in CFA francs on the CEMAC regional market, when those securities are established but exclude the change in the outstanding of IMF credits at the BEAC (recours au dredits due FMI) . At end-December 2009, NDF was assessed at -956.29 billion CFAF. For each test date, any adjustment by the BEAC to the data reported by individual commercial banks, on account of their misclassification of government or for other reasons, will be reported to the Fund.

D. Foreign Debt and External Arrears

10. The definition of **government** used for the various external debt indicators includes government, as defined in paragraph 2, public institutions of an administrative nature (*Etablissements Publics Administratifs*), public institutions of a scientific and/or technical nature, public institutions of a professional nature, public institutions of an industrial and/or commercial nature (*Entreprises Publiques d'Intérêt Commercial*), and local governments, with the sole exception of the national oil company (SNPC)—see paragraph 12 below.

11. For the purposes of this memorandum**, debt and concessional loans** are defined as follows:

- As specified in the guidelines adopted by the Executive Board of the IMF,[1] debt will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time 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. 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. 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.

- Loan concessionality is assessed on the basis of the commercial interest reference rates (CIRRs) established by the OECD. A loan is said to be on concessional terms if, on the date of conclusion of the contract, the ratio of the net present value of the loan, calculated on the basis of the reference interest rates, to its nominal value is less than 35 percent (i.e., a grant element of at least 35 percent).[2]

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[1] See Executive Board Decision No. 6230-(79/140) as amended by Decisions Nos. 11096-(95/100) and 12274-(00/85).

[2] See "Staff Guidance Note on Debt Limits in Fund-Supported Programs" http://www.imf.org/external/np/pp/eng/2009/121809.pdf, December 22, 2009.

For debts with a maturity exceeding 15 years, the ten-year reference interest rate published by the OECD is used to calculate the grant element. For shorter maturities, the six-month market reference rate is used.

The concessionality requirement applies not only to the central government, but also covers debt incurred by public enterprises. The sole exception to this concessionality requirement is the projected external loans to the Port Authority of Pointe Noire to support its rehabilitation from the European Investment Bank in an amount up to euro 29 million, and from the Central African States Development Bank in an amount up to euro 9.1 million.

12. The quantitative indicative target with respect to **external debt** apply not only to debt as defined in the above-mentioned guidelines, but also to commitments incurred or guaranteed for which no value has yet been received or on which only partial drawings have been made. However, this does not apply to financing from the IMF or to Treasury bills and bonds issued by the Congolese Treasury in CFA francs on the CEMAC regional market.

13. For **external debt with an initial maturity of less than one year** (a continuous quantitative performance criterion)**,** normal short-term import and export credit are excluded from the scope of the indicator, including the prepayments.

14. The ceiling on any **new nonconcessional external debt with a maturity of more than one year contracted or guaranteed by the SNPC**, with or without government guarantee, will be observed continuously. The SNPC may borrow only to finance investments related to its core activities (research, exploration, production, refining and distribution of oil, construction of a Brazzaville headquarters, creation and strengthening of its database, etc.). In addition, these investments must be included in the SNPC's investment budget approved by its board of directors. The ceiling on debt does not apply to changes in loan accounts with oilfield partners or to loans with maturities of less than one year.

15. The accumulation by the government of **external payment arrears** is the difference between (i) the gross amount of external debt service payments due (principal and interest, including penalty and/or late interest, as appropriate) and (ii) the amount actually paid during the period under consideration. Under the program, the government commits itself to not accumulate external payment arrears on non-reschedulable debt (that is, debt to Paris Club creditors contracted after the cutoff date and debt to multilateral creditors). Non-accumulation of external payment arrears is an indicator to be continuously observed.

E. Oil-Collateralized External Debt and Oil Prepayments

16. Oil-collateralized external debt is external debt which is contracted by giving an interest in oil. Pre-financing is defined as an oil-collateralized loan which is repaid by the sale of the oil in a different calendar year. New pre-financing by or on behalf of the government is strictly prohibited under the program. The refinancing and/or deferral of the existing stock and/or due dates are permitted but should not give rise to an augmentation of the existing stock of oil-collateralized debt.

17. A prepayment is defined as an advance payment by the purchaser of oil on a specific oil shipment. Prepayment-related operations must be repaid within 6 months, but in any case within the calendar year in which they were contracted.

F. Payment Arrears and Domestic Debt

18. Domestic payment arrears of the government are equivalent to the difference over the period under review between the amount of payments authorized and the actual payments made (within 90 days).

II. Information for Program Monitoring

19. The government will submit the following information to the staff of the IMF through its Resident Representative, and within the time period specified below.

A. Oil Sector

20. Regarding the oil sector, the government will submit the following information to IMF staff within four weeks after the end of the month:

- the monthly data on oil production by oil field, production costs, volume exported, export prices, and the operations of the national oil company (SNPC);
- the breakdown concerning the share of crude oil that accrues to the government, by oil field, distinguishing the type of resource to which this share relates (royalties, profit oil, etc.);
- any change in the tax parameters;
- a breakdown of oil prices;
- a monthly detailed list of shipments commercialized by SNPC on behalf of the government, including information on the type of product, the date of loading, the recipient, the number of barrels and the selling price (in US dollars and CFAF) as well as the date of receipt of the sale proceeds by the Treasury; and

- actual and projected quarterly data to determine the required subsidies in the fuel sector, including prices, quantities, and costs.

B. Government Finance

21. Regarding government finance, the government will submit the following information to IMF staff:

- A table on government fiscal operations (TOFE) and its annexes. The annexed tables include (i) the breakdown of oil revenue in value terms with the corresponding notes on computation, (ii) excess oil trends and any bonus payments, (iii) the breakdown of tax and non-tax revenue, and central government expenditure, particularly transfers and common charges; and (iv) a report on the amounts of and rationales for emergency payment and cash advance procedures. The provisional TOFE and its annexes will be reported monthly within four weeks from the end of the month, whereas the final TOFE and its annexes will be reported within six weeks from the end of each month.

- Monthly data on the prices and taxation of petroleum products. These data will include: (i) the price structure in effect during the month; (ii) the details of computation of the price structure, (f.o.b. Mediterranean price) at retail prices, including the border impact prices, taxes, transit costs, economic adjustments, ex-refinery prices (for CORAF and imports), entry distribution prices, margins and fees, transport costs and losses, financing expenses, and insurance; (iii) amounts released for sale; and (iv) a breakdown of the tax revenue from oil products—customs duties and value-added tax—and direct/indirect subsidies incurred by the budget. These data will be reported within four weeks from the end of the month.

- The Treasury balance to monitor expenditures. It will include the amount of commitments, payment orders, and payments, for both current and capital expenditure. It will be produced on a quarterly basis, and submitted to Fund staff no later than four weeks after the end of each quarter.

- Data on implementation of the public investment program, including the breakdown relating to financing sources. If the data on the execution of investments financed with foreign grants and loans are not available on schedule, a linear estimate of execution in comparison with annual forecasts will be used. These data will be reported on a quarterly basis within four weeks from the end of the quarter.

- Complete monthly data on domestic financing of the budget (net bank credit to, and net non-bank credit to the government). These data will be reported monthly within four weeks from the end of the month.

- The table used to monitor the expenditure process will list the amount of commitments, payment orders, and payments, for both operating and capital expenditures. It will be produced on a quarterly basis, and submitted to Fund staff no later than four weeks after the end of the quarter.

- A quarterly table for monitoring poverty reduction expenditures, based on the pro-poor sectors defined in the poverty reduction strategy paper—basic health care and education; infrastructure and rural integration; water and electricity; disarmament, demobilization and reintegration; social protection, and agriculture). The quarterly tables will be submitted within four weeks of the end of the quarter.

- A monthly table of prepayments, which will also indicate the nature of the expenditures (current transfers, investment, etc.) and the justification for the need to use the prepayment option.

C. Monetary Sector

22. The government will submit on a monthly basis, within four weeks of the end of the month, the following preliminary information:

- the consolidated balance sheet of the monetary institutions, the central bank survey, and the commercial banks survey;

- the integrated monetary survey;

- the table of lending and deposit rates; and

- the usual banking supervision indicators for banks and non-bank financial institutions, where necessary.

23. The final data for the integrated monetary survey will be transmitted within six weeks of the end of the month.

D. Balance of Payments

24. The government will submit the following information to IMF staff:

- any revised balance of payments data (including services, private transfers, official transfers, and transactions for the capital and financial account) as soon as the data are revised; and

- foreign trade statistics (volume and price) prepared by the national statistics agency within three months of the end of the reporting month.

E. Debt

25. The government will submit the following to the staff of the IMF within four weeks of the end of the month:

- data on the stock, accumulation, and payment of domestic arrears;
- data on the stock, accumulation, and payment of external payment arrears;
- a breakdown of estimated domestic and external public debt service, service due, and actual payments, including breakdowns of principal and interest and by creditor;
- the list and amounts of new external debt incurred or guaranteed by the government, including detailed information on the terms and conditions (currency, interest rate, grace period, and maturity) stated in the original agreement; and
- actual disbursements of foreign financial assistance (project and non-project), including new borrowing and any external debt relief granted by foreign creditors (CCA tables).

F. Real Sector

26. The government will submit the following to the staff of the IMF:

- monthly itemized consumer price indices, within four weeks of the end of the month;
- any revision of the national accounts; and
- any other indicators and statistical data used to track overall economic developments, including information on activity in the forestry sector and wood-processing industry, as well as the short-term economic bulletins prepared monthly.

G. Structural Reforms and Other Data

27. The government will submit the following information to the IMF staff:

- a monthly detailed table concerning the implementation of structural measures under the program;
- any study or official report on the economy of the Republic of Congo, within two weeks of its publication; and

- any decision, order, law, decree, ordinance, or circular having economic or financial implications for the program, within two weeks from the time it is published, or, at the latest, from its entry into force.