Letter of Intent

MINISTRY OF FINANCE

BANK OF SIERRA LEONE

GOVERNMENT OF SIERRA LEONE

June 10, 2019

Madame Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431 U.S.A.

Dear Madame Lagarde:

1. **On behalf of the Government of Sierra Leone, we hereby request the IMF Executive Board to complete the first review of the Extended Credit Facility (ECF) arrangement and to approve the disbursement of the second tranche of the loan** based on partial implementation of end-December 2018 performance criteria and progress on the implementation of structural benchmarks.

2. **As documented in the attached Memorandum of Economic and Financial Policies (MEFP), economic performance was stable but subdued in 2018**. Ongoing challenges in the mining sector, together with a slowdown in the nonmining sector due to the impact of government procurement arrears contributed. However, domestic revenue increased significantly thanks to recent reforms and slightly exceeded the program target, while donor budget support fell short of program. Given this shortfall in budget support and constraints on domestic bank financing, we held back recurrent expenditures and took a cautious approach to implementing the capital budget. As a result, we were able to achieve a lower than programmed deficit.

3. **Notwithstanding these challenges, performance is broadly in line with the ECF approved by the Executive Board in November 2018**. All quantitative targets were met, except the end-December 2018 performance criterion on Net Domestic Asset (NDA) of the BSL and the end-March 2019 indicative target on poverty-related spending. Several structural reforms—the forensic audit of the BSL, developing a strategic plan for the two state-owned banks, and a strategy for clearing domestic arrears—have proved to be more complex and dependent on expert advice than anticipated, causing us to miss three structural benchmarks. There was no new accumulation of non-concessional external public debt and no public sector arrears to sovereigns or to external private creditors. We are committed to enhancing program monitoring to prevent a re-occurrence of

missed targets, and hereby request the IMF Executive Board to approve a waiver for the non-observance of the program target on NDA of BSL. To ensure we continue to advance our structural reform agenda, we have reformulated the approach to focus on measured, incremental steps, and we have agreed three new structural benchmarks accordingly. We also agreed another structural benchmark on amending the NRA Act, which will support the program's revenue mobilization goals.

4. The accompanying MEFP lays out specific government policies for 2019 and beyond that will strengthen program implementation, enabling us to meet program objectives by the end of the ECF program in 2022. We remain firmly committed to implementing measures to increase domestic revenue mobilization, improve expenditure management to contain fiscal risks, and stabilize public debt, while implementing a strategy for the clearance of arrears. Further reforms of the National Revenue Authority, Public Investment Management framework, and expanded roll out of both the Treasury Single Account (TSA) and Integrated Financial Management Information System (IFMIS) would support the effectiveness of fiscal policy. The BSL also remains committed to bringing inflation down to its medium-term target by maintaining a tight monetary policy and refraining from intervening in the foreign exchange market. Our financial sector reforms would strengthen the BSL's independence and governance, improve financial stability, and deepen financial intermediation. Finally, following the release of our new medium-term *National Development Plan—Education for Development*, we have brought a sharper focus to promoting inclusive growth and expanding the social safety net, alongside the need to improve the business environment and promote economic diversification.

5. The Government believes that the policies contained in the attached MEFP are adequate to achieve the objectives of our program, but we will take any further measures that may become appropriate for this purpose. Sierra Leone will consult the IMF on the adoption of these measures, and in advance of revisions to the policies contained in the MEFP, in accordance with Fund policies on such consultations. Sierra Leone will provide the Fund with any information that may be necessary for monitoring the implementation of the measures and the achievement of program objectives.

6. The government consents to make public the content of the IMF staff report, including this letter, the attached MEFP and TMU, and the World Bank's Assessment of our National Development Plan. It therefore authorizes the IMF to publish these documents on its website once the IMF Executive Board approves the completion of the first review under the ECF.

Very truly yours,

_______________/s/_______________	_______________/s/_______________
Jacob J. Saffa	**Kelfala M. Kallon**
Minister of Finance	Governor of Bank of Sierra Leone

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

Attachment I. Memorandum of Economic and Financial Policies

INTRODUCTION

1. **This Memorandum of Economic and Financial Policies (MEFP) supplements the one dated November 14, 2018**. It reviews economic developments and reports on performance under Sierra Leone's economic and financial program supported by the International Monetary Fund (IMF) under the Extended Credit Facility (ECF) arrangement 2018–22. It outlines key policies and reform measures for the remainder of 2019 and the medium-term. These policies aim to foster macroeconomic stability, improve competitiveness, promote sustainable broad-based inclusive economic growth and poverty reduction over the medium-term.

2. **Since the ECF was approved, the macroeconomic situation has been stable but remains challenging**. The government continues to implement bold policies to stabilize the macroeconomy, tackle structural impediments, boost economic activities, plug revenue leakages, tightening expenditure controls to minimize inefficiencies, and expand social programs. Against the background of slow economic activity in late 2018, government boosted consumers' disposable income by allowing falling global oil prices to pass through to pump prices, resulting in a 15 percent decrease in the pump price of gasoline.

3. **Economic development, anti-corruption and poverty reduction are key pillars of our government's economic reform agenda**. Our newly launched National Development Plan (NDP), *Education for Development* (2019–23) is a holistic economic and social agenda, focused on reducing poverty and building "a diversified, resilient and green economy". The agenda reflects our commitment to address corruption, and improve transparency and accountability in managing public resources. The strategy includes programs on governance and accountability; human capital development; empowering women, children, adolescents and persons with disabilities; economic diversification, mitigating vulnerabilities and building resilience.

RECENT ECONOMIC DEVELOPMENTS

4. **Weak performance in both mining and nonmining sectors contributed to a slowdown in real GDP growth to 3.5 percent in 2018 from 3.8 percent in 2017**. In the mining economy, rutile production fell short of projection due mainly to industrial actions, while the two iron ore mines remained shut throughout 2018. In the nonmining economy, the impact of government spending arrears in the first three quarters of the year, together with less than full implementation of the 2018 budget contributed to the slow down. Consumer prices remained high, reaching a peak of 19.3 percent in September 2018, before moderating to 17.5 percent in March 2019. The pressure on prices reflected a combination of factors including food price developments, the pass through of exchange rate depreciation, and the impact of the liberalizing domestic fuel prices.

5. **Improved revenue performance and lower than-budgeted expenditure narrowed the overall fiscal deficit (excluding grants) to 7.9 percent of GDP in 2018 from 11.3 percent in 2017**. Domestic revenues increased to Le 4.4 trillion (13.7 percent of GDP) from 12.3 percent of GDP in 2017, and exceeded the program target, mainly due to policy and administrative reforms

including operationalizing Treasury Single Account, liberalizing domestic fuel prices, rationalizing duty and tax waivers, and implementing the ECOWAS Common External Tariff. Notwithstanding, budget implementation was challenging due to uneven liquidity in the banking system, which contributed to less than programmed borrowing. Given the reduction in most recurrent expenditures, together with scaling back of domestic capital spending (pending the financial and technical audits), fiscal operations resulted in a lower deficit than programmed.

6. **Broad money grew slower than programed while the BSL directly accommodated the budgetary financing needs**. Despite higher-than-programed credit to the private sector, substantially lower overall credit to the government resulted in less-than-programmed broad money growth. To support money market operations, the Bank of Sierra Leone (BSL) engaged in secondary market operations to provide liquidity to the banking system. In addition, the BSL provided bridge financing to Government in lieu of the delayed World Bank Budget Support, which contributed to higher-than-programmed net domestic assets of the BSL. The BSL had initially addressed the buildup in price pressures by gradually increasing the Monetary Policy Rate (MPR) from 15 percent in December 2017 to 16.5 percent in July 2018. However, BSL refrained from increasing the MPR in the second half of the year on the back of slowing growth momentum, rollover risk in the domestic debt market, and tight liquidity conditions in the banks.

7. **The banking system remained stable, with banks largely profitable and adequately capitalized**. The capital adequacy ratio for the industry was 38.4 percent and all banks met the minimum 15 percent as at end-December 2018, though there is a wide variation among banks. The asset base and total deposits of the banking system continue to increase, and gross loans and advances increased by 18.2 percent by end 2018, with largest proportion (more than half) going to commerce, finance and construction. However, borrowing costs remain persistently high. Aggregate non-performing loans decreased to 12.7 percent in December 2018 from 14.6 percent in December 2017 due mainly to the write-off of bad loans in the two state-owned banks under enhanced BSL supervision.

8. **The current account deficit improved to 13.8 percent of GDP in 2018 from 14.5 percent in 2017, partly on account of subdued imports**, as well as improvements in services, income and current transfers. Notwithstanding improvements in the current account, weak performance of export, delayed donor inflows and speculative behavior caused the Leone to depreciate against major international currencies. On a year-on-year basis, the Leone vis-à-vis the United States Dollar depreciated by 11.9 percent in 2018 relative to 2017. These pressures intensified in early 2019. To prevent disorderly depreciation of the Leone, the BSL stepped up its foreign exchange interventions. As a result, official foreign exchange reserves declined to US$502.80 million as at end-December 2018 from US$533.8 million at end-December 2017.

9. **The end-20018 stock of public debt is estimated at US$2.24 billion, nearing 60 percent of GDP in 2018**. Much of the 18.6 percent increase compared to 2017 reflects higher domestic debt, limiting the recourse to financing through arrears. The total stock of domestic debt increased to Le 5.66 trillion from Le 4.56 trillion at end 2017 mainly due to issuance of new securities. This, together with a slight increase in interest rates, saw domestic interest payments rise to Le 865.8 billion compared to Le 535.28 billion. External debt also increased with, new disbursements to finance infrastructure projects. External debt stood at US$1.57 billion up from US$1.51 billion at

end 2017, as multilateral debt (around three-quarters of external debt) grew from US$1.13 billion at end 2017 to US$1.2 billion and bilateral debt edged up from US$177.61 million to US$185.82 million at end 2018. However, commercial debt decreased from US$195.05 million to US$188.5 million.

PROGRAM PERFORMANCE

10. Program performance is broadly on track. All but one end-2018 quantitative performance criteria, the NDA of BSL, were met. BSL's bridge loan to the government, together with interventions in the foreign exchange market, contributed to the higher-than-programmed NDA. The bridge loan was repaid in the first quarter of 2019 and we plan to enhance our program monitoring to avoid a recurrence. All end-December 2018 and end-March 2019 indicative targets were met, except the floor on poverty-related spending in March. There was no new accumulation of non-concessional external public debt and no external payment arrears of the public sector.

11. Structural reforms are underway, but the complexity of some issues has made progress in those areas slower than programmed. The audit of the BSL's 2017 financial statements was completed in February 2019. The BSL is committed to a joint audit, between an international audit firm and a local firm, of the 2018 financial statements and plans to publish the statements upon completion of the audit. Developing a strategic plan for the two state-owned banks has proved more complex than anticipated, including the need for an updated baseline from the 2016 E&Y diagnostic study. We have made good progress toward the audit and validation of arrears supported by UK DFID and IMF technical assistance (TA), as well as a complementary arrears stocktaking by the Audit Service of Sierra Leone (ASSL). However, further work needs to be done to bring together these efforts and elaborate details and identify financing for the plan to clear these arrears. The benchmark on the forensic audit of foreign exchange transactions between the BSL and quasi-government agencies (MDAs) was missed as the scope of the audit was broader than initially expected and we now expect to receive the final audit report in late May/early June.

GOVERNMENT ECONOMIC PROGRAM FOR 2019 AND BEYOND

A. Program Objectives

12. Our policy objectives remain as enunciated at the time of ECF program request. Our goals are to preserve macroeconomic stability, accelerate the implementation of structural reforms, promote inclusive growth and poverty reduction through the implementation of our NDP. In this regard, the Government will continue to pursue policies aimed at ensuring fiscal and debt sustainability, financial sector stability, transparency and accountability in the use of public resources, improved business environment and strengthened social protection systems.

B. Medium-Term Macroeconomic Outlook

13. The economic outlook for 2019 and the medium term is broadly balanced. The economy is projected to grow by 5.1 percent in 2019, and to average 4.8 percent during the program. The resumption of iron ore mining at the Marampa Mines (which produces higher grade iron ore), normal agricultural activity, and public construction activities, alongside improvements in the business environment (due to the intensified fight against corruption and broad ranging structural reforms) are expected to support growth prospects. Inflation is projected to fall to 14 percent by end-December 2019 and return to single digits by 2021 on the back of projected stability in the exchange rate as exports increase in the medium-term, increase in domestic food production and the proactive stance of monetary policy. The overall fiscal deficit (excluding grants) is projected to decline steadily, from 7.4 percent of GDP in 2019, to 5.3 percent in 2022, driven by expenditure reforms and stronger revenue mobilization. Stronger foreign inflows, including direct investment, from the expected expansion operations in rutile and iron ore mines would finance the still high but declining current account deficit. Rising international reserves over the program period will strengthen external stability and the country's resilience to shocks.

PROGRAM POLICIES

A. Fiscal Policy

14. The tight fiscal stance of 2018 assisted us to mitigate some near-term macro-fiscal risks. Going forward, much remains to be done including paying down arrears, and creating the fiscal space necessary to boost infrastructure and social spending to achieve our goal of inclusive growth. A tight fiscal stance remains necessary given our large public debt and recent classification as high risk of debt distress. Moreover, our reliance on foreign and domestic financing call for even more cautious assumptions about the financing of the program.

15. The fiscal path for the rest of the program entails a significant deficit reduction, sufficient to ensure the debt to GDP ratio begins to turn down by the end of the program. In this regard, the fiscal adjustment will continue to be guided by the key fiscal anchors—debt sustainability and domestic financing. We target a gradual decline in the overall deficit (excluding grants), averaging nearly ¾ of a percentage point per year over the medium term, slowing the pace of debt accumulation. This, together with efforts to seek more grants, will limit our recourse to net external debt financing of the deficit, averaging less than 1½ percent of GDP per year during the program period. Fiscal adjustment will facilitate a steady decline in domestic bank financing to 2.1 percent of GDP in 2022. However, the repayment of Fund budget support (extended during the Ebola epidemic and on-lent from the BSL), scheduled to begin 2020, will curtail the available amount of net domestic financing to 1.4 percent by the end of the program. The escalation in total debt service payments, including repayments of Fund budget support, will average 25 percent of domestic revenue during 2020–23. This will limit our ability to raise priority spending, adversely affect the implementation of our NDP and slowing our economic recovery.

Structural Reforms to Improve Fiscal Policy Transmission

16. The fiscal stance will be supported by strong implementation of ongoing structural reforms. Effective revenue generation and expenditure management processes are essential for macroeconomic stability, the strategic and efficient allocation of resources, effective delivery of vital goods and services, and strengthening of transparency and accountability. The Government has adopted a comprehensive *Public Financial Management (PFM) Strategy 2018–21* building on the previous PFM strategy, 2014–17. The new strategy aims to deepen reforms in all PFM-related areas, including strategic policy and budget planning; public investment management, Fiscal Risk and Debt management, budget execution, revenue administration, local Government finance and PFM oversight and public accountability. Implementation of the PFM strategy is ongoing and being monitored through a new governance framework that includes a PFM Steering Committee, a PFM technical Committee, and Thematic Working Groups.

Domestic Revenue Mobilization

17. Implementing the revenue enhancing measures in the previous MEFP improved tax administration and broadened the tax base, contributing to strong revenue performance in 2018. Measures include (i) liberalizing fuel pricing; (ii) streamlining the process for granting duty and tax waivers; (iii) enforcing upfront payment of fuel taxes and duties; (iv) implementing the ECOWAS Common External Tariff; (v) broadening the coverage of the Treasury Single Account (TSA); (vii) revising of fees/rates levied by Ministries, Departments and Agencies (MDAs) including fisheries licenses; (viii) data-matching and special tax audits; (ix) strict enforcement of tax legislation; and (x) migrating from ASYCUDA++ to ASYCUDA World. To sustain this improved performance and achieve the targeted revenue to GDP ratio of 20 percent by 2023, the Government will deepen the reforms in these specific areas:

Tax Policy

i. **Limit exemptions and waivers, and improve efficiency in the operation of the duty waiver regime**, by developing a policy on duty and tax waivers using the *Tax Incentive Handbook*; enacting legislation that provides comprehensive guidance on exemptions and waivers; and adopting an automated waiver system through the ASYCUDA World establishment, to fully track and monitor duty and tax waivers utilization.

ii. **Continue to implement the liberalized formula for petroleum pricing, and continue to use it to determine fuel prices (continuous structural benchmark)**. For transparency, we are considering publishing the fuel price template on a regular basis, rather than only when price changes.

iii. **Implement the new *Extractive Industry Revenue Act (2018)* (EIRA)** to all new mining and petroleum projects and mining Lease Agreements that come for renewal. We also plan to draft the EIRA Regulations to support the implementation of the Act in 2019, and the IMF is providing capacity building on fiscal modeling of the extractive sector to the Ministry of Finance, National Revenue Authority (NRA), National Minerals Agency and the Petroleum Directorate. This TA will support implementation of the EIRA including mineral revenue forecasting, evaluation of mining and petroleum projects using the EIRA fiscal regime, risk assessment and tax administration for the extractive sector.

Tax Administration

i. **Prepare a revised NRA Act that draws on TA**, with a view to modernizing the NRA’s governance and organizational structure. The new law would establish clear governance and accountabilities, including responsibility within government and focusing the powers of the NRA Board on oversight. We plan to submit the draft law to the IMF for review no later than end-September (**structural benchmark**), before submitting it to Cabinet by end-October, and subsequently Parliament.

ii. **Automate tax processes and procedures** with the installation of the Integrated Tax Administration System (ITAS) and Electronic Cash Registers commencing in the second half of 2019; develop a migration plan for ITAS, including data cleansing and ascertaining ledgers; and roll out the banking module to government revenue transit banks before ITAS is delivered.

iii. **Improve revenue collection by TSA agencies**.

iv. **Carry-out the re-registration of businesses** to verify the existing tax payers and register new tax payers to expand the tax base.

v. **Intensify the ongoing data matching exercise and leverage the results** to support a risk-based approach to strengthening field audit.

vi. **Intensify monitoring and enforcement, including through stricter enforcement of tax legislation**, and reviewing and implementing a robust taxpayer education strategy to support enforcement and compliance.

vii. **Reduce leakages through enhancement of NRA integrity mechanisms** underpinned by the establishment of an internal affairs unit at the NRA.

viii. **Enhance intelligence and investigations**, including the Tax Inspectors Without Borders (TIWB) Audit supported program.

Expenditure Management

18. Implementing expenditure management reforms contributed to the lower than budgeted spending in 2018, allowing us to mitigate some of the fiscal risks. Going forward, expenditure management will focus on further improving efficiency in public expenditure management, while implementing priorities articulated in our NDP. Accordingly, human capital development including the Free Quality Education Programme, Health and Social Protection will remain our top priority. Other priorities include developing infrastructure to diversify and improve the competitiveness of the economy to promote sustainable economic growth and job creation. To create the fiscal space for implementing these priorities, the Government will embark on reforms to maintain the wage bill at sustainable levels, improve public procurement, curtail wasteful recurrent spending and extra-budgetary expenditures and improve the efficiency of domestic capital expenditures.

Wage Reforms

19. The Government remains committed to achieving a wage bill at not more than 6 percent of GDP. Substantial gains were recorded from the biometric verification exercise of the past year, and more than 10 percent of public sector workers including staff of sub-vented agencies were either not matched or not verified. We are optimistic that by the end of the ECF program, the following key reforms would ensure a transparent, accountable and manageable wage bill:

i. **Institutional regular monthly Payroll Quality Assurance** to check for discrepancies in the running of the Government payroll. This will include checks for significant changes in pay, invalid National Social Security Insurance Trust (NASSIT) numbers and invalid BBANs (Basic Bank Account Numbers).

ii. **Remove retiring employees from the payroll in a timely manner**, using a new payroll system to analyze employees' Dates of Birth embedded in their NASSIT numbers.

iii. **Strengthen the Payroll Oversight Committee** to generate comprehensive and timely payroll reports on monthly basis for effective monitoring of the Government payroll.

iv. **Establish a Wages and Compensation Commission** that is empowered by law as the sole agency to determine pay and compensation across the public service. The Commission will address the pay inequities and multiple pensions observed in the public service while initiating and pursuing reforms relating to public sector wages. In preparation for the establishment, a Consultant has been appointed, draft bill produced, and consultative workshops being held across the country with key stakeholders.

v. **Integrate the payroll of the tertiary institutions into the centralized Government payroll** beginning in 2019 to pave the way for the regular monitoring of movements in their respective payrolls. While this reclassification of spending is expected to increase somewhat the ratio of wages to GDP, we remain committed to bringing the ratio to the targeted 6 percent within the program period.

Public Procurement Reforms

20. Improved public procurement processes were instrumental to achieving lower than budgeted expenditure in 2018. Going forward, some of the measures to be implemented as part of expenditure control measures include:

i. **Publish the revised Public Procurement Regulations and update the Public Procurement Manual** in line with the Public Procurement (Amendment) Act 2016. The Regulations are awaiting Parliamentary approval, while the *Manual* will be updated in line with the new procurement regulations.

ii. **Regularly publish Price Norms**. The Government will continue the quarterly publication of Price Norms to guide procurement contracts; and ensure value for money in Government procurement activities.

iii. **Introduce an electronic public procurement system**. The Directorate of Science Technology and Innovation had developed a strategy to guide the implementation of an *e-Government Procurement (e-GP)* system. Steps are under way to select an agency to implement the electronic system.

iv. **Develop a national strategy for public procurement**. The 5-year Strategy provides a comprehensive roadmap for procurement reforms and will enable the Government of Sierra Leone to initiate sequential and sustained measures for strengthening the procurement system. The strategy will enhance the effectiveness and coherence of reform efforts.

v. **Reconstitute the Independent Procurement Review Panel (IPRP)**. The IPRP will serve as an independent grievance redressal mechanism available to bidders who wish to challenge public procurement proceedings as a result of perceived breaches of standard procedures in compliance with the public procurement legal and regulatory instruments.

Goods and Services Expenditure Management

21. Strengthening expenditure commitment control systems in the goods and services categories is essential to reduce the accumulation of arrears. To this end, the Ministry of Finance is introducing a range of reforms to assist in realizing this objective, including:

i. **Expanding the coverage of the Integrated Financial Management System (IFMIS)** to the remaining 30 MDAs by end-May, bringing the total covered to 56. The Accountant-General's Department will continue to enforce the requirement to generate Local Purchase Orders through IFMIS for goods and services expenditure. Upgrading IFMIS to Version 7 will further help in enhancing the expenditure commitment control system through automating the processing of Public Expenditure Tracking System (PETS) forms. IFMIS will be further modified to include a functionality to accommodate multi-year contracts to facilitate the processing of payments as well to ascertain existing commitments of MDAs for the medium term at any point in time. This will provide information that will assist to reduce the accumulation of arrears.

ii. **Establishing active Budget Committees in all MDAs**. The committees will prepare budgets, projections, and analyze how best to use their quarterly budget allocations. To date there are 20 active committees, with a goal to have committees established and active in all 56 MDAs by 2021.

iii. **Strictly adhering to the provisions in the PFM Act** (2016) relating to the control of extra-budgetary expenditures.

Capital Expenditure Management

22. Improving the efficiency of managing capital expenditure is essential to mitigating fiscal risks. Key reforms of capital expenditure planned for the coming year include:

i. **Ensuring to the extent possible that domestically-funded projects are negotiated in local currency to limit the exchange rate risk**, strengthen project appraisals for new projects, review compensations for domestically funded projects and strengthen the monitoring and evaluation mechanism for all capital projects.

ii. **Undertaking a Public Investment Management Assessment (PIMA)** to identify strengths and weaknesses in public investment management across all phases of public investment:

planning, allocation, and implementation. We have requested that the IMF conduct a PIMA and hope it will begin later this year.

iii. **Adopting a National Public Investment Policy** to improve the effective planning and efficient execution of investment activities and inform capital expenditure rationalization. The policy will be informed by the findings of the Fund-led PIMA. Given the importance of ensuring consistency with our debt sustainability objectives and our program commitments on external borrowing, we plan to consult the Fund on externally-funded, flagship infrastructure projects.

Treasury Single Account (TSA)

23. Implementation of the TSA was an important contributor to increase strong revenue performance in 2018. Total revenue collected by the original 6 TSA agencies amounted to just over 6 percent of total revenue in 2018, while Ministry of Finance disbursed 37 percent of the receipts to the TSA agencies to meet their operational needs. To further deepen the impact of TSA implementation on total revenue, Government will:

i. **Continue to broaden the coverage of the TSA**. In addition to the six MDAs added in 2018, another five agencies were added to the TSA operations in early 2019 following the enactment of the Finance Act of 2019.

ii. **Print and disseminate the *TSA Operations Manual***, and having agreed an MOU with the BSL, complete the automation process between the Accountant-General's Department and the BSL.

iii. **Commence implementing phase II of the TSA** to include sub-vented agencies, semi-autonomous agencies and project accounts, which will further expand the TSA's scope.

State-owned Enterprises and Fiscal Risks

24. In line with commitments made in the last MEFP, the government has implemented new policies aimed at strengthening SOE oversight the past year. The risk entailed in the operations of the SOEs needs to be managed, analyzed, and quantified so as to be able to proactively respond to potential shocks to the achievement of fiscal objectives. These include:

i. **Establishing a new *Fiscal Risk Management and Fiduciary Oversight of State-Owned Enterprises* (SOEs) Division in the Ministry of Finance**. The division is charged with monitoring the financial performance of SOEs and managing annual fiscal risks. The Division has initially focused on SOEs that have the greatest potential to cause a significant fiscal burden for the Government, such as the Electricity Distribution and Supply Authority (EDSA). EDSA is now recording substantial revenue and in February 2019, it was able to meet all its obligations, including operational expenses, without recourse to Government subsidy.

ii. **Undertaking data reconciliation of interagency arrears** amongst SOEs, with the aim of ascertaining the net arrears and developing a strategy for the clearance of these arrears.

iii. **Publishing a quarterly report on arrears stock at MDAs and SOEs**, and the annual financial statements of SOEs, beginning with EDSA, Electricity Generation and Transmission Company (EGTC) and Guma Valley Water Company (GVWC).

iv. **Developing a strategy, jointly with the National Commission for Privatization** (NCP), to transform and limit the Sierra Leone Telecommunication Company (SIERRATEL) fiscal exposure.

v. **Developing a strategy for on the governance structure and ownership of Sierra Leone Cables Limited** (SALCAB) in line with the Financial Agreement signed between the Government and the World Bank in 2010.

vi. **Going forward, other reforms to be implemented include**: eliminating the backlog of SOEs' audited financial reports; classifying SOEs according to GFSM2014; completing the cross-SOEs arrears clearance strategy; preparing internal quarterly fiscal risk reports to inform the management of the Ministry of Finance: preparing a consolidated SOE financial performance report; and developing a fiscal risk register.

Debt Management and Domestic Arrears Clearance Strategy

Debt Management

25. Achieving the fiscal adjustment path that underpins the ECF program will be essential to putting debt on a sustainable path. Sierra Leone's high level of external debt, and weak growth, exports and revenue put the attainment of the macroeconomic objectives of the program at risk. Domestic debt has almost doubled over the past 4–5 years, at much higher cost and with a term profile susceptible to rollover risks. The high stock of implicit debt, in the form of domestic arrears owed to suppliers, compounds the problem. Therefore, consistent with commitments made in the last MEFP, we have commenced implementing key reforms aimed at efficiently managing and reducing the debt stock. These include:

i. **Sustaining fiscal consolidation drive** with a view to improving the domestic primary balance over the program period and slowing the accumulation of domestic debt.

ii. **Prioritizing grants and highly concessional loans** to finance the budget and especially infrastructure projects.

iii. **Exploring non-debt creating financing models** such as Public-Private Partnerships supported by a thorough analysis of the potential fiscal risks and without recourse to government guarantees.

iv. **Preparing a Medium-Term Debt Management Strategy** to guide debt management practices. The strategy will address key issues in both domestic, external and implicit debt, as well as the interlinkages with BSL balance sheet vulnerabilities. An action plan is being developed following a recent IMF TA mission. The strategy will analyze the scope for, and relative merit of, issuing a range of maturities of government securities, with the aim of shorter-term securities (i.e., 3, 6, 12 months) mainly for cash management and short-term budget financing needs, and gradually extending maturities to longer term bonds for long-term financing needs such as infrastructure projects. In doing so, the strategy will aim to reduce both financing costs and rollover risks. The strategy will be complemented by regular Debt Sustainability Analyses prepared ahead of the annual budget cycle and intended to provide early warning signals on debt levels and the risks of debt distress that can inform debt management policy.

Clearance of Domestic Arrears

26. The Government has made good progress toward clarifying the magnitude of domestic procurement arrears. To date, the Government has undertaken two main steps:

i. **Beginning in 2018, it estimated total arrears and future payment obligations at Le 10.7 trillion**. This amount includes: (i) arrears comprising crystalized obligations (unpaid checks) of Le 1.03 trillion and unprocessed vouchers for works completed of Le 418.9 billion; and (ii) outstanding balances on contracts entered into by MDAs for goods and services and infrastructure projects exceeding Le 9 trillion.

ii. **In June 2018, Government engaged the services of the Audit Services Sierra Leone** (ASSL) to verify this stock of arrears. Claims totaling Le11.59 trillion, (including those submitted later by MDAs) were submitted to the Audit Service for verification.

27. The results of these audit warrant further work to reconcile the different arrears figures. First, we note that ASSL's report includes future payment obligations, which have not fallen into arrears. Second, the outstanding unpaid checks as of December 2018 of about Le 1,156 billion, are not included in the verified claims of ASSL due to timing difference. Third, we need to ensure that any double-counting is eliminated between the amounts verified by ASSL and the outstanding stock of unpaid checks. Finally, arrears to five contractors captured as verified claims in ASSL's report or as part of crystalized obligations have been liquidated by MoF, and should no longer be included in the stock of arrears. These issues will be addressed in months ahead.

28. Given the magnitude of fiscal burden and risks to sustainability, we plan to complete the arrears stocktaking and prepare a clearance plan in a prompt manner. The burden of arrears is a major factor affecting economic activity in the nonmining economy, and a prolonged resolution will only delay economic recovery. We recognize that, once we have a final estimate, this could result in a significant upward revision of the arrears included in our macroeconomic framework. In the absence of donor funding and/or a rescheduling plan that does not undermine debt sustainability, this could necessitate a faster fiscal adjustment path. To ensure we have a clear picture of the situation, we will complete the arrears stocktaking and obtain a comprehensive arrears figure, in line with IMF TA recommendations, by end-August (**structural benchmark**).

29. The next critical step will be to finalize details of our plans to clear this stock arrears. Building on the draft *Strategy on the Treatment of Domestic Suppliers and Contractors Arrears* prepared earlier this year, we will move to making the plan more concrete and operational. By the end of September, we will outline details of the medium-term framework with a clear resource envelope, and specify the prioritization of, and mechanisms for repaying and or rescheduling those arrears. These details will then inform the 2020 budget and the next DSA. Subject to determining the resource envelope and allocations in the medium-term budget, we are currently considering a range of options, drawing on IMF TA, with the aim of containing the costs and impact on debt sustainability. These options include:

i. **Outright cash payments for small claims in the MDAs category** at a level to be determined. These claims are many but smaller in amounts, and outright cash payments will allow suppliers, mostly SMEs to be liquid to re-finance their operations.

ii. **Apply revenue windfall or grant resources**. The Government is in discussions with the World Bank to significantly scale up its next annual budget support, and will also engage other development partners such as DfID, with a view to directing grant resources toward the clearance of these arrears.

iii. **Securitization of some claims**. As upfront cash payment is a limited option due to the likely large amount of the final arrears figure and the challenging fiscal situation, securitization may be unavoidable. Mindful of the debt sustainability implications and what debt the market can bear (in line with recent IMF TA), possible options under securitization include:

   a. **Issuing medium to long-term securities to settle arrears**. This could trigger some costs in the form of interest payments demanded by suppliers/contractors to compensate for the extended time of settling the claims.

   b. **Issuing treasury bills to raise resources and clear some of the verified arrears** to allow suppliers and contractors settle obligations with the banking systems.

30. Several measures contained in the Government's PFM Strategy will assist to avoid the buildup of new arrears. These include the Issuance of Quarterly allocations on the basis of trends in revenue performance, improving fiduciary management in MDAs through the deployment of Budget Officers and Internal Audit Staff; improved cash management, strengthening commitment controls through the IFMIS, improved debt management operations; and enhanced oversight of the state-owned enterprises and local councils to minimize the incidence of contingent liabilities.

B. Monetary, Exchange Rate and Financial Sector Policies

Monetary and Exchange Rate Policies

31. Monetary policy will continue to focus on bringing inflation down to single digits over the course of the program (in line with the medium-term macroeconomic outlook set out in paragraph 13). Given current inflationary pressures, the BSL will continue to implement a tight monetary policy stance to bring inflation down to 14 percent by end 2019. Pending the development of effective price-based monetary policy, the BSL will continue to use monetary aggregates as the operating target and, over time, will work to strengthen the role of indirect instruments, supported by IMF TA.

32. BSL will continue to improve its monetary policy operations to facilitate transition to a forward-looking framework. The BSL's capacity for more rigorous analysis including developing high frequency data, liquidity forecasting, and medium-term forecasting has benefited from IMF TA. The BSL will therefore continue to review its existing liquidity operations framework so as to improve the monetary transmission mechanism. While progress will take time, the BSL will also aim to enhance its liquidity management via the development of the repo market. Finally, the BSL is also working on producing a monetary policy report to enhance the transparency of monetary policy conduct.

33. The objective of building external reserves during the program remains paramount. A key objective of the ECF is to build and maintain a reserve coverage ratio of around 3½ months of imports during the program period. In this regard, we aim to stop routine foreign exchange market sales, which contributed to a lower pace of reserve accumulation in the past year. Rather, BSL will participate in the foreign exchange market only for liquidity management purposes and to smooth out short-term fluctuations in the exchange rate. In addition, we will commence foreign exchange purchase auctions as soon as possible to be able to meet the reserve target for the review period. Purchase operations will be appropriately timed to factor in exchange market developments. We are also developing new foreign exchange guidelines for exporters and non-governmental organizations, and will consult the IMF before finalizing them.

34. We will continue to strengthen the BSL's governance and operational practices by addressing shortcomings in internal controls and maintaining adequate oversight. An international audit firm was contracted to conduct an audit of the foreign exchange transactions between the BSL and quasi government agencies (MDAs) during July 2015—June 2018, in line with IMF safeguards assessment's recommendations. The firm issued an interim report after completing a first phase of the exercise, indicating significant lapses in internal controls and processes, and we expect to receive the final forensic audit report in early June. With that in mind, we plan the following steps moving forward:

i. **Publish the final audit report** within two months of receiving it and after tabling it in Parliament as constitutionally required;

ii. **Identify potential quick wins to be implemented immediately** such as: (i) strengthening the BSL's internal controls to limit access to cash and vault areas, and ensure adherence to policies and procedures; and (ii) the Ministry of Finance issuing a circular to stop MDAs from depositing foreign exchange into commercial banks instead of the BSL; and

iii. **Building on these initial efforts, develop and adopt a remedial action plan** to address the findings of the forensic audit within two months of receiving the final audit report (**structural benchmark for end-August 2019**).

Financial Sector Policies

35. Our objective to deepen financial intermediation to *foster higher, broader-based, and more inclusive growth* remains as stated at the approval of the current ECF program. The BSL is committed to safeguarding financial stability by strengthening the supervisory framework and managing risks within the banking system. We are also committed to strengthening the financial soundness of banks, while exerting stronger oversight over their cross-border relationships.

36. Work is progressing on various initiatives aimed at promoting financial inclusion. The planned introduction of a National Switch for Sierra Leone is progressing with World Bank assistance, and the process of contracting an operator is at an advanced stage. Once installed, the National Switch system will improve payments systems, and facilitate revenue collection (through the introduction of electronic cash registers for GST) and financial inclusion. As part of the policies to deepen financial system, the Government (in cooperation with the UN Capital Development Fund, the UNDP, and the non-profit, Kiva) is planning to introduce a new national identity system, which the BSL will use as a platform to enable the development of unique financial histories for citizens. The new Credit Reference Bureau (CRB)-Unique Identifier will upgrade the existing Credit Bureau platform and significantly reduce manual interventions in the processing of credit reports. Implementation of the project is expected to commence in 2020.

37. The BSL continues to safeguard financial stability through strengthening the regulatory and supervisory framework, and appropriately assessing risks within the banking system and other financial institutions. Over the past year, we have been transitioning to risk-based supervision (RBS) and are focusing our supervisory resources on the banking institutions that pose the greatest risk. In 2018, the BSL conducted full scope RBS examination on seven banks, as well as a targeted AML/CFT examination for two banks. The BSL has already conducted four RBS examinations in 2019. The institution also published its first Financial System Stability Report earlier this year. While the ownership dispute of FiBank in late 2018 resulted in temporary disruption in operations, the BSL's subsequent focus on enhanced supervision helped to stabilize the situation.

38. Work continues to advance on enhancing the legal framework underpinning BSL's regulatory functions.

i. **The *Bank of Sierra Leone (Amendment) Act 2019* and the *Banking Act (Amendment) 2019* were passed by Parliament in late May**. Following their earlier submission to Parliament last year, these laws were amended in particular to include a clause giving the BSL oversight of Islamic banking activities. Having now been passed by Parliament they should soon receive Presidential assent. Together, these new laws will improve the legal framework for the financial sector.

ii. **A new *Borrowers and Lenders Act* was also passed by Parliament in late May**. The law is intended to broaden the scope of the Collateral Registry to include the registration of immovable assets (one stop shop) and also enable individuals and non-incorporated entities who are not licensed and supervised by the Bank of Sierra Leone to be able to register their security interest.

iii. **A *Deposit Insurance Fund Bill* is currently being drafted with the help of the U.S. Treasury Department**. Other activities relating to the introduction of deposit insurance system include: development of a roadmap; modeling of the fund size; sensitization of banking industry and workshops with various stakeholders.

39. Efforts to enhance compliance with global Anti Money Laundering/Combating Finance of Terrorism (AML/CFT) standards will assist in resuming correspondent banking relations. The BSL completed a Technical Compliance Questionnaire supplied by GIABA, the ECOWAS region FATF-style institution. The questionnaire is part of the mutual evaluation of Sierra Leone's AML/CFT regime coming up in July. In December, BSL signed an MoU with FIU to strengthen collaboration, cooperation and information sharing. To improve the compliance of banks with global standards, the BSL rolled out the Risk-Based Approach Supervisory tool for AML/CFT compliance. It is also partnering with the Sierra Leone Association of Commercial Bank (SLACB) to facilitate the process for the formation of a forum of National Compliance Officers for Commercial Banks. Also, the AML/CFT Amendment Act was passed by Parliament in late May.

The Two State-Owned Banks

40. The immediate fiscal risks posed by the two state-owned banks have eased while under enhanced supervisory oversight by BSL. The banks reported aggregate risk weighted capital adequacy ratio of 68 percent, nonperforming loans of 44 percent and return on assets of 17 percent at end-December 2018. Nonperforming loans have eased, but at 44 percent remain higher than industry average. The Government recently replaced the oversight committee of the banks with normal Boards of Directors.

41. However, given the systemic importance of these banks, the government remains committed to putting the banks on a firmer commercial footing and minimizing the risk of undue influence. Our goal is to ensure these banks are able to deliver efficient banking services that support intermediation, financial inclusion and responsible lending to the private sector, thereby contributing to overall financial sector development. While we had hoped to have in place a strategic plan for these banks by end-March, our initial assessment revealed a more complex situation and need for more detailed assessment of progress since the 2016 E&Y Diagnostic Study. We judged that the situation warrants external expert advice to correctly assess the situation and advance this work. At this stage, we envisage a phased approach that will:

i. **complete an updated Diagnostic Study of the two state-owned banks** (**structural benchmark for end-September**) to assess developments since the 2016 diagnostic and set out a common understanding of the situation as a baseline for next steps. We have requested World Bank support and are in the process of agreeing a terms of reference; and

ii. **based on the diagnostic study, take decisions about the intended function, business model and governance framework** by March/April 2020, including stronger internal controls, and a new business model that protects them against political influence, and durably limits the fiscal risks. It will however be important to secure technical support to effectively move this work forward; and

iii. **maintain the BSL's enhanced supervision and directives of no lending to Politically Exposed Persons**, subject to developing a timetable for transitioning back to standard supervisory oversight in line with the implementation of the new governance framework and business model.

C. Inclusive Growth and Social Protection

42. Poverty reduction and the need to provide protection for vulnerable segments of the population remain key objectives of the ECF program. After the civil war, the country made some progress on poverty reduction, but Ebola Virus Disease (EVD) epidemic of 2014–15 eroded some of the gains. Furthermore, there are emerging challenges associated with climate change, including flooding, which is severely impacting on the livelihood of the poor and vulnerable. As a result, the Government has decided to revamp its social protection agenda.

43. Inclusive growth and poverty reduction are front and center in our recently launched comprehensive reform agenda. Launched in early March, the new NDP aims to ensure a "*united, peaceful, progressive and happy nation where the people have access to jobs, food, and education and health services and there is equal justice and equal opportunity for all*". Reforms focus on addressing corruption and investing in human capital. Human capital development has been identified as the main pathway to sustainably transforming our economy and lifting more people out of extreme poverty leading to inclusive growth. The human development interventions identified in the NDP are the main channels through which we expect to deliver inclusive growth and social protection.

44. In the meantime, we will continue to provide additional support to the most vulnerable segments of our population, and make progressive efforts to augment funding of social protection activities. In 2019, Le 13.5 billion was allocated from the recurrent budget to the social protection sector for implementing pro-poor programs, including cash transfers, and Le 33.2 billion from the domestic capital budget was allocated to meet counterpart contributions for various social protection programs funded by development partners. Going forward, the Government is committed to:

i. **Expanding the coverage of ongoing cash transfer programs** being implemented by NaCSA;

ii. **Creating targeted employment schemes** (e.g., cash-for-work and food-for-work programmes) for youth, women, and others, especially the most vulnerable of these groups, through public–private partnerships and development partners.

iii. **Ensuring the successful implementation of activities** funded by the Post Ebola Recovery Social Investment Fund in the Ministry of Social Welfare, Gender and Children's Affairs;

iv. **Supporting informal savings schemes** and other community savings and insurance schemes with welfare provision;

v. **Implementing policy and legislative reforms** to address inequality, such as laws pertaining to wages and social security benefits; and

vi. **Developing a National Health Policy**, with a view to establishing a National Health Insurance Scheme.

We will continue to work with the World Bank and other partners to identify additional policies that could be implemented to build on the social protection measures in the current program.

D. Business Environment and Economic Diversification

45. Sierra Leone currently ranks 163 out of 190 in the 2019 World Bank *Ease of Doing Business* Ranking, a decline relative to 148th in 2018. Significant improvements were made however in several areas, including the Ease of Starting Business, for which Sierra Leone ranked 55 out of 190, above some middle-income countries in the region. The recent migration to the ASYCUDA World system for the speedy clearance of goods at the Queen Elizabeth II Quay and new legal and regulatory reforms, relating to protecting investors against expropriation and the free transfer of funds, are expected to further ease the business environment.

46. Diversification of the economy is one of the key goals of our NDP. The Government's commitments to new investments in agriculture, fisheries, tourism, manufacturing and the services sectors was articulated in the economic diversification cluster of the NDP. To turn this commitment into reality, the Government supported by the World Bank is in the process of initiating an Economic Diversification Study. In addition, the World Bank has also committed US$30 million to a project that will focus on the pathways for diversifying the country's economy by facilitating investments in the tourism sector; promoting continued business environment reforms; and supporting the growth of SMEs and entrepreneurship, including direct and indirect support to companies and investments.

E. Strengthening Statistics

47. Efforts to strengthen the governance and improve effectiveness of the national statistical agency are yielding fruit. In the past year, reforms initiated by Statistics Sierra Leone's (SSL's) new leadership have been instrumental to attracting donor support from World Bank (who withdrew funding in 2017), the Bill and Melinda Gates Foundation, UNFPA, and others. With improved governance and financial management, both the coverage and quality of data have improved. The coverage of statistical information has expanded to various areas including: (i) Social Safety Nets; (ii) National Civil Registration; (iii) Rental Census to support NRA's revenue mobilization; (iv) completion of the Sierra Leone Integrated Household Survey to support poverty analysis; (v) launching the multiple indicator cluster survey report; and (vi) undertaking a Business Establishment Survey to better support economic policy decision making and help rebase GDP. Going forward, SSL will continue to:

i. **Strengthen collaboration with, and seek additional funding** from global development partners.

ii. **Successfully partner with organizations across the country** to bring better information about Sierra Leone, promoting wider coverage and dissemination of national statistics.

iii. **Elevate Sierra Leone as a leader among low-and middle-income countries** in ensuring full transparency of data and in using data to ensure achievements targeting the SDGs. This will help Sierra Leone collaborate with countries across the Global South and North, and help sustain our development path.

iv. **Strengthen capacity at SSL** and expand technical expertise to support the collection of essential routine data about Sierra Leone, including by launching new initiatives and completing others to collect better data and strengthen development across Sierra Leone.

PROGRAM MONITORING

48. **The program will be monitored on a semi-annual basis, through quantitative targets and structural benchmarks**. Quantitative targets for end-June and end-December 2019 are performance criteria. Those for end-September 2019 and end-March 2020 are indicative targets. The second review of the program will be completed on or after December 1, 2019, and the third review on or after June 1, 2020.

Table 1. Sierra Leone: Quantitative Performance Criteria and Indicative Targets, 2018–20

(Within-year cumulative change – starting from June for 2018, and from January for 2019 and 2020; Le billions, unless otherwise indicated)

	2018					2019									2020
	Jun.	Dec.				Mar. IT				Jun. PC	Sept.		Dec.		Mar.
	Stock	Prog.	Adj. Prog.	Prel.	Status 4/	Prog.	Adj. Prog.	Prel.	Status 4/	Prog. 5/	IT	CR No. 18/371	PC	CR No. 18/371	IT
Performance criteria															
Net domestic bank credit to the central government (ceiling) 1/	5171	823	1104	533	Met	407	352	271	Met	812	791	1155	1085	1357	175
Unadjusted target (ceiling)			823				407								
Adjustment for the shortfall (excess) in external budget support			175				45								
Adjustment for the excess(shortfall) in unpaid checks and other outstanding payments			106				-100								
Net domestic assets of the BSL (ceiling)	858	404	617	670	Not met	223	303	-124	Met	341	522	458	634	576	15
Unadjusted target (ceiling)			404				223								
Adjustment for the shortfall (excess) in external budget support			175				45								
Adjustment for exchange rate depreciation (appreciation)			38				34								
Gross international reserves of the BSL, US$ millions (floor)	474	7	-21	10	Met	-20	-21	-11	Met	-27	-6	-33	17	14	-6
Unadjusted target (floor)			7				-20								
Adjustment for the shortfall (excess) in external budget support			-40				-5								
Adjustment for the shortfall (excess) in the US$ value of IMF disbursement			0				0								
Adjustment for the increase (decrease) in BSL short-term foreign currency liabilities			13				4								
New concessional external debt with original maturity of one year or more contracted or guaranteed by the public sector, US $ millions (ceiling)	...	80		35	Met	100		42	Met	100	100	100	100	100	100
New non-concessional external debt contracted or guaranteed by the public sector, US$ million (ceiling) 2/	...	0		0	Met	0		0	Met	0	0	0	0	0	0
Outstanding stock of external debt with maturities of less than one year contracted or guaranteed by the public sector (ceiling) 2/	...	0		0	Met	0		0	Met	0	0	0	0	0	0
External payment arrears of the public sector (ceiling) 2/	...	0		0	Met	0		0	Met	0	0	0	0	0	0
Indicative targets															
Total domestic government revenue (floor)	...	2356		2430	Met	1224		1358	Met	2549	3797	3866	5302	5350	1485
Poverty-related spending (floor) 3/	...	275		749	Met	293		196	Not met	634	1016	1027	1495	1467	403
Domestic primary balance (floor)	...	-282		-45	Met	-98		254	Met	-208	-171	-306	-247	-264	-58
Memorandum items:															
External budgetary assistance (in $ million)	...	67.0		27.5		5.0		0.0		13	61	24	85	41	30
Exchange rate (Leones/US$)															
Program	7741	8743				9040				8999	9280	9635	9539	9932	9815
Actual	7741			8396				8676							

1/ Includes IMF budget support-related SDR on-lending from the Central Bank to the Government.

2/ These apply on a continuous basis.

3/ Poverty-related spending is defined in paragraph 22 of the TMU.

4/ Preliminary status

5/ As set at the time of program approval on November 30, 2018.

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Table 2. Sierra Leone: Structural Benchmarks		
STRUCTURAL BENCHMARKS	**TIMING**	**STATUS**
Benchmarks for First Review		
Complete the audit of BSL's 2017 financial statements	January 31, 2019	Met
Publish the final report of the forensic audit of foreign exchange transactions between the BSL and MDAs during July 2015–June 2018 and adopt a remedial action plan to address findings.	May 31, 2019	Not met (see new benchmarks)
Develop a strategic plan for the two state-owned banks including a timetable for putting in place an independent governance framework for the banks that protects them against political influence, and thereby durably limits their fiscal contingency risks.	March 31, 2019	Not met (see new benchmarks)
Continue to use the automatic fuel price indexation mechanism to set fuel price determination	Continuous	Met
Adopt a plan for dealing with the outstanding stock of unpaid obligations to domestic suppliers containing: (1) a comprehensive stock-taking, transparent verification, and prioritization of arrears; (2) measures to prevent new arrears; (3) making allocations for clearance of arrears in the medium-term budget framework; and (4) plans to rationalize the balance sheet of the BSL.	March 31, 2019	Not met (see new benchmarks)
Proposed Benchmarks for Second Review		
Adopt a remedial action plan to address the findings of the forensic audit report.	August 31, 2019	
Complete the stocktaking of payment arrears to domestic suppliers to determine a comprehensive arrears figure, drawing on IMF technical assistance recommendations.	August 31, 2019	
Prepare draft amendments to the NRA Act, drawing on technical assistance recommendations (from the IMF and the UK DfID), and submit to Fund staff for review (to be done prior to submitting to the Cabinet).	September 30, 2019	
Update the 2016 diagnostic study of the two state-owned banks, with support from the World Bank.	September 30, 2019	
Continue to use the automatic fuel price indexation mechanism to set fuel price determination	Continuous	

Attachment II. Technical Memorandum of Understanding

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 (ITs) will be evaluated in terms of cumulative flows from the beginning of the period.

2. **Program exchange rates**.[1] For the purpose of the program, foreign currency denominated values for 2019 will be converted into Sierra Leonean currency (leone) using a program exchange rate of Le 8396.05/US$ and cross rates as of December 2018.[2]

Sierra Leone Program Exchange Rate for ECF Arrangement
Cross Rates as of end-December 2018

Currency	Currency Units per SDR	Leones Per currency unit	US dollars Per currency unit
US dollars	1.39	8,396.05	1.00
British Pound Sterling	1.10	10,659.19	1.27
Japanese Yen	154.14	75.76	0.01
Euro	1.21	9,616.83	1.15
SDR	1.00	11,677.14	1.39

QUANTITATIVE PERFORMANCE CRITERIA

3. **Quantitative performance criteria are proposed for June 30, 2019, and December 31, 2019 with respect to**:

- net domestic bank credit to the central government (NCG) (**ceiling**);
- net domestic assets (NDA) of the Bank of Sierra Leone (BSL) (**ceiling**);
- gross international reserves (GIR) of the BSL (**floor**);
- New concessional external debt with original maturity one year or more contracted or guaranteed by the public sector, US$ millions (**ceiling**);

[1]The source of the cross-exchange rates is International Financial Statistics.

[2]For calculating program targets for 2019, all end-December 2018 stock variables will be based on the program exchange rate of Le 8396.05/US$. The program exchange rates for test dates are specified in Table 1 of the Memorandum of Economic and Financial Policies (MEFP).

- New non-concessional external debt contracted or guaranteed by the public sector, US$ million (**continuous ceiling**);

- Outstanding stock of external debt with maturities of less than one year contracted or guaranteed by the public sector (**continuous ceiling**); and

- External payment arrears of the public sector (**continuous ceiling**).

4. The program sets indicative targets for September 30, 2019, and March 31, 2020 with respect to:

- Total domestic government revenue (**floor**)

- Domestic primary balance (**floor**)

- Poverty related expenditure (**floor**)

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

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

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

b. the net position of the government with the BSL, including: (a) treasury bills and bonds, excluding holdings of special bonds provided by government to cover BSL losses and to increase its capital; (b) ways and means; (c) any bonds issued in the conversion of ways and means into debt; and (d) any other type of direct credit from the BSL to the government, including the special on-lending arrangements relating to budget support as approved under the 2018–22 ECF arrangement; less (a) central government deposits; and (b) any debt relief received, notably HIPC, MDRI and relief deposits, as well as debt relief under the CCR Trust.

6. Adjustment clauses. The ceiling on changes in NCG will be adjusted (a) upward by the leone value of the shortfall in external budgetary assistance[3]—the upward adjustment will be capped at the equivalent of US$20 million; (b) a downward (upward) adjustment by the increase (decline) in the value of the cumulative net flow of unpaid checks and other outstanding payments (or known as 'crystalized obligations') (relative to the end-December 2018 stock of Le 1,156 billion);

[3]External budgetary assistance is defined as budget grants and loans, excluding HIPC assistance. The amounts are specified in Section D.

(c) a downward (upward) adjustment by the excess (shortfall) in leone value of net issues of government securities to non-bank private sector.[4]

7. 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.

a. **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 state-owned enterprises are excluded from this definition of central government.

B. Net Domestic Assets of the BSL

8. Definition. Net domestic assets (NDA) of the BSL are defined as the end-period stock of 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), deposits of commercial banks with the BSL and the BSL liabilities to other private sector entities. Net foreign assets of the BSL are defined as gross foreign exchange reserves minus gross foreign liabilities (defined below):

a. **BSL's Gross foreign exchange reserves** are defined as the sum of:

- the BSL's holdings of monetary gold (excluding amounts pledged as collateral);
- holdings of Special Drawing Rights (SDRs), including the August 28, 2009 General allocation and the September 9, 2009 Special allocation;
- BSL's holdings of convertible currencies in cash or in nonresident financial institutions (deposits, securities, or other financial instruments).

b. **BSL's gross foreign exchange reserves** exclude:

- pledged, or any encumbered reserve assets, including but not limited to reserve assets used as collateral or guarantees for third-party external liabilities;
- deposits with Crown Agents and other correspondent banks rated below BBB; and
- precious metals other than gold, assets in nonconvertible currencies and illiquid foreign assets.

[4]Taken together, clauses (b) and (c) would imply that a reduction in the stock of unpaid checks from cash budget resources would increase the NCG ceiling by the same amount, but that a reduction through securitization would not.

c. **BSL's gross foreign exchange liabilities** are defined as:

- the total outstanding liabilities of the BSL to the IMF excluding those arising from the August 28, 2009 SDR general allocation and the September 9, 2009 SDR special allocation; and debt relief from the Catastrophe Containment and Relief (CCR) Trust granted in 2015;

- convertible currency liabilities of the BSL to nonresidents with an original maturity of up to and including one year; excluding foreign liability to China of Le 35 billion relating to a legacy clearing account for a previous Bilateral Trade Agreement;[5]

- commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options), including 2017–18 foreign exchange swap arrangements with commercial banks;

- balance on zero coupon bonds issued by BSL to Securiport LLC on behalf of the government.

9. Adjustment clauses. The ceiling on changes in NDA of the BSL will be adjusted upward (downward) by the leone value of the shortfall (excess) in the external budgetary assistance—the upward adjustment will be capped at the equivalent of US$20 million, and by exchange rate depreciation (appreciation).

C. Gross International Reserves of the BSL

10. Definition. Unless otherwise noted, gross international reserves (GIR) of the BSL will be calculated as reserve assets of the BSL. Reserve assets are defined in 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. Specifically, GIR-BSL excludes 2017–18 foreign exchange swap arrangements with commercial banks.

11. Adjustment clauses. The floor on the change in gross international foreign exchange reserves will be adjusted (a) downward (upward) by U.S. dollars equivalent cumulative shortfall (excess) in programmed external budgetary assistance; (b) downward (upward) for any cumulative 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).

[5]The authorities have confirmed that this BTA is no longer operational.

D. Assumptions on External Budgetary Assistance

12. The programed external budgetary assistance for the calculation of NCG, NDA, and GIR targets will amount, on a cumulative basis, from January 1, 2019 to:

End-March 2019	USD 0 million
End-June 2019	USD 13 million
End-September 2019	USD 61 million
End-December 2019	USD 85 million

The programed external budgetary assistance will amount, on a cumulative basis, from January 1, 2020 to end-March 2020 to USD 30 million.

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

13. New external debt is defined as all forms of new external debt with original maturity of one year or more contracted or guaranteed by the public sector based on the residency of the creditor. The external debt definition applies not only to debt as defined in the Guidelines on Public Debt Conditionality in Fund Arrangements (Decision No. 15688-(14/107), December 5, 2014, Point 8 but also to commitments contracted or guaranteed for which value has not been received. For the purposes of this PC, external debt is defined on the basis of the residency of the creditor. The "public sector" is defined in paragraph 19.

14. For program purposes, the debt is deemed to have been contracted when it is signed by the government of Sierra Leone and ratified by Parliament. Excluded from this PC are disbursements from the IMF and those debts subject to rescheduling. The government will report any planned external borrowing and its terms to Fund staff before external debt is contracted or guaranteed by the government. The ceiling on new external debt will be applied on a continuous basis from September 1, 2018.

15. For program purposes, a debt is concessional if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the net present value (NPV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The NPV of debt at the time of its signing date of an underlying loan agreement is calculated by discounting the future stream of payments of debt service due on this debt. The discount rate used for this purpose is 5 percent.

F. New Non-Concessional External Debt Contracted or Guaranteed by the Public Sector

16. Nonconcessional external debt is defined as external debt (defined in paragraph 13) on terms that do not meet the definition in paragraph 15. External debt and its concessionality will be reported by the Debt Management Division of the Ministry of Finance and will be measured in U.S. dollars at current exchange rates.

17. For loans carrying a variable interest rate in the form of a benchmark interest rate plus a fixed spread, the PV of the loan would be calculated using a program reference rate plus the fixed spread (in basis points) specified in the loan contract. The program reference rate for the six-month USD LIBOR is 3.34 percent and will remain fixed for the duration of the program. The spread of six-month Euro LIBOR over six-month USD LIBOR is -250 basis points. The spread of six-month JPY LIBOR over six-month USD LIBOR is -300 basis points. The spread of six-month GBP LIBOR over six-month USD LIBOR is -100 basis points. For interest rates on currencies other than Euro, JPY, and GDP, the spread over six-month USD LIBOR is -200 basis points. Where the variable rate is linked to a benchmark interest rate other than the six-month USD LIBOR, a spread reflecting the difference between the benchmark rate and the six-month USD LIBOR (rounded to the nearest 50 bps) will be added. This PC will apply on a continuous basis.

G. Outstanding Stock of Short-term External Debt with Maturities of Less Than One Year Contracted or Guaranteed by the Public Sector

18. 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. 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 paragraph 19. This PC will apply on a continuous basis.

H. External Payment Arrears of the Public Sector

19. Definition. External payment arrears of the public sector are defined to include all debt-service obligations (interest and principal) arising from loans contracted or guaranteed by the public sector. For the purposes of this PC, the public sector comprises the central government, regional government, state-owned enterprises, as listed in Annex 7 of the 2019 budget documents, and the BSL. The non-accumulation of external arrears is a continuous performance criterion during the program period. For the purposes of this performance criterion, external arrears are obligations that have not been paid on due dates (taking into account the contractual grace periods, if any). Excluded from this PC are those debts subject to rescheduling or restructuring or are under litigation. This PC will apply on a continuous basis.

QUANTITATIVE INDICATIVE TARGET

A. Domestic Revenue of Central Government

20. 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. Domestic Primary Balance

21. Definition. Central Government Revenue less expenditures and net lending adjusted for interest payments and foreign financed capital spending.

C. Poverty Related Expenditure

22. Definition. For program monitoring purposes, poverty-related expenditures are defined as the total current expenditures of the following ministries and institutions: Higher and Secondary Education, Health and Sanitation, the Health Service Commission, Social Welfare, Youth, Agriculture, Fisheries, Transport and Communications, Energy, Sierra Leone Electricity and Water Regulatory Commission, Water, Correctional Service, National Fire Authority, Local Councils, the National HIV and AIDS Commission, Anti-Corruption Commission, Statistics Sierra Leone, and the National Commission for Social Action; and capital expenditure for the Ministry of Works, Energy, Sierra Leone Electricity and Water Regulatory Commission, Water, Health and Sanitation, the Health Service Commission, Agriculture, Fisheries, Local Councils, and the National Commission for Social Action.

D. Program Monitoring

23. 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 I. Implementation of the Public Debt Limits in Fund-Supported Programs with Respect to External Debt

The term "debt" has the meaning set forth in point No. 8a of the Guidelines on Public Debt Conditionality in Fund Arrangements adopted on June 30, 2015, which reads as follows:
"(a) For the purpose of these guidelines, 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 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. For the purpose of these guidelines, 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 in this paragraph, 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."

Attachment A. Summary of Data Reporting 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	Daily	COB + 2 days
	BSL monitoring sheet of treasury bills and bonds holdings	Weekly	COB + 1 day
	Borrowing and lending interest rates	Monthly	End of month + 6 weeks
	Results of foreign exchange and Treasury Bills auctions	Weekly	End of week + 1 days
	Stocks of government securities	Monthly	End of month
	Banking supervision ratios	Quarterly	End of quarter + 4 weeks

Type of Data	Tables	Frequency	Reporting Deadline
Monetary and financial data	Gross official foreign reserves	Weekly	End of week + 1 week
	Foreign exchange cash flow table	Monthly	End of month + 3 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
	Report on the stock of debt outstanding, and loan agreements under discussion	Quarterly	End of month + 3 months
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