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10:00 a.m., June 28, 2019

**1. Sierra Leone—First Review Under the Extended Credit Facility Arrangement, Request for a Waiver of Nonobservance of Performance Criterion, and Financing Assurances Review**

Documents: EBS/19/54

Staff: Ongley, AFR; Fletcher, SPR

Length: 41 minutes

## Executive Board Attendance

T. Zhang, Acting Chair

### Executive Directors    Alternate Executive Directors

D. Mahlinza (AE)

H. Razafindramanana (AF)

J. Corvalan (AG), Temporary

N. Heo (AP)

K. Florestal (BR), Temporary

P. Sun (CC)

A. Arevalo Arroyo (CE), Temporary

A. McKiernan (CO)

O. Stradal (EC), Temporary

A. Castets (FF)

K. Merk (GR)

P. Dhillon (IN), Temporary

M. Psalidopoulos (IT)

T. Ozaki (JA), Temporary

S. Alavi (MD), Temporary

W. Abdelati (MI), Temporary

H. Etkes (NE), Temporary

J. Sigurgeirsson (NO)

P. Snisorenko (RU), Temporary

F. Rawah (SA), Temporary

A. Mahasandana (ST)

P. Inderbinen (SZ)

D. Ronicle (UK)

P. Pollard (US), Temporary

G. Tsibouris, Acting Secretary  
 H. Malothra, Summing Up Officer  
 M. Gislen, Board Operations Officer  
 M. McKenzie, Verbatim Reporting Officer

### Also Present

African Department: K. Ongley, N. Aivazova, D. Desruelle, Y. Mu, K. Ongley, D. Robinson, A. Selassie, J. Yao. Finance Department: N. Denewet. Legal Department: A. Rosha, D. Schwarz. Strategy, Policy, and Review Department: Y. Wu. World Bank Group: Y. Kiendrebeogo. Alternate Executive Director: I. Mannathoko (AE), K. Obiora (AE). Senior Advisors to Executive Directors: S. Evjen (NO), G. Gasasira-Manzi (AE), W. Nakunyada

(AE), O. Odonye (AE), T. Sitima-wina (AE). Advisors to Executive Directors: A. Abdullahi (AE), W. Al Hafedh (SA), X. Cai (CC), M. Coronel (BR), D. Crane (US), J. Garang (AE), M. Ismail (AE), M. Kikiolo (AP), U. Latu (ST), R. Lopes Varela (AF), A. Urbanowska (SZ).

**1. SIERRA LEONE—FIRST REVIEW UNDER THE EXTENDED CREDIT FACILITY ARRANGEMENT, REQUEST FOR A WAIVER OF NONOBSERVANCE OF PERFORMANCE CRITERION, AND FINANCING ASSURANCES REVIEW**

Mr. Mahlinza and Mr. Nakunyada submitted the following statement:

Introduction

Our authorities appreciate the constructive dialogue with staff during the recent Extended Credit Facility (ECF) program review mission. They broadly share staff's assessment and agree with key policy recommendations.

Sierra Leone has made steady progress in stabilizing macroeconomic conditions since the end of the Ebola crisis in 2016. Renewed reform efforts supported by the decisive implementation of longstanding reform measures by the new administration, which assumed power in April 2018, have laid a strong foundation for accelerated economic recovery. The reform agenda is guided by the new Medium-Term National Development Plan (NDP 2019–2023), whose objectives include improving livelihoods through education; promoting diversification, boosting resilient and inclusive growth; addressing governance challenges; and strengthening public financial management. To anchor reform efforts, the authorities concluded a new ECF arrangement with the IMF in November 2018. This arrangement, which has been under implementation for the last six months, seeks to entrench macroeconomic stability, ensure fiscal and debt sustainability, support structural reforms, and build buffers.

To help achieve the reform objectives, our authorities look forward to Executive Directors' support for the completion of this first review under the ECF arrangement. They further request a waiver for the non-observance of a performance criterion.

Program Performance

Performance under the ECF arrangement remains broadly satisfactory, and the program remains on track. All end-December 2018 quantitative performance criteria (QPCs) were met, except the net domestic assets (NDA) of the Bank of Sierra Leone (BSL) and the indicative target on poverty-related spending. The QPC on NDA was missed due to a bridge loan extended by the BSL to government in anticipation of timely disbursements under donor budget support. The effect of the delay in budget support on the end-December NDA targets was, however, corrected in the first quarter

of 2019. Going forward, the authorities will be vigilant in ensuring stronger program performance through regular monitoring and prompt implementation of corrective actions.

Implementation of structural reforms has progressed well, although three out of five structural benchmarks (SBs) were delayed owing to unforeseen technical complexities. The development of a strategic plan for the two state-owned banks (SOBs) proved more complex as it required an update of the baseline diagnostic assessment prepared in 2016. A new diagnostic study will now be prepared with support from the World Bank, for completion by end September 2019. Work on the audit and validation of arrears was completed and the authorities are now integrating related work streams to ascertain the headline arrears amount. This work is now expected to be completed by end-August 2019. Regarding the delayed SB on the forensic audit of the BSL, the scope of the audit turned out to be broader than expected. Nevertheless, the audit report has been finalized and the authorities are now focusing on publishing the report and developing an action plan by end-August 2019.

#### Recent Economic Developments and Outlook

Economic growth slowed from 3.8 percent in 2017 to 3.5 percent in 2018 against the background of a contraction in non-mining activity and the continued closure of major iron ore mining operations, owing to low export prices. The slowdown in public investment projects, which dampened construction activity, also constrained growth. Real GDP growth is, however, expected to rebound to 5.1 percent in 2019 and average 4.8 percent in the medium-term, largely benefitting from the resumption of iron ore production at the Marampa Mines, the commencement of several construction projects, and increased investments in agriculture.

Inflation, which peaked at 19.3 percent in September 2018, declined to 17.5 percent in March 2019. Going forward, inflation is expected to decline owing to improved food supplies, and tight monetary conditions. At the same time, external reserves declined from 3.7 months of imports in 2017 to 3.6 months of imports in 2018, reflecting delayed disbursement of donor budget support. In the medium term, gross reserves are expected to average 3.5 months of imports.

## Fiscal Policy and Debt Management

The authorities remain committed to sustain fiscal consolidation efforts to place public debt firmly on a downward path. Towards this end, they are aggressively implementing several tax administration measures including: eliminating fuel subsidies; maintaining automatic fuel price adjustments; automating tax processes to enhance monitoring<sup>1</sup>; conducting specialized tax audits, enforcing tax compliance; streamlining duty waivers and exemptions; and expansion of the Treasury Single Account (TSA) to cover additional Ministries, Departments and Agencies' (MDAs). The on-going data matching exercise between the National Revenue Authority (NRA) and various government agencies, and the adoption of the Extractive Industry Revenue Bill in 2018, which seeks to improve the fiscal regime for mining companies, could yield additional benefits.

The authorities have implemented several expenditure control measures related to public sector vehicle procurement, fuel allocation, and travel expenses, as well as the development of a vehicle fleet policy with the assistance of the World Bank. In addition, the introduction of biometric verification of civil servants, has reduced leakages. The authorities will continue to protect poverty-reducing spending and other priority expenditures outlined in the NDP. Additional efforts include the ongoing strengthening of public investment management and re-negotiation of the terms for several infrastructure projects to ensure fair pricing and value for money. In parallel, public procurement processes have been improved and plans to introduce an e-Government Procurement (e-GP) System to improve the quality of public procurement, have advanced. Going forward, the authorities will continue to pursue a conservative medium-term expenditure path, supported by the on-going automation of government payment systems.

To mitigate the elevated debt vulnerabilities, the authorities continue to prioritize concessional loans to finance infrastructure projects with potential to spur high growth. Accordingly, priority will be accorded to non-debt creating financing, including public-private partnership (PPP) and Build Operate and Transfer (BOT) arrangements. Relatedly, the authorities are looking forward to the IMF-led PIMA to help identify strengths and weaknesses in public investment. Furthermore, the Medium-Term Debt Management Strategy developed in collaboration with the World Bank is expected to guide debt management practices going forward. Moreover, the

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<sup>1</sup> Automation efforts include the Integrated Tax Administration System (ITAS) for domestic taxes, the web-based ASYCUDA World for Customs and Electronic Cash Registers for goods and services tax (GST).

authorities are planning to conduct regular self-assessments of debt sustainability to provide important early warning signals.

### Monetary and Financial Sector Policies

The authorities remain committed to maintaining a tight monetary policy stance through reserve money targeting to reduce inflation to single digit levels in line with the BSL objective. Going forward, the authorities will continue to improve monetary policy operations to facilitate transition to a price-based monetary policy framework. They also continue to attach importance to improving the transmission mechanism and transparency in the conduct of monetary policy while strengthening forward-looking liquidity management through the development of the repo market. Fund technical support will help in strengthening the role of indirect monetary policy instruments and deepening domestic capital markets. To preserve reserve buffers and allow greater exchange rate flexibility, the BSL commits to confine foreign exchange interventions to the smoothening of disorderly market conditions.

The banking sector remains broadly stable, liquid, and profitable, with ample capital buffers, an expanding deposit base, and improved asset quality. Importantly, the withdrawal of correspondent banking relationships (CBRs) has slowed following measures adopted to strengthen the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) framework. The BSL is also stepping up efforts to further strengthen the regulatory framework to mitigate fintech and cyber-risks. Further, the authorities are aggressively promoting financial inclusion. In addition, amendments to the BSL Act, recently passed by Parliament, are expected to help strengthen central bank governance and operational autonomy.

### Structural Benchmarks

The clearance of domestic arrears to reduce macro-fiscal risks ranks high on the authorities' agenda. In this regard, ongoing public financial management (PFM) reforms to support good governance and strict adherence to commitment controls through the Integrated Financial Management Information System (IFMIS), are expected to help prevent the future build-up of arrears. At the same time, the authorities are currently engaging the World Bank to seek additional support to clear some of the arrears. Meanwhile, the government has already developed a draft strategy to pay down arrears including through: outright cash payments; issuance of longer dated government securities; utilization of grant resources and budgetary

allocations. IMF assistance is expected to help ascertain the scope for securitization.

The authorities appreciate the need to mitigate fiscal risks emanating from the two State-Owned Banks. To this end, the government appointed new Boards of Directors while the BSL adopted an enhanced supervision approach and put in place stringent rules to prevent lending to politically-exposed persons (PEPs). Credit risk management and underwriting practices have also been enhanced. Consequently, performance of the SOBs has improved, with better credit quality and profitability. Furthermore, internal controls and identified governance deficiencies have been addressed.

### Conclusion

Our authorities reiterate their firm commitment to implement reforms geared to raise growth prospects, improve living standards, increase private sector investment, and achieve Sustainable Development Goals (SDGs). To this end, they are determined to successfully implement reform measures under the Extended Credit Facility arrangement to entrench macroeconomic stability and unlock the country's growth potential. They remain optimistic that continued Fund policy engagement and technical support will help in the realization of the country's overall development objectives.

Ms. Pollard and Ms. Crane submitted the following statement:

We thank staff for the report and Mr. Mahlinza and Mr. Nakunyada for the informative buff statement. We welcome early progress under the program, while recognizing the steep path ahead to meet key program objectives including strengthening of reserves and creation of fiscal space to boost carefully prioritized investments in human and physical capital. We encourage the authorities to persist in their efforts. We thank staff for the helpful references to capacity development in the report. We concur with the thrust of the staff appraisal and would highlight several points.

Fiscal. We welcome the fiscal prudence so far, and the progress on key reforms such as the Treasury Single Account, while encouraging the authorities to focus on growth-friendly measures. The reduction in capital spending in 2018 is understandable given delays in donor financing, but still unfortunate. We appreciate the authorities' focus on domestic revenue mobilization and agree with the more conservative spending plans so that spending does not get out ahead of revenues. Maintaining the target of revenues exceeding 16 percent of GDP by the end of the program appears

ambitious but achievable, and if the authorities are able to accelerate revenues further, they could have room for higher development spending. Getting a firm grasp on the stock of domestic payment arrears and moving forward on an arrears clearance strategy will be key to reducing pressures on banks and reducing uncertainty for the private sector.

**Public Investment Management.** Making best use of limited resources is a key priority. We strongly support the authorities' interest in a Public Investment Management Assessment (PIMA) and commend the authorities for their commitment to consult with IMF staff before finalizing large infrastructure financing packages. Could staff comment on the Presidential infrastructure initiative (including a recently announced tender for up to \$2 billion for an airport connector bridge) and whether the PPP unit and the Ministry of Planning's public investment unit have adequate capability to manage this large-scale investment, without crowding out other worthwhile investment projects? Also, can staff offer preliminary comments on the possible impact on debt sustainability?

**Monetary Policy.** We encourage the authorities to persist in efforts to curb inflation and rebuild reserve buffers over time. With inflation still in the double digits, a tighter monetary stance should be considered. We recognize the authorities' concerns that exchange rate depreciation could pass through to inflation, but we concur with staff that the authorities should refrain from using limited reserves to lean against depreciation pressures. Can staff elaborate on the approach to supporting gradual reserve accumulation during the program, as we note the quantitative targets have reserves falling over the next several quarters and a modest increase at year end. We also agree with staff that the BSL should shift from providing liquidity to banks on an ad hoc basis to a transparent, forward-looking approach.

**Structural Reforms.** We understand that structural reform objectives proved more complex to achieve than originally anticipated. In the next program review, we would find it helpful if staff presented the sequencing of incremental steps toward larger reforms in a graphic similar to that for Kosovo and Mali on pages 35/36 in the Review of Conditionality – Supplemental Information Paper. This type of presentation could be particularly helpful in fragile states, to better illuminate how smaller steps (which may need to shift based on circumstances on the ground) contribute to meaningful reforms and promote parsimony of objectives.

**Poverty Reduction Strategy.** The World Bank Assessment Letter and Box 1 on the National Development Plan provide helpful context on the

authorities' plans to accelerate growth and reduce poverty. We commend the authorities for the extensive public consultations reflected in the plan and encourage them to consider the World Bank's advice to focus on implementation of a manageable scope of priorities.

Mr. Ozaki and Mr. Komura submitted the following statement:

We thank staff for the comprehensive report and Mr. Mahlinza and Mr. Nakunyada for the informative statement.

We welcome the new government's commitment on its reform agenda and the ECF-supported program. We take note that the program is broadly on track. All quantitative targets were met although the performance criteria (PC) on net domestic asset (NDA) of the Bank of Sierra Leone (BSL), the indicative target on poverty-related spending, and three structural benchmarks (SBs) were missed. On the PC on NDA, we note that the authorities repaid the bridge loans and has committed to avoid a recurrence while the Box 2 implies that the breach could have been avoided by more timely actions. Against this backdrop, we can support the completion of the first review under the ECF-supported program.

The Sierra Leone's economy remains involving significant risks and fragilities as highlighted in paragraph 9. For example, the economy lacks economy and policy buffers to negative shocks from external conditions. Moreover, there exists a difficulty in maintaining reform momentum. We urge the authorities to complete reform agendas under the program, including the three SBs for the second review (which are related to the missed ones in the first review), with strong ownership. We would also like to highlight the importance of keep prioritizing and sequencing reforms and technical assistance given capacity constraints.

As we broadly concur with staff's appraisals, we would like to offer a few comments for emphasis:

#### Fiscal Policy

Sierra Leone needs to secure fiscal sustainability while preserving fiscal space for priority spending. We commend that the authorities remain committed to reduce domestic bank borrowing to around 2 percent of GDP. We agree that revenue mobilization plays a critical role in achieving the goal. The recent Review of Conditionality highlights that programs often fail to achieve revenue mobilization as planned, decreasing capital spending. In this

context, we support to take more conservative revenue assumption and use stronger-than-expected revenue, if materialized, for additional priority spending.

### Debt Management

The authorities need to improve their debt management capacity. We commend that the authorities are preparing a Medium-Term Debt Management Strategy. In addition, as non-debt financing, including PPPs, entails potential risks, we also welcome their commitment to consult staff before determining large infrastructure projects and encourage the authorities to make further efforts to contain those risks, including by enhancing infrastructure governance.

Further efforts to clear domestic payment arrears are warranted. We note that the total stock of arrears is expected to exceed the 4 percent of GDP estimated in the program. We urge the authorities to timely complete the arrears stocktaking and identify a final arrears figure for finalizing the clearance strategy.

### Financial Sector

Steady progresses in reforming the two state-owned banks are needed. We commend that two state-owned banks are recovering due to better BLS's supervision. Noting that developing a strategic plan for the two state-owned banks has proved more complex than expected, we welcome that the authorities have engaged the World Bank for a targeted diagnosis and encourage them to achieve steady progresses in this area.

Mr. Lopetegui and Mr. Corvalan Mendoza submitted the following statement:

We thank staff for the report on Sierra Leone and Mr. Mahlinza and Mr. Nakunyada for their informative buff statement.

The new government elected in April 2018 has shown commitment to reform and macroeconomic stabilization and the program is broadly on track; we support the completion of the first review under the Extended Credit Facility (ECF) arrangement. We take positive note of the new National Development Plan (NDP) that covers the years 2019-23, and which comprises a sub-set of a 20-year long-term national vision for the country. The ultimate goal is to achieve middle-income status by 2039. To reach the NDP goals, strong and continued commitments will be needed to increase tax revenue,

strengthen spending discipline, and closely monitor public debt dynamics to avoid arrears accumulation. The strong and credible fiscal anchor will be fundamental to reduce inflation in a sustained basis and deploy the reforms envisaged in the ambitious NDP.

The new administration has taken several corrective actions aimed at strengthening public finances. Domestic revenues exceeded the 2018 nominal target, and expenditure was significantly reduced by more than 2 percent than programmed. This initial performance sends a strong positive signal to stakeholders about the authorities' commitments to address fiscal imbalances. We are also pleased to read about the NDP process, which went through extensive public consultations, and according to the report, an estimated two million people contributed to the setting of priorities. The validation of the process of the plan is commendable. As shown in Box 1, the macro framework of the NDP is more ambitious than the ECF. Given the strong commitments of the authorities to move ahead with the NDP, we encourage the Fund and other development partners to intensify the capacity development of the country. The NDP is ambitious and will require sufficient funding and operational skills to implement the agenda. While we appreciate the information in Annex I, for future reports, we would like to see more detailed information on capacity development strategies, such as timing and sequencing, and potential coordination with other organizations.

Public debt is categorized as high-risk of distress. We take positive note of the authorities' strategy to finance the budget with concessional loans and its reliance on grants, as well as to remain cautious to foreign borrowing, until revenue mobilization and expenditure control efforts are secure. The total stock of arrears caught our attention. At this point in time, it is hard to understand the huge discrepancies in arrears figures, which are described in Box 3. The initial figure of arrears was 4 percent of GDP when the ECF was requested, and today's potential figure is up to 14 percent of GDP. More progress is needed to strengthen public finance management and the accountability of public institutions. The magnitude of the fiscal liability and associated risks with this level of arrears are too high, therefore, we would like to hear from staff whether these outcomes put the completion of the program at risk.

The fiscal anchor seems fundamental for this program. Strengthening tax administration is essential and the success of the program depends, to a large extent, on bringing about a fundamental shift in the tax paying and collecting culture, an objective that will require sustained efforts by the National Revenue Authority and strong political backing by the government.

Monetary policy will be successful as long as the fiscal anchor becomes credible. We welcome the authorities' efforts to gradually strengthen the Bank of Sierra Leone (BSL)'s capacity to use indirect monetary instruments, as well as their commitment to allowing greater exchange rate flexibility. We take positive note of the BSL law and banking bills that were passed in Congress. The BSL mandate has been clarified to monetary and financial stability, and the law also strengthened its independence and accountability. We learned from the report that external buffers are needed to shield the economy from shocks and more reserves accumulation is warranted. We also take into consideration the authorities' concern of higher depreciation of the domestic currency if the BSL proactively accumulate reserves, and its impact of inflation. We would appreciate further details from staff on the pass-through process in Sierra Leone.

The financial system is small and underdeveloped but generally well capitalized. The non-performing loan (NPL) ratio is not only high but variation among different banks is worrisome (NPLs range from 0 to 30 percent in different banks). On top of that, it is important to limit fiscal contingency risks from two state-owned banks. We encourage the authorities to make use of the new laws introduced by Congress, to modernize the regulation and supervision of the financial system as soon as possible, and to aim towards best international practices.

With these comments, we wish the authorities of Sierra Leone all the best in their future endeavors.

Mr. Sun and Ms. Cai submitted the following statement:

We thank staff for the well-written report and Messrs. Mahlinza and Nakunyada for their helpful buff statement. We commend the authorities' efforts to push forward new reforms and implement the reform measures of previous Fund-supported programs. It is good to note that program implementation is broadly on track. We largely agree with staff's appraisal and support the completion of the first review under the Extended Credit Facility Arrangement.

Maintaining fiscal and debt sustainability remains crucial. We take note of the lower-than-programmed fiscal deficit, which is partly attributed to significant underspending. While we commend the authorities' conservative approach to expenditure, priority spending and growth-enhancing infrastructure spending should be maintained. Strengthening public financial

management and improving spending efficiency are essential to increase fiscal resilience and contain contingent fiscal risks. We welcome the authorities' plan to undertake a Public Investment Management Assessment and adopt a National Public Policy. Non-debt creating financing including PPP could help to meet the financing needs for potential large infrastructure projects. Meanwhile, we encourage the authorities to closely monitor risk arising from PPP with the help of the Fund's technical assistance, where needed. We welcome the ongoing public financial management reforms and encourage enhanced revenue performance to support additional priority spending and reduce domestic arrears.

Enhancing reserve accumulation with greater exchange rate flexibility can play a vital role in reining in inflationary pressure and building buffers against a volatile external environment. We concur with staff that a tighter monetary stance would be appropriate should inflationary pressure persist. Deepening the interbank market and improving monetary policy communication is important for the functioning of the central bank. We welcome the new central bank law, which can strengthen its independence and accountability. We also encourage the authorities to further develop skills needed to improve banking system efficiency. We take positive note of the improvement of correspondent banking relationships and encourage the authorities to continue to strengthen the AML/CFT framework.

Further structural reforms are vital to boost potential growth and reduce poverty. Three out of five structural benchmarks were delayed owing to unforeseen technical complexities. We therefore encourage staff to provide technical assistance in this regard and adjust capacity development priorities where necessary. We take positive note that inclusive growth and poverty reduction are in the center of the recently launched comprehensive reform agenda and encourage the authorities to continue to improve the business environment and diversify the economy.

With these remarks, we wish the authorities every success in their policy endeavors.

Ms. Levonian and Mr. Hart submitted the following statement:

We welcome the initial progress under the ECF and the authorities' continued commitment to the program in a challenging context. A necessary fiscal adjustment is underway and inflation, while high, is trending downwards. Nevertheless, there remain significant external and internal risks to the program. The authorities have capacity constraints and structural

reforms are proving more complex than expected. But the authorities remain committed to the program, as outlined in Mr. Mahlinza and Mr. Nakunyada's helpful buff. In the context of the remedial measures for the missed PC and the broadly satisfactory performance thus far, we support the completion of review, the waiver, and the proposed decision.

The balance between containing fiscal risks and meeting spending needs is a key challenge. We welcome the authorities' efforts to limit spending, expand the coverage of the Treasury Single Account, and sustain the automatic fuel price adjustment. This will also help support lower inflation. Still, the country has major social and development spending needs. The program's emphasis on raising revenues to meet these needs is appropriate. We welcome ongoing enhancements to the national revenue agency and measures to strengthen tax compliance. Nevertheless, progress in these areas is typically slow. We thus support staff's more conservative stance on future revenue projections.

Relatedly, strengthening fiscal governance and investment management should be top priorities. The ongoing PFM reforms and efforts to increase transparency over fiscal risks (including SOEs) are welcome. Strengthening public investment management, supported by a forthcoming PIMA, would help the authorities better execute on their infrastructure ambitions. We welcome the effort to explore non-debt sources of financing, but also the authorities' commitment to consult the Fund before agreeing to any large infrastructure projects, especially for PPPs (which have the potential to increase contingent liabilities).

The ongoing uncertainty around domestic arrears poses an additional risk to debt sustainability. Box 3 points to a stock of arrears that is potentially much larger than the 4 percent of GDP indicated earlier. We welcome the buff's indications that the authorities are drawing on Fund TA and working with the World Bank to obtain support in developing an arrears clearance strategy. Once the stock of arrears and a plan to address them become clear, we would encourage staff to develop different scenarios for accommodating this within the program. This should also be captured in a revised DSA for the next review.

Monetary policy should aim to contain inflation while maintaining sufficient FX buffers in the context of external vulnerabilities. We welcome the authorities' commitment to maintain an appropriately tight monetary policy stance and to allow greater exchange rate flexibility. FX interventions should be limited to periods of heightened volatility, mindful of the impact of

inflation on the poorest and most vulnerable. Modernizing the monetary policy framework with the help of Fund CD should further improve transparency and the overall effectiveness of monetary policy.

It is important that the program retain its catalytic role. We note several good examples of complimentary work by the World Bank throughout the report. But we also note the expected downward trend in donor funding, and the risk that further reductions could limit the ability to reorient spending towards social and infrastructure priorities. Can staff expand on what is driving lower donor support and the prospects for attracting further concessional financing for infrastructure and social spending?

Finally, we welcome the inclusion of Annex 1 outlining Fund CD activities, how they support the ECF's objectives, and potential risks. The feedback from the authorities is also helpful. There could be merit in including relevant capacity development programs from the World Bank Group and other partners, where relevant to the program's success.

Mr. Merk and Ms. Kuhles submitted the following statement:

We thank staff for an informative report and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. We broadly concur with staff's assessment. Although policy measures taken by the authorities have helped to stabilize the economic situation in Sierra Leone, substantial vulnerabilities persist. Mainly suppressed by domestic hindrances, economic growth remains lackluster while inflation and the current account deficit stay well in the double digits. The fiscal situation has improved somewhat, although mostly on the back of substantial underspending in capital investments. The Bank of Sierra Leone (BSL) continues to serve the financing needs of the government. Not least with a view to the considerable program risks – notably including serious vulnerabilities stemming from the elevated debt level – we call on the authorities to step up their efforts to firmly entrench stability-oriented macroeconomic policies and proceed along the structural reform agenda. The authorities' agenda focusing on strengthening governance and accountability is highly welcome in this regard.

Program performance has been rather mixed. The end-December performance criteria (PC) on net domestic assets of the BSL, the end-March IT on poverty-related spending and three out of five structural benchmarks (SBs) were missed. Concerning the IT on poverty-related spending, could staff elaborate in which way the absorption capacity of the poor became a binding constraint for the authorities? With more than half of Sierra Leoneans

living in poverty, we recognize that the floor on poverty-related spending continues to be of great importance going forward, to make sure that growth will be inclusive. We take note of staff's remark, that more timely remedial actions could have prevented the breach of the PC on NDA. We would argue that the practice of repeated fiscal borrowing from the central bank with a repayment shortly before the program's respective test date goes against the economic spirit of the adjustment program. The authorities should rather seek to prepare for potential delays in donor budget support by building additional fiscal buffers. In this regard, we would be interested in staff's view on measuring program performance in fiscal borrowing from the BSL by flows rather than stocks.

Nevertheless, taking note of the authorities' reiterated commitment to the program and the corrective actions taken, we can go along with completing the first review under the ECF-supported arrangement. At the next ECF review, we will play close attention inter alia to the implementation of SBs, three of which correspond to key measures missed for the present review.

We welcome the emphasis in the staff report on measures to tackle fiscal risks and promote efficiency through fiscal structural reforms. Not least with a view to persistent vulnerabilities related to high (external) debt service requirements – a substantial part of which are repayments to the Fund – and the need to prepare for the necessary clearance of arrears, the authorities appear well advised to press ahead with fiscal adjustment in a timely manner. Consequently, we encourage strong efforts on the part of the authorities to raise revenues according to their target, while at the same time observing staff's recommendation for a medium-term expenditure path. Any windfalls should be used for debt reduction. We welcome the authorities' ongoing efforts to strengthen governance, accountability and compliance in the fiscal sector as well as their plans to bolster public financial management and debt management in consultation with the Fund, prioritizing grants and highly concessional loans.

Persistently elevated inflation makes a strong case for pursuing tighter monetary policies and for strengthening the BSL's framework. Given the high degree of fiscal dominance apparent in the regular recourse to bridge loans from the BSL to finance budgetary shortfalls, and the resort to scarce foreign exchange reserves to counter depreciation pressures, we would be interested in staff's view whether the new BSL Bill can effectively ensure an adequate level of central bank independence in Sierra Leone. Does staff propose additional measures in this regard? We second staff's call to actively

strengthen reserve buffers while generally allowing for exchange rate flexibility. We call on the authorities to work towards setting state-owned banks on a firm commercial and financial footing. Could staff comment on the merits of privatizing said banks?

Mr. Geadah and Ms. Abdelati submitted the following statement:

We thank staff for a concise and balanced report and Mr. Mahlinza and Mr. Nakunyada for the informative buff Statement. We welcome the actions taken by the new government to stabilize conditions and their overall adherence to program targets. Nevertheless, the situation remains challenging and continued efforts are needed to manage fiscal risks in a way that ensures debt sustainability and provides enough space for priority spending. Also, it is important to put in place a strategy to clarify the magnitude of domestic payment arrears and to clear them in a timely manner. We support the steps being taken to limit macro-fiscal risks from the state-owned banks by updating the diagnostic studies before preparing reform plans. We also support the focus on strengthening the governance framework of the central bank and its supervisory capacities and on modernizing its monetary policy framework. We support completion of the First Review and have the following two comments.

We commend the authorities for preparing Sierra Leone's medium-term National Development Plan: Education for Development, which lays out the first 5 years of a 20-year vision for achieving middle income status. We note that the macro framework and economic policy agenda of the NDP are broadly aligned with those of the ECF-supported program. We hope that adequate financing and technical assistance will become available as the World Bank assessment highlighted the financing of the agenda and implementation capacity as the key risks to its success. While recognizing that every country has its own unique circumstances, we would welcome information on any good models or lessons from peers who have successfully implemented such an education-focused strategy.

While structural benchmarks are appropriately kept to a reasonable number—five benchmarks for the First Review and five benchmarks for the Second Review—they are complex and three of them could not be met on time. We do not dispute that the benchmarks were macro-critical and necessary for achieving the objectives of the program. However, staff states: “they have proved to be more complex and dependent on expert advice than anticipated”. We have seen a similar difficulty in other cases related to the design of structural benchmarks. One SB called for a strategic plan for the two

state-owned banks by March 31, 2019, while the revised SB calls for updating a 2016 diagnostic study with support from the World Bank by September 30, 2019 as a preliminary step toward having a strategic plan. Similarly, in the case of a plan for dealing with the outstanding stock of arrears to suppliers by end-March, a preliminary step will be needed to complete the stock taking of arrears with IMF technical assistance by end-August 2019. We would be interested in a stock taking of structural benchmarks that in retrospect proved to be overly ambitious in design and/or needed technical assistance and additional time to complete.

Mr. Tan and Mr. Chea submitted the following statement:

We thank staff for the comprehensive report and Mr. Mahlinza and Mr. Nakunyada for their informative buff statement.

Given Sierra Leone's persistently challenging macroeconomic conditions, we commend the authorities' commitment in securing fiscal sustainability, and in implementing the reform agenda to strengthen macroeconomic and social development. While the program performance is assessed to be broadly on track, lingering fiscal risks and volatile external environment pose vulnerabilities to the country's economic outlook in the near- and medium-term. In this context, further efforts in ensuring durable fiscal consolidation and preserving financial and monetary stability are crucial in promoting inclusive and sustainable economic growth. We broadly concur with staff's recommendations and support the completion of the first review of the ECF-supported program, and the other proposed decisions. The following comments are offered for emphasis.

Effective revenue mobilization and expenditure prioritization are vital in securing fiscal sustainability over the medium-term. We are pleased with the authorities' continuous efforts in the ongoing Public Financial Management (PFM) as well as tax policy and administrative reforms to enhance spending efficiency and create fiscal space for priority spending such as social and infrastructure developments. Given Sierra Leone's macro-fiscal risks and rising debt service over the medium-term, we also support the authorities' request for an IMF-led Public Investment Management Assessment (PIMA) and the development of a new Medium-Term Debt Management Strategy to align investment with the recently-launched National Development Plan (NAP). In particular, it is paramount that decisive actions are taken to address domestic payment arrears and we echo staff's call for the authorities to swiftly enforce on an arrears clearance strategy and to safeguard the viability of the two state-owned banks.

Given the volatile external macroeconomic environment, it is important to make further progress toward preserving financial and monetary stability. We welcome the authorities' new BSL and Banking Bills to promote the integrity and accountability of the financial system and enhance the banking regulatory and supervision frameworks. Continued efforts are warranted, particularly with respect to the missed SBs on forensic audit of the BSL and strategic plan for the two state-owned banks. We also concur with staff for the authorities to build up international reserve buffers and anchor monetary policy to bring inflation down to single digit. This will help the economy to adjust to the volatile macroeconomic environment and mitigate against unexpected shocks.

Lastly, we encourage the authorities to continue to work closely with development partners and leverage Fund TA to achieve the overall program goals, including with respect to helping boost human capital required to resolve structural bottlenecks and support social development. The slower than expected structural progress is evident of the authorities' capacity constraints vis-à-vis the complexity of the structural reforms needed. While we note that Annex I set out the key CD priorities from public finance management, tax policy and revenue administration, financial sector supervision, central banking operations and governance to statistics, we would appreciate staff comments on the need and sequencing for technical assistance in relation to other medium-term objectives under the authorities' NDP for accelerating growth and reducing poverty.

With these remarks, we wish the authorities continued success in their policy endeavors

Mr. De Lannoy, Mr. Psalidopoulos, Mr. Etkes and Mr. Persico submitted the following joint statement:

We thank staff for the comprehensive report and Messrs. Mahlinza and Nakunyada for their informative buff Statement. We share the staff's appraisal and commend the authorities for the broadly satisfactory program performance. We approve the completion of the first review under the Extended Credit Facility Arrangement (ECF) as well as the proposed waiver of non-observance of a performance criterion. The remarks below are provided for emphasis.

Recently real GDP growth slowed but it is expected to rebound. Inflation, while declining, remains at a disquieting high level. Staff projected a

sensible economic recovery (5.1 percent of GDP) in 2019 and a medium-term growth of 4.75 percent over the medium term. In our view, the immediate projections appear overly optimistic, also taking into account the rigidities of the mining sector (the closing of some mines is a quasi-structural element as it will take time for them to return fully operational) and the domestic nature of the main downside risks. The persisting double-digit inflation calls for urgent and coordinated action among fiscal and monetary authorities.

We welcome a lower-than-programmed fiscal deficit, although it is partially due to a cautious and somewhat non-optimal budget execution. We note that the authorities adjusted the public expenditures to address delays in the expected budget support. We wonder whether the program design could help the authorities to address this issue going forward. Staff's comments are welcome. While we take good note of the positive revenues' performance, we invite the authorities not to rely on one-off fiscal measures but to timely implement the envisaged reforms in order to deliver permanent improvements and to streamline existing taxation. Additionally, we call on the authorities to strengthen the budget execution in order to preserve priority and social spending.

Despite an overall positive program performance, structural improvements remain limited. The missed structural benchmarks on arrears clearance and state-owned banks, as well as the missed quantitative criterion on net domestic assets are unfortunate. As the "inability to clear and prevent new arrears poses a sizeable risk to securing debt sustainability", we would have appreciated an update on the risk of debt distress. Staff's comments are welcome. Moreover, in light of the missed indicative target on social spending, we see merit in the modification of the target in a performance criterion as already done for similar programs.

We are somewhat surprised by staff's risk assessment. First, climate fluctuations and climate change may affect Sierra Leone, as the majority of the workforce is employed in agriculture and about one third of GDP is generated by this sector. Specifically, World Bank data suggest that average temperatures are expected to rise due to climate change. In addition, according to recent events it seems that global monetary tightening is not expected in the next few years. Staff's comments are welcome.

We welcome the central bank's plan to bring inflation down to 14 percent by end-2019. At the same time, it is surprising that no elements of this plan are considered in program conditionality. In particular, we wonder if building on the envisaged technical assistance- staff could provide a

potential road map for establishing a clear and transparent transmission mechanism. Considering that a large share of the population lives below the poverty line, reducing inflation as well as strengthening the governance of the central bank and banking sector, are key elements of the overall strategy to support inclusive growth.

We appreciate the complementarity between the ECF and the authorities' National Development Plan (NDP) as well as the reported cooperation with the World Bank in several areas. We welcome the measures aimed at reducing poverty envisaged in the MFEP. We see merit for a better integration of these actions in program conditionality in order to both complement the signaling role of the social spending floor and to support the implementation of the NDP. At the same time, we would appreciate a greater attention to social and poverty issues in staff's analyses (human capital, inequality, etc.).

We welcome Annex I on the Technical Assistance (TA) priorities, as a good step forward in the much-desired integration of Capacity Development (CD) in surveillance and lending. The annex lays out the objectives and priorities for an unspecified time horizon. We encourage staff to complement the annex with information on past TA and training of officials by topic, assess if past CD activities were effective, and spell out priorities for training. Finally, staff could also relate CD activities to the program criteria and benchmarks. Staff's comments are welcome.

Mr. Benk and Mr. Stradal submitted the following statement:

We thank staff for their informative paper, and Messrs. Mahlinza and Nakunyada for their helpful buff statement. We welcome the continued commitment of President Bio's administration to the reform agenda under the Extended Credit Facility (ECF) arrangement. However, we note that the opposition parties control a majority in the parliament, which poses risks for implementing the needed reforms. We commend the progress achieved in the early stages and encourage the authorities to persevere in their reform efforts as significant vulnerabilities remain. We support the completion of the first review under the ECF and the request for a waiver of nonobservance of performance criterion, but highlight the elevated near-term risks stemming from weak institutions which require close monitoring.

Maintaining fiscal prudence remains essential. We welcome the authorities' recommitment to reducing the wage bill to 6 percent of GDP by the end of the program, guided by the public sector payroll verification

exercise currently underway. We concur with staff in supporting the authorities' request for a Public Investment Management Assessment which may unlock significant efficiency gains. Domestic revenue mobilization plans, including strengthening the National Revenue Authority's governance framework and streamlining tax processes, should be implemented in a timely manner to create space for much-needed infrastructure and human capital investments. We encourage the authorities to step up their efforts to strengthen their debt management strategy to minimize the recurrence of arrears and central bank financing of the budget.

We are concerned by the identification of a larger stock of arrears than previously assumed. It is critical that the total amount of arrears is ascertained as soon as possible to enable effective fiscal planning and an adequately informed Debt Sustainability Analysis. We note that the government is discussing with the World Bank the possibility of scaling up budget support to US\$ 100 million, of which US\$ 60 million would be used to clear arrears. Could staff discuss the alternatives in case the discussions do not produce the desired support?

Tight monetary policy is needed as the headline inflation has been in the double-digit territory for the past three years with no clear downward trend. We concur with staff that flexibility of the exchange rate should play a more prominent role in macroeconomic adjustments, while safeguarding the scarce FX reserves. We welcome the new legislation aimed at strengthening the central bank's (BSL) independence, governance, and accountability. We encourage immediate steps to strengthen the BSL's internal controls to facilitate ministries and agencies depositing their foreign currency at the BSL, rather than in commercial banks. With regards to the two state-owned banks, could staff elaborate on the preliminary prospects for privatization?

We welcome Annex I, detailing the capacity development priorities which seem well-aligned with the program objectives. We underscore the key role of improving the governance of tax administration, the central bank, and state-owned enterprises and banks, including the imposition of effective anti-corruption safeguards. We recognize the invaluable role that the Resident Representative Office plays in ensuring that the technical assistance provided by the Fund is leveraged to a maximum possible extent given the capacity constraints.

Mr. Inderbinen, Mr. Sigurgeirsson, Mr. Evjen and Ms. Urbanowska submitted the following joint statement:

We thank staff for the informative report and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. We broadly concur with staff's assessment and policy recommendations and would like to offer some comments for emphasis.

Sierra Leone's economic outlook is broadly balanced in the near- and medium term. Despite lackluster growth, elevated inflation, and high public debt, the overall program performance is satisfactory. We thus support the completion of the first review under the Extended Credit Facility (ECF) arrangement. Nevertheless, risks to the program are significant, especially those related to fiscal discipline. We note the missed performance criterion on net domestic assets (NDA) of the central bank, and we encourage the authorities to put in place a control system to prevent a future build-up of arrears. Additionally, poverty reduction and social protection should continue to be a priority for the authorities.

A tight fiscal stance is crucial to alleviate risks to sustainability. Stabilizing public debt while implementing a credible strategy for clearing domestic arrears remains essential to the program's success. Further fiscal consolidation efforts should focus on mobilizing domestic revenue and improving tax administration. In this context, we welcome the ongoing work on the amended National Revenue Authority's (NRA) Act as well as the plans to automate tax processes. On the expenditure side, recent commitments to lowering fuel subsidies and rationalizing expenditures are welcome.

Improving debt management should complement efforts to restore debt sustainability. Given the country's significant development needs and the magnitude of the fiscal burden, the authorities' intention to prioritize grants and highly concessional loans to finance infrastructure projects is warranted. Furthermore, we urge the authorities to follow through on their commitment to adhere to the external debt ceiling (as set out in Table 1 of the MEFP) and to carefully assess the cost of any potential new borrowing. We welcome the progress in preparing a Medium-Term Debt Management Strategy with the support of the World Bank. The MTDMS will be an important tool to guide policymakers in their borrowing decisions.

More rapid reserve accumulation, while allowing for greater exchange rate flexibility, remains a key program component. Building and maintaining adequate reserve buffers, alongside reforms to deepen the foreign exchange

market, would help shield the economy against external shocks. Moreover, we welcome the BSL's commitment to modernize its monetary policy framework. Public trust in the central bank is of significant importance at the current juncture, given that bringing down inflation to single digits is a key pillar of the program.

Strengthening the BSL's governance framework remains imperative. Reducing vulnerability to corruption in the central bank is especially important to safeguard Fund resources. Addressing the findings of the forensic audit will be critical to bolstering public trust in the institution, and we encourage the authorities to move expeditiously in resolving this matter.

We welcome the inclusion of Sierra Leone's capacity development strategy in Annex I. We share staff's view on the overall CD priorities, which are at the core of the planned structural reforms. Continued Fund technical assistance will be crucial to meet the program's objectives. At the same time, capacity building efforts should take into account the absorptive capacity of Sierra Leone. More generally, we encourage the authorities to step up their efforts to adopt the necessary reforms to unlock the country's growth potential.

Mr. Razafindramanana and Mr. Lopes Varela submitted the following statement:

We thank staff for their comprehensive report on Sierra Leone and Mr. Mahlinza and Mr. Nakunyada for their informative buff statement.

We welcome progress made by the Sierra Leonese authorities in the implementation of their ECF-supported program to strengthen the macroeconomic stability, advance structural reforms, and achieve a higher and more inclusive economic growth. This good implementation of the program has helped in reducing the fiscal deficit, inflation, and current account deficit. We note in particular that all quantitative targets set for end-December 2018 were met except the criterion on net domestic assets of the Bank of Sierra-Leone and the end-March 2019 indicative target on poverty-related spending.

Given the authorities' performance and strong commitment to achieving the program's objectives, we support the completion of the first review under the ECF-arrangement, the request for waiver of non-observance of performance criterion and financing assurances review.

Sierra Leone's economic outlook is promising with the resuming of higher-grade iron production and increased agriculture and services as well as with the pursuit of policy reforms to further improve the business environment. Increased efforts in these areas will help mitigate risks and vulnerabilities surrounding the economy.

Going forward, we broadly agree with the staff's policy recommendations and wish to make the following comments for emphasis.

The authorities' continued commitment to safeguarding fiscal and debt sustainability is commendable. The measures envisaged in the 2019 budget to increase revenues and reducing expenditures will help meet the program targets and improve fiscal management. Moreover, we also encourage the authorities to step up their efforts in domestic revenue mobilization, given the pressing needs for more resources to finance essential spending and address the challenge represented by the rising debt. In this regard, we see merit in the authorities' plan to enhance the NRA's governance and operations as well as the implementation of the Integrated Tax Administration System (ITAS) which will help to strengthen tax compliance and meet the authorities' revenue objectives. On the expenditure front, the authorities' efforts should be further focused on improving efficiency in public expenditure management while implementing priorities highlighted in their national development plan (NDP). Besides, the commitment to achieving the target of 6 percent of GDP is worth noting and streamlining measures envisaged in this regard are appropriate. Furthermore, we are encouraged by the authorities' request for an IMF-led PIMA to further improve public investment management by identifying weaknesses and strengths to promote efficiency in the use of scarce public resources. We look forward to the adoption of National Public Investment Policy based on PIMA 's recommendations.

Prudent debt management is crucial to support the authorities' efforts to keeping public finances in order. The authorities' decision to set a ceiling on new concessional public external debt as well as their commitment to zero limits for non-concessional public external debt are steps in the right direction and will help to address the debt issue. We encourage them to step up their efforts to finalize the Medium-Term Debt Management Strategy to improve the management of their debt. Also, the avoidance of further arrears' accumulation to suppliers and additional efforts to clear the outstanding stocks would be critical to mitigating its adverse effects in the overall economy. In this regard, there is also a need to design and implement a well-sustainable strategy for arrears clearance, which would increase confidence in public service delivery and public finances management.

Increased efforts to pursue the inflation declining path and further progress with exchange rate flexibility are critical to enhancing macroeconomic stability and external position. We note that the authorities have made good progress in reducing the inflation and we encourage them to speed up their efforts to meet the 2019 inflation objective and move forward to a single digit. To this end, it will be necessary to keep a tight monetary policy stance to subdue inflationary pressures and foster the decreasing course of inflation. The use of indirect instruments by the Bank of Sierra Leone (BSL) is to be envisaged with a TA from the Fund. The BSL should also shift to a more transparent and forward-looking approach regarding the provision of liquidity to banks. On the exchange rate, allowing more flexibility will help increase the economy's competitiveness and mitigate vulnerabilities stemming from external shocks. Moreover, we encourage the BSL to pursue needed reforms to deepen the foreign exchange market and avoid measures leading to restrictions on current international transactions.

Strengthening BSL governance and tackling the two state-owned banks difficulties are necessary to enhance the banking system stability. We commend the authorities for the recent passage of the new BSL Act which will help bolster the Central Bank's independence and accountability as well as its supervisory capacity to better address the vulnerabilities in the banking sector. We also see merit in the planned diagnostic of the two state-owned banks with a view to elaborating a strategic plan for their restructuring to ensure financial viability and compliance with prudential norms. We would appreciate staff comments on the privatization of these two banks to address the fiscal risks and foster the development of a sound banking system.

With these comments, we wish the Sierra Leonean authorities every success in continuing implementing their ECF-supported program.

Mr. Heo and Mr. Kikiolo submitted the following statement:

We thank staff for the candid report and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. We generally concur with the staff analysis and make the following points for emphasis.

Given the staff assessment that the program performance is broadly satisfactory despite slower than anticipated progress in structural reforms, we support the completion of the first review under the ECF arrangement, request for a waiver of nonobservance of performance criterion, and financing assurances review. We also noted that Sierra Leone has the capacity to repay

the Fund. We encourage the authorities to implement the remedial measures and maintains strong commitment to the structural reform agenda. The ECF program ended in 2018 and this review is about a successor program after that. What were the main lessons from the previous one, good or bad? How were those lessons incorporated in the current program? Can staff highlight the main differences between the two programs?

We encourage the authorities to sustain fiscal consolidation to put debt on a downward trajectory. We appreciate the tax administration measures the authorities are continuing to undertake as highlighted in the buff statement. We also welcome the authorities' conservative expenditure approach considering the substantial fiscal risks to revenue collections. Efforts to tighten procurement processes and expenditure leakages are commendable and we see value for the PFM reforms to be sustained. Considering poverty is pervasive in Sierra Leone, we concur with staff that poverty related spending should be protected. Also, the authorities should ensure revenue excesses are invested in priority infrastructures. We note the budget support shortfalls in 2018 had affected planned government programs including infrastructure investment. What were the underlying reasons for the shortfall and what assurances are there to ensure planned budget support for 2019 are disbursed on time?

We look forward to the medium-term debt management strategy the authorities are developing in line with IMF TA recommendations that aims to reduce roll-over risk and borrowing costs. We applaud the authorities for redoubling efforts to clear domestic payment arrears as these arrears could pose a challenge to efforts to reduce the "high" risk of debt distress as indicated by the 2018 debt sustainability analysis. We appreciate the inclusion of the arrears verification exercise as a structural benchmark seeing its importance to the finalization of an arrears clearance strategy. With regard to domestic arrears, the buff stated that the "IMF assistance is expected to help ascertain the scope for securitization." We welcome staff's elaboration on it.

We encourage the authorities to safeguard price and financial stability. Given the high inflation, we concur with staff that the authorities should focus on lowering inflation and a contractionary monetary policy is deemed appropriate though we noted that the BSL has refrained from raising the policy rate further in 2019 due to slower economic activity and tight financial conditions. Going forward, we support the authorities' intention to develop indirect instruments in line with plans to modernize the monetary policy framework. We also wonder how can BSL improve the transmission mechanism of monetary policy? We welcome staff's elaboration. We agree

that the authorities should continue to build reserve buffers. We also welcome the financial legislative reforms including amendments to the BSA Act and the Banking Act as these will greatly enhance the legal framework and support financial sector development in Sierra Leone. Could staff elaborate more on the situation of the delayed forensic audit of BSL? What is the main takeaway from the audit report, which is due to publish by end-August 2019?

We urge the authorities to sustain policy reforms that improve the business environment and promote economic diversification. We take positive note of the significant improvement in ease of starting business index which Sierra Leone ranked 55 out of 190. We appreciate the solid intentions of the medium-term national development plan—education for all strategy and would encourage the authorities to liaise closely with development partners as this will require significant investment. We also encourage the authorities to accelerate governance reforms, upskill workers, and promote potential productive sectors. Finally, we echo the authorities' request for technical assistance from the Fund and other development partners.

Mr. Guerra and Ms. Arevalo Arroyo submitted the following statement:

We thank staff for the report and Mr. Mahlinza and Mr. Nakunyada for their helpful buff Statement. Sierra Leone has made significant progress since the Ebola crisis. We are encouraged by the authorities' reform agenda under the Medium-Term National Development Plan (NDP) to secure macroeconomic gains and lay the foundations for sustained inclusive growth. We note that the Extended Credit Facility (ECF) program is broadly in track, although the implementation of structural benchmarks has proven more challenging than expected. We support the authorities' request for completing the first review under the ECF arrangement and the waiver for the nonobservance of the PC.

Continued commitment to fiscal sustainability and revenue mobilization will be crucial for the success of the program. Considerable efforts to reduce expenditures, expand the TSA and implement the liberalized fuel price mechanism have yielded a lower fiscal deficit and higher domestic revenue. Although progress is ongoing, the quality of the adjustment should be considered and efforts to enhance revenue mobilization should continue. In this regard, as domestic capital spending has been below budget, we support that authorities now envisage a gradual increase. On the revenue side, although we welcome the ambitious commitment by the authorities to raise domestic revenue to 20 percent of GDP, we agree with staff that a more cautious revenue path is prudent for medium-term goals. Reforms to enhance

the governance and operation of the National Revenue Authority (NRA) and to upgrade the new tax system (ITAS) will contribute to achieve the program's revenue targets. We also see merit in the request for a PIMA mission to strengthen public investment.

Improving debt management and an arrears clearance strategy are needed for ensuring debt sustainability. We support that the Medium-Term Debt Management Strategy draws from IMF's TA and the intention to prioritize grants and highly concessional loans. We welcome Box 3 that provides a useful overview of progress in the determination of the actual size of the stock of arrears and as stated in the buff, we look forward to the results of the undergoing work to ascertain the headline arrears amount.

The current tight monetary policy stance is appropriate to anchor monetary policy in bringing down inflation to single digit levels. We welcome IMF technical assistance to strengthen the role of indirect instruments to achieve a more effective price-based monetary policy, as well as regarding the deepening of domestic capital markets.

We agree with staff that allowing exchange rate flexibility is required amidst a volatile external environment. While we take note of the concerns regarding the potential inflation pass-through arising from depreciation, we consider that limiting FX sales to smooth excessive volatility is warranted to maintain adequate international reserve coverage.

Efforts on strengthening governance and accountability of the BSL are on the right path, but further measures are required. We see merit on the passage of the BSL and Banking Bills. We look forward to the remedial action plan to address the forensic audit recommendations as well as swifter progress on the implementation of safeguard recommendations.

We welcome the helpful Annex on Capacity Development activities by the IMF. In particular, we find useful to have the overall CD priorities and their alignment with many of the structural reforms needed under the program.

Mr. Mouminah, Mr. Alkhareif and Mr. Rouai submitted the following statement:

We thank staff for their candid report and Mr. Mahlinza and Mr. Nakunyada for their helpful buff statement. We broadly share staff conclusions and policy recommendations, support the proposed decision, and would like to emphasize the following points.

We are encouraged by the progress being made by Sierra Leone under the ECF-supported arrangement. Despite important challenges, we commend the new government for staying the course under the ECF and for taking important actions that are helping in stabilizing the economy. The fact that the program's goals are aligned with the authorities' recently-launched National Development Plan (NDP) for 2019-23, a point emphasized during the recent Board discussion on the Review of Conditionality, augurs well for strengthening ownership and for a successful implementation of the program's commitments.

The improvement in the fiscal position is welcome. Thanks to the authorities' efforts to mobilize revenue and expand the coverage of the Treasury Single Account (TSA), it is expected that the overall deficit for 2019 will be lower than at the time of the program request. Despite these improvements, we take note of the reduction in capital spending and encourage the authorities and staff to focus their efforts on addressing the following two challenges:

**Budget Financing:** We note that the government has relied on large borrowings from the Bank of Sierra Leone (BSL) to bridge for delayed donors' support, thus breaching the December 2018 PC on NDA. While we are comforted by the authorities' commitment under the program to reduce domestic bank borrowing to around 2 percent of GDP, could staff clarify why banks' appetite for T-bills is declining?

**Domestic Arrears Clearance.** We take note of staff conclusion that clearance of arrears is more complex and will take more time than projected when the program was approved. In this regard, we welcome current efforts to identify arrears and manage fiscal risks through the ongoing public financial management (PFM) reforms. Could staff clarify how the uncertainty about the level of arrears is impacting the program parameters and the private sector in general and provide an update on current discussions between the authorities and the World Bank on using additional financial support for arrears clearance?

We support the authorities' efforts to strengthen the BSL and the banking sector governance. We commend the authorities for adopting the new BSL and Banking Bills, which will be helpful in promoting financial stability. In the same vein, we encourage the authorities to develop a remedial action plan to address the findings of the forensic audit of the BSL conducted by the external audit firm, and also the remaining safeguards assessment's recommendations.

With these remarks, we wish the authorities all the success.

Mr. Castets, Mr. Ronicle, Mr. Bellocq and Mr. Hemingway submitted the following joint statement:

We thank staff for their comprehensive papers and Mr. Mahlinza and Mr. Nakunyada for their informative buff. Overall the Government has demonstrated a commitment to reform which needs to be sustained and accelerated to maintain macroeconomic stability, deliver stronger growth and ensure fiscal sustainability. We support the proposed decision to complete the First Review and provide the following comments for emphasis.

Macroeconomic performance has stabilised during the program, reflecting the action taken by the authorities. This has included a welcome commitment to fiscal consolidation and action to control inflation. Nonetheless, the economic situation remains fragile, with growth remaining moderate, high inflation and a high risk of debt distress. In this context, we agree with staff that main risk facing the program is difficulty in maintaining reform momentum due to political resistance or greater than expected capacity constraints.

We emphasize the importance of prioritising reforms given this risk. While recognising the immediate fiscal and macroeconomic challenges the government is facing, we would like to see higher priority being given to the quality of reforms in terms of their impact on poverty reduction and economic diversification and growth. We also note that the government have set very ambitious objectives, so we emphasize the need for realism as well as ambition. For example, whilst we are supportive of the high level of ambition in the National Development Plan and the Government's flagship Free Quality Education Initiative, we have serious concerns about affordability. A realistic and phased approach to Free Quality Education delivery is needed, alongside a greater focus on health and education system reform to increase the extent to which investments in these areas reach intended beneficiaries and deliver improvements in outcomes.

We agree that fiscal reforms are critical to the program success. It is encouraging to see the initiatives being taken across government to tighten fiscal controls, accountability and oversight. This includes the government's commitment to follow-up on the findings of the recently conducted technical audits and the forensic audit of the BoSL, as well as planned initiatives to strengthen the integrity of the NRA and improve the functioning of internal

audit across MDAs. We hope to see clear and transparent updates on progress against these commitments going forwards in line with the programme. We note some disagreements between staff and the authorities on the appropriate revenue and expenditure paths, with the authorities reducing planned capital expenditure in the context of the program retaining a more measured revenue assumption. We agree with staff that a prudent approach, that avoids committing to an overly-ambitious spending envelope is appropriate. In addition, we would be grateful for more information on the impact the increase in estimated domestic arrears is expected to have on the fiscal strategy in the program.

We believe successful fiscal reform will increase fiscal space through a combination of domestic revenue mobilisation and more effective and efficient public spending. We note that the public deficit has been reduced more than anticipated at the program approval mostly due to underspending. We also note that the indicative target on social spending has not been met in March. Could staff indicate whether basic services delivery has been impacted by the ongoing fiscal consolidation efforts and which ministerial departments bear the brunt of the underspending? We commend the authorities for their progress in automating revenue administration and expanding the coverage of IFMIS, though note these digital solutions will only deliver their potential benefits if used correctly. We also welcome the target to raise domestic revenue, though caution that, in the current environment of constrained fiscal space, it is important these increases are sustainable and the need for immediate increases in revenues does not trump efforts to create a simplified tax system that supports sustainable inclusive growth. We would welcome staff comments on the degree to which the authorities' tax proposals address the issue of transparency and accountability and promote a fairer and more competitive business environment. We take positive note of revenue outperforming expectations in 2018, given resource mobilisation was identified as a key risk at program inception; could staff elaborate on whether they see these increases as sustainable, given both the authorities' level of ambition and the fact that much of the increase comes from non-tax sources?

Improving the efficiency and effectiveness of government spending and reducing leakages due to corruption should also be prioritised. With that in mind, we also welcome the government's commitment to undertake a public investment management assessment (PIMA) and to consult staff prior to committing to any large infrastructure financing packages. In light of the constrained fiscal space, it is important the economic and fiscal impact (including contingent liabilities) of any major projects are fully assessed.

We welcome the wider complementary CD support staff are providing to the Sierra Leonean authorities, outlined in Annex I, noting the important role CD from the IMF and World Bank has played in several of the key reforms outlined in the report. We encourage staff to continue to strengthen its coordination with other donors on the capacity development agenda. For example, there is a need to revitalise the governance structures around the Government's PFM reform strategy, which are referenced in the Memorandum of Economic and Financial Policies. These are not currently meeting on a regular basis. A regular and coordinated dialogue between the government and the donor community is important to monitor progress, identify challenges early and ensure capacity building support is well aligned to priority agendas. We would be interested in staff views on the success of CD missions to date. We would also like to know more on the timing and quantity of CD planned and the extent to which this has been coordinated with other donors, particularly given staff concerns about absorptive capacity.

The Acting Chair (Mr. Zhang) made the following statement:

The Board approved this program with Sierra Leone in November 2018. This is a very good example of how the Fund can engage effectively with fragile states and try to respond to the very real on-the-ground constraints. Since then, the country is making progress under the program, and the new government has taken steps to promote macroeconomic stability. However, Sierra Leone continues to face challenges and fragilities. In some cases, it actually suffered from a setback. As indicated in the gray statements, there is a need to focus the policies on a number of the areas, including creating fiscal space for priority spending while ensuring flexibility in response to fiscal risks. Also, efforts should be strengthened to enhance governance and accountability and, most importantly, keep the structural reforms on track.

The staff representative from the African Department (Ms. Ongley), in response to questions and comments from Executive Directors, made the following statement:<sup>2</sup>

I thank Directors for their statements. They have given us quite a bit to think about as we take our engagement with Sierra Leone forward. In addition to the written responses that were provided yesterday, I would like to address questions around three broad topics: domestic arrears, public infrastructure projects, and capacity development (CD).

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<sup>2</sup> Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

On domestic arrears, we appreciate the uneasiness that some Directors have expressed. Both we and the authorities are conscious of the risks, and the steps that we have agreed between now and the second review are intended to bring closure to this issue quite quickly.

At this stage, it is not possible to put a precise final figure on the arrears amount. What we do know is that it is likely to be considerably lower than the 14 percent that was suggested in one of the gray statements. I wanted to clarify that the 14 percent figure in Box 3 refers to the total amount of verified claims from a recent audit, and that includes both arrears and also future payment obligations. The arrears component of that also needs to be reconciled against the known stock of existing arrears, and so deducting these components will reduce the overall amount.

Until we have a final headline figure, it will be difficult to provide a realistic assessment of what the impact will be on debt sustainability and also on the program. That assessment will also depend on knowing the mix of options that the authorities will use to resolve or repay arrears.

A key element will be the amount of donor support to pay down arrears. On that score, Directors have asked about the World Bank. Our World Bank colleagues have indicated that they are considering the authorities' request for additional resources favorably. The World Bank was recently in the field on a mission to discuss this.

Support from the World Bank, however, is just going to be one element of the package. The authorities are also approaching other donors. The clearance strategy will also involve haircuts, cash allocations from the budget, as well as sub-securitization. The steps and conditionality that we have agreed upon with the authorities between now and the second review have been sequenced to give us the necessary information to make the assessment of debt sustainability. That includes finalizing the comprehensive arrears figure by end-August and also having the clearance strategy finalized by the end of September. That will inform both the Debt Sustainability Analysis (DSA) but also the 2020 budget and medium-term fiscal path.

I wanted to turn to the issue of public investment. One chair had asked about the Lungi Bridge Project. There has been quite a bit of media coverage on this. It gives the impression that the discussions are more advanced than is actually the case. The project is still in its very early stage, and the authorities are at the stage of just testing the waters with investors.

Importantly, I also wanted to emphasize that we have had quite an open and good dialogue with the authorities on this. They have reiterated several times that they are committed to pursuing non-debt financing options and also not offering public guarantees. This is important but so too is their commitment to consult with us at various steps along the way. That said, we have also cautioned them that other financing vehicles can carry risks. A number of Directors have also pointed that out in their gray statements.

Fortunately, just this past week, the authorities asked us for a note on the potential pitfalls of different financing options and the lessons from experiences in other countries. From their perspective, the idea is to have something in their back pocket before their discussions become more concrete.

On the question of the implementation of projects, the planned Public Investment Management Assessment (PIMA) that the Fund will conduct hopefully later this year or early next year will be instrumental in gauging their overall implementation capacity but also in laying the foundation for improved public investment efficiency. More broadly, as capital projects move forward, it will be vital that the main agencies involved—and that is the president’s infrastructure initiative team, the public-private partnership (PPP) unit, and the Ministry of Planning and Economic Development—coordinate closely on these issues.

Finally, I wanted to touch on the issue of CD. We welcome the questions that Directors have raised here. They reflect the importance of integrating our CD work with both our surveillance and our program work. Annex I of our report is a collaborative product, and it reflects the discussions that we have had with the authorities on forward-looking CD priorities. But several of the questions that were raised touch on other dimensions that are broader than Sierra Leone, and we welcome those questions. What we plan to do is to consult with colleagues in the Institute for Capacity Development (ICD) and think about how to take this forward in the context of plans to implement the CD strategy that the Board recently approved.

Coming back to Sierra Leone-specific issues, it is a large consumer of CD, and that reflects its large needs. However, from our perspective, we are also mindful that absorptive capacity will be a watch point, so we are keeping that in mind as we continue our dialogue with the authorities.

The authorities' large needs also mean that they are working with other donors, so there is a premium for us on coordinating with other donors. That is a point that Directors raised. We do have a good working relationship with development partners on both the content and timing of our CD, and our Resident Representative office plays a critical role in that. She participates in monthly meetings with donors and the authorities.

Finally, on the issue of CD, the CD that the Fund is delivering is well aligned with the program goals. We can see that and the payoffs in terms of things like tax administration, public financial management (PFM), and also the support in drafting the recently approved central banking law. But the consultative process between the team and CD-providing departments also means that we have been able to respond flexibly to emerging priorities. The upcoming PIMA assessment is a good example of that, which was not originally slated for this year, but we have been able to bring that forward.

Ms. Florestal made the following statement:

We commend the Sierra Leonean authorities for keeping on track with program commitments under the Extended Credit Facility (ECF), despite multi-faceted challenges. We note the ad hoc nature of the revenue performance, largely held by non-tax resources. We regret that fiscal targets were met by underspending on poverty reduction, which led to the missing of the corresponding indicative targets at end-March 2019. The focus of the national development plan on the high poverty rate and rapidly growing population, among other key issues, is welcome.

All three unmet structural benchmarks required more complex steps to be achieved. They are now programmed to be completed through the adoption of incremental steps and after the provision of expert advice. The adoption of a measured incremental step approach is welcome. Nonetheless, we are disappointed that this was not the case when starting the program.

We take note of the staff's engagement to apply greater realism in implementation. We encourage Fund staff to make more effort to comprehend ex ante what is required to achieve large and/or difficult structural measures. We understand that the net domestic assets (NDA) of the Bank of Sierra Leone (BSL), a quantitative performance criterion (QPC) was not met at end-2018 partly because the authorities had recourse to the BSL to bridge donors' delayed delivery of budget support. The corrective actions taken by the authorities are welcome. But like other Directors, we remain concerned about delays in donor disbursements during the upcoming fiscal year, despite

the fact that those delays are qualified by Fund staff as procedural in nature. Hence, we question whether the US\$20 million cap on the adjustor for shortfalls in donor support should not have been higher. We have yet to be convinced that a superior adjustor would not have been a superior course of action than the borrowing from banks at market rate to meet the NDA target, as suggested in Box 2.

The progress made on the governance framework of the BSL and in strengthening the governance of the banking sector is to be commended. We concur with the staff that putting the two public banks on a solid commercial footing remains a key priority. We note, however, that the profitability of banks has substantially increased, but the situation of nonperforming loan (NPLs) has also deteriorated, although unequally across the banking system. Could the staff elaborate on the reason behind the deteriorations?

We support the conclusion of the first review of the ECF and the waiver for the unmet QPC. Going forward, new QPCs and structural benchmarks (SBs) have been proposed for end-December. We hope that they sufficiently consider the challenges revealed thus far. In addition, we find that the wording of the structural benchmark on the National Revenue Authority Act does not bode well with country ownership. It would have been more appropriate to request that the authorities share the draft with Fund staff prior to Cabinet review and ensure that it is in line with whatever the Fund is concerned would be or would not be included in that act.

A US\$100 million limit was put on the contracting of new external debt in 2019. The relationship between the title of Annex I and its content is hard to decipher. That said, while acknowledging the high risk of debt distress in Sierra Leone, we encourage the Fund to help the authorities find the appropriate balance between avoiding a worsening of the debt situation and accessing the needed funds to boost growth and achieve development.

Mr. Castets made the following statement:

We issued a joint gray statement with Mr. Ronicle in which we support the authorities' request for the completion of this first review, and we commend the authorities for the progress made in macro-economic stabilization.

I have to say that when we approved the program six months ago, we expressed some doubts regarding the feasibility of the frontloaded fiscal consolidation expected under the program in a country as fragile as Sierra

Leone. The authorities were at the time expected to implement a spending cut amounting to 2.5 percent of GDP between 2018 and 2019, which was quite elevated in a context in which the country was still facing a very high level of social and development needs.

We note today that the public deficit has been reduced even more rapidly than anticipated at the program approval, mostly due to underspending. I must say that, in our view, there is still some doubt regarding the sustainability of and the pace of the spending cut in a low-income country (LIC) such as Sierra Leone. In this regard, we have some concerns regarding the medium-term sustainability of such a fiscal adjustment.

We believe that fiscal consolidation has to rely as much as possible on domestic resource mobilization, in particular, in resource rich countries. In that regard, there has been limited progress since the beginning of the program.

As underlined in our joint gray statement, we see that the indicative target on social spending was not met in March. We wondered, in our questions, whether basic services were impacted by the fiscal consolidation effort. The staff's answer is reassuring, but we would call staff's attention to whether a fiscal consolidation of this magnitude can really be painless because it would certainly set a precedent. We had precedents where, in the first steps of the program implementation, the staff was also very reassuring regarding the impact of the fiscal consolidation, and we discovered afterwards that there was a social cost.

Finally, I thank the staff for the detailed answer on CD. We believe it is an extremely important dimension in a fragile country.

Mr. Ronicle made the following statement:

Per capita GDP in Sierra Leone stands at about US\$550 per head. It ranks sixth-lowest on the World Bank's Human Capital Index. The Fund has been engaged more or less continuously since the end of the civil war in 2002. This is the second ECF since the end of the Ebola outbreak since 2016, with the 2017 program having rapidly gone off track. Sierra Leone is clearly a fragile state, and we welcome the depth of Fund engagement here.

We welcome the government's commitment to reform and the stabilization achieved to date and urge the authorities to keep up the pace of change. We support the completion of the first review.

Mobilizing revenue is one of the key objectives of this program, and fiscal slippages were one of the principal reasons the 2017 program went off track. We were, therefore, pleased to see strong revenue performance in 2018 and are encouraged that the staff believe the reforms planned in revenue administration will help sustain strong revenues. That being said, a large share of the increase in revenues in 2018 was accounted for by non-tax sources. Could the staff elaborate on what these are and whether the pickup in them is likely to persist?

The staff's clarification on the arrears process was very helpful, and we look forward to seeing the revised DSA for the second review.

Given the priority we place on lifting people out of poverty, we were reassured by the staff's answers on pro-poor spending and the protection of basic services, despite the 2018 under-spend, though like Mr. Castets, we believe there is a need for vigilance in this area. It seems appropriate to us that the capital spending baseline over the program has been reduced somewhat, given the risks around project selection, including the airport connector bridge project. We hope the forthcoming PIMA mission will help address capacity issues in this area.

Finally, turning to CD, while the annex provided in the report was helpful, we felt it could have offered more details, not least given how important CD is to Sierra Leone and the program. In particular, we would have been keen to see a more detailed plan that linked missions to program objectives, set up the sequencing of missions, and detailed our engagement with other providers. I thank the staff for the comments this morning, which addressed our concerns, but I would encourage the staff to consider including a bit more details in the report in the future.

Mr. Razafindramanana made the following statement:

We have issued a gray statement in which we expressed our full support for the completion of the first review under the ECF arrangement. I would like to limit my comments to a few points.

We commend the Sierra Leonean authorities for their commitment to program objectives and the progress made to reduce macroeconomic imbalances and put the program back on track. Going forward, tackling the risks and vulnerabilities stemming from their limited capacity and the still

high debt levels warrant the pursuit of continued policy reforms to preserve macroeconomic stability and accelerate the pace of structural reforms.

On the fiscal front, as noted by many Directors, the authorities should continue with their fiscal consolidation efforts through further revenue mobilization and better expenditure controls to support their development and social needs. The authorities' planned PIMA to enhance public investment is a welcome step that will be central to aligning investment priorities with the budget framework.

On the debt issue, we commend the authorities for the notable improvements in their debt management. We encourage them to continue to rely as much as possible on highly concessional loans and grants for their financing needs and to step up their efforts to finalize the medium-term debt management strategy to help keep the debt sustainable.

Finally, efforts to maintain the inflation on a declining path should continue, with the aim to attain the authorities' single-digit objective, as well as further allowing exchange rate flexibility and the accumulation of buffers to foster macroeconomic stability and external balance.

With these comments, we wish the authorities all the best in continuing to implement the ECF-supported program.

Mr. Sigurgeirsson made the following statement:

I appreciate Ms. Ongley's comments on technical assistance (TA). In recent discussions on fragile countries, we have brought up the issue of CD and absorptive capacity. A lack of sufficient capacity to absorb Fund TA has been a common thread in many recent country cases, and in some cases, it appears that TA has taken a life of its own. I appreciate the annex in the report on CD. It even mentions risks, including capacity constraints, and suggests mitigating factors. But as Mr. Ronicle mentioned, we can always ask for more, and things could be fuller. For example, it would have been helpful to have a better picture of the scale of TA provided for comparison reasons. We have had recent cases of countries where we have had 50 TA missions within a year. I am not saying that that is the case here, but sometimes that happens. Some recent reports have provided itemized lists of TA, and it would be helpful to see such lists in annexes in more reports so that stakeholders have a better understanding of the TA provided.

On strengthening the banking sector, what we see is very important, and we note that the structural benchmark on developing a strategic plan for the two state-owned banks was missed and proved to be more complex and dependent on expert advice than anticipated. We thank the staff for the clarification in the written answers on the banking system. We are pleased to see that the World Bank has been engaged in conducting targeted diagnostics of the banks by the end of September. It is promising to see an example of constructive cooperation with the World Bank and a clear delineation of our work streams.

A well-functioning banking system and enhanced financial intermediation will be key to improving the business environment and facilitating growth. We urge the authorities to complete the work that has started.

Mr. Etkes made the following statement:

We issued a joint gray statement with Mr. Psalidopoulos, and we would like to highlight the important role of country teams in setting the CD priorities and, when it is possible, even to evaluate the impact of past CD projects.

Indeed, the African Department (AFR) is nicely experimenting with the integration of surveillance and CD. We now have at least six cases where these kinds of annexes have been added to the country reports, and we can see which one is better and what the advantages are for each one of them.

We note that the country team's CD priorities in their report were endorsed by Ms. Levonian, Mr. Inderbinen, and a few more colleagues. In total, eight chairs supported these priorities. We hope that the Summing Up will include an explicit reference to the Board's support for these priorities. It could signal to the Institute for Capacity Development (ICD) that the Board is supportive of the priorities and the integration between CD and surveillance.

The staff representative from the African Department (Ms. Ongley), in response to further questions and comments from Executive Directors, made the following additional statement:

On the issue of NPLs and the banking system, I just wanted to clarify that NPLs are actually declining, both in the banking system on average but also for the two state-owned banks. For the state-owned banks, it is largely a reflection that, for the last several years, they have been under enhanced

supervision by the BSL, pending a decision on what the future steps are for them.

Mr. Ronicle asked the staff to elaborate on the non-tax revenue increases and whether they were sustainable.

The staff representative from the African Department (Ms. Ongley) responded that non-tax revenues were mainly a reflection of the Treasury Single Account, and a significant amount of the non-tax revenues were being channeled through that.

Ms. Florestal remarked that Table 8 did not reflect the slight increase in NPLs.

The staff representative from the African Department (Ms. Ongley) responded that there had been an increase from 12.6 to 12.7 percent. The level had been hovering around 12.6 to 12.8 percent for the past few quarters.

Mr. Mahlinza made the following concluding statement:

I thank Directors for their support for the completion of the first ECF review for Sierra Leone. Directors' constructive views and policy recommendations are highly appreciated and will be faithfully conveyed to the authorities.

My authorities remain committed to the steadfast implementation of reforms under the ECF to further entrench macroeconomic stability, tackle structural impediments, boost growth, and uplift living standards. As such, they view the Fund's program, which is aligned with the key objectives of the new national development plan, as an important instrument to anchor their reform agenda.

Consistent with the calls from Directors, the authorities are committed to sustaining current fiscal consolidation efforts to place public debt on a sustainable path. Accordingly, they are pursuing several aggressive domestic revenue mobilization and expenditure control measures to further reduce their fiscal deficit and create fiscal space to pay down domestic arrears and finance priority investment and social expenditures.

Under the medium-term debt strategy, they are planning to pursue responsible borrowing by prioritizing non-debt-creating financing models, including PPPs and build-operate-transfer arrangements. Our authorities are also committed to discussing with the Fund any large infrastructure financing packages.

In addition, work has advanced to finalize a combination of the headline arrears amounts. Enhanced commitment controls are expected to prevent the accumulation of new arrears.

On inflation, the authorities stand ready to further tighten monetary policy, and they look forward to the Fund's TA to help develop market-based monetary policy instruments to improve monetary policy effectiveness. At the same time, they will soon commence foreign exchange auctions to help build external reserves while limiting foreign exchange interventions to smoothen disorderly market conditions. Moreover, the recent passing of the BSL Act by Parliament is expected to strengthen governance and the operational autonomy of the BSL.

In their gray statements, Directors emphasized the need to accelerate the implementation of structural reforms. Our authorities remain committed to advancing the structural reform agenda.

As indicated in our buff statement, the BSL forensic audit report was finalized. The BSL is already leveraging low-hanging fruits, including tightening security, strengthening internal controls, and enhancing IT security features by restricting user access rights. At the same time, they have agreed with the World Bank on the terms of reference for a diagnostic study on the two state-owned banks, and work is expected to commence in July. Based on the findings of this study, the authorities are planning to adopt an effective strategic plan that will help place these banks on sound commercial footing.

In conclusion, I would like to restate the authorities' appreciation of the Fund's policy guidance and CD to help address the underlying economic challenges. They look forward to continued Fund support to help anchor reforms, entrench macroeconomic stability, improve fiscal and debt sustainability, and build adequate reserve buffers.

Finally, I thank the mission chief, Ms. Ongley, and her team for their constructive engagement with my authorities and for responding to the issues raised by Directors. We also appreciate her constant outreach to our office. My Sierra Leonean authorities value the Fund's advice and TA and look forward to further collaboration in implementing the ECF.

The following summing up was issued:

Executive Directors welcomed the progress that Sierra Leone has made under the ECF-supported program despite the difficult environment. However, they noted that underlying fragilities and capacity constraints pose challenges to the economic outlook. Directors welcomed the authorities' commitment to their reform agenda, including the National Development Plan (NDP), and emphasized that policy priorities ahead should focus on securing macroeconomic stability, building policy buffers, and fostering sustainable and inclusive growth.

Directors noted the authorities' focus on achieving fiscal and debt sustainability while enhancing the needed infrastructure and social spending. In this regard, they called for continued fiscal consolidation efforts, especially focusing on domestic revenue mobilization (DRM) and recurrent expenditure restraint. Directors also recommended using any higher than expected revenues to support priority spending.

Directors emphasized the need to maintain the momentum of reforms in order to tackle fiscal risks. Priority should be given to strengthening revenue administration and policy reforms and enhancing public financial management, which will help support good governance, improve expenditure control, and avoid emergence of new arrears. Stronger public investment management, including undertaking a Public Investment Management Assessment by the Fund, would help support the authorities' ambitious infrastructure plans. Directors called for quick actions to complete the arrears stocktaking and related clearance strategy. They looked forward to the authorities' new Medium-Term Debt Management Strategy that draws on technical assistance from the Fund. Directors emphasized that strengthening debt management capacity and giving priority to non-debt creating financing of infrastructure projects is critical for debt sustainability, while cautioning that the latter can also carry fiscal risks.

Directors emphasized the importance of a tight monetary policy stance aimed at bringing down inflation. They also noted the progress made on developing indirect instruments to enhance the effectiveness of monetary policy. Directors underscored that greater exchange rate flexibility and reserve buffers are important to bolster the economy's resilience to external shocks. They encouraged the authorities to refrain from undue foreign exchange intervention. Directors highlighted that continued steps to strengthen the governance framework of the Bank of Sierra Leone (BSL) and to address the findings from the recently completed forensic audit would enhance the BSL's accountability and operational effectiveness.

Directors emphasized that structural reform efforts should give priority to reducing poverty, protecting vulnerable segments of the society, improving the business environment, diversifying the economy, and unlocking Sierra Leone's growth potential. Directors welcomed the alignment of the Fund's capacity development activities with the authorities' reform agenda.

The Executive Board took the following decision:

**Sierra Leone—First Review Under the Extended Credit Facility Arrangement, Request for a Waiver of Nonobservance of Performance Criterion, and Financing Assurances Review**

1. Sierra Leone has consulted with the Fund in accordance with paragraph 4A(b) of the arrangement for Sierra Leone under the Extended Credit Facility (ECF) (EBS/18/99, 11/19/2018) (the "ECF Arrangement") to review program implementation and to reach understandings regarding the conditions for further disbursements.
2. The letter dated June 10, 2019 from the Minister of Finance and the Governor of the Bank of Sierra Leone (the "June 2019 Letter") together with its Memorandum of Economic and Financial Policies (the "June 2019 MEFP") and the Technical Memorandum of Understanding (the "June 2019 TMU") shall be attached to the ECF Arrangement, and the letter dated November 14, 2018 from the Minister of Finance and the Governor of the Bank of Sierra Leone, together with all of its attachments, shall be read as supplemented and modified by the June 2019 Letter and its attachments.
3. Accordingly, the ECF Arrangement for Sierra Leone shall be amended as follows:
  - a. A new paragraphs 2(d) shall be included in the ECF Arrangement to read as follows:

"2(d) the fourth disbursement, in an amount equivalent to SDR 15.555 million, will be available on or after June 1, 2020, at the request of Sierra Leone and subject to paragraphs 4 and 5 below."
  - b. Paragraph 4.A(b) shall be amended, with respect to the third disbursement, to replace the references to "paragraph 60 of the MEFP" with "paragraph 48 of the June 2019 MEFP"

c. A new paragraph 4.B of the ECF Arrangement shall be inserted to read as follows:

“4.B. Sierra Leone will not request the fourth disbursement under this arrangement specified in paragraph 2(d) above:

(a) if the Managing Director of the Trustee finds that the data as of December 31, 2019 indicate that:

(i) the ceiling on the net domestic bank credit to the central government; or

(ii) the ceiling on net domestic assets of the Bank of Sierra Leone; or

(iii) the floor on the gross international reserves of the Bank of Sierra Leone; or

(iv) the ceiling on the new concessional external debt with original maturity of one year or more contracted or guaranteed by the public sector;

as set out in Table 1 of the June 2019 MEFP and further specified in the June 2019 TMU was not observed; or

(b) until the Trustee has determined that the third program review, referred to in paragraph 48 of the June 2019 MEFP, has been completed.”

d. The continuous performance criteria set forth in paragraphs 5(a), 5(b) and 5(c) shall be as specified in Table 1 of the June 2019 MEFP and further specified in the June 2019 TMU.

e. A new paragraph 5(e) of the ECF Arrangement shall be inserted to read as follows:

“, or (e) until the Trustee has determined that, with regard to each disbursement and for so long as Sierra Leone has outstanding sovereign external payments arrears to private creditors, a financing assurances review has been completed.”

4. The Fund decides that the first review specified in paragraph 4.A.(b) and the financing assurances review specified in paragraph 5(e) of the ECF Arrangement are completed, and that Sierra Leone may request the second disbursement referred to in paragraph 2(b) of the ECF Arrangement, notwithstanding the nonobservance of the end-December 2018 performance criterion on the ceiling on net domestic assets of the Bank of Sierra Leone, specified in paragraph 4.A(a)(ii) of the ECF Arrangement, on the condition that the information provided by Sierra Leone on the performance under this criterion is accurate. (EBS/19/54, 6/14/19)

Decision No. 16546-(19/56), adopted  
June 28, 2019

APPROVAL: July 30, 2020

JIANHAI LIN  
Secretary

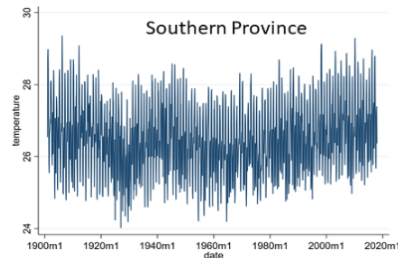
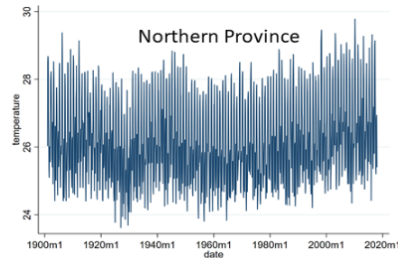
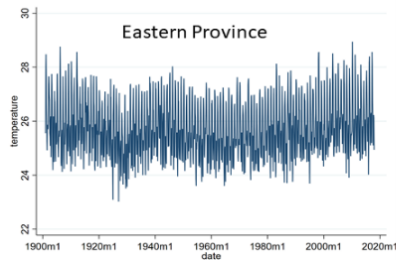
## Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

### Outlook and risks

1. ***We are somewhat surprised by staff's risk assessment. First, climate fluctuations and climate change may affect Sierra Leone /.../ In addition, according to recent events it seems that global monetary tightening is not expected in the next few years. Staff's comments are welcome.***
  - In evaluating risks, staff considered climate change. For example, we analyzed temperature changes in Sierra Leone at the provincial level at monthly frequency for the past 120 years (see charts). Average temperatures have been rising for 4 decades and this is certainly a long-term challenge. On balance, we felt that Sierra Leone faces more pressing immediate risks that were higher priority for inclusion in the RAM. The risk of tightening global financial conditions reflects the risk presented in the latest G-RAM. Sierra Leone's RAM will be updated for the next review, in line with any updates to the G-RAM.

Average Temperature in the Last Century  
Sierra Leone at Provincial Level  
(excluding Freetown)



### Donor budget support and fiscal policy

2. ***We note the budget support shortfalls in 2018 had affected planned government programs including infrastructure investment. What were the underlying reasons for the shortfall and what assurances are there to ensure planned budget support for 2019 are disbursed on time?***

3. *Can the staff expand on what is driving lower donor support and the prospects for attracting further concessional financing for infrastructure and social spending?*
4. *We note that the authorities adjusted the public expenditures to address delays in the expected budget support. We wonder whether the program design could help the authorities to address this issue going forward. Staff's comments are welcome.*
5. *Could staff indicate whether basic services delivery has been impacted by the ongoing fiscal consolidation efforts and which ministerial departments bear the brunt of the underspending?*
  - Given the procedural nature of delayed World Bank and AfDB budget grants, we do not see substantive reasons to be concerned about future disbursements. Nevertheless, the program assumptions are cautious in the near- and medium-term. Despite more certainty of disbursements by the end of this year, the program assumes disbursement of the next World Bank budget support in early 2020 (rather than late 2019). For the outer years, where there is less certainty, the program assumes a moderate decline in support by development partners as a share of GDP. This is consistent with the authorities' aspirations of decreasing their reliance on external support by mobilizing domestic revenue.
  - The tighter fiscal stance has not had a major impact on the delivery of basic services. Underspending was implemented largely by holding back expenditure on capital projects and an across-the-board disciplined approach to discretionary expenditure (e.g., staff travel, office improvements, vehicle procurement). In the short run, staff will continue to encourage the authorities to prioritize critical expenditure if disbursements by development partners are delayed. The cautious assumptions on support by development partners also allow for careful budget planning, limiting the risk of unnecessary disruptions to infrastructure and social spending.

### **Revenue reform**

6. *We would welcome staff comments on the degree to which the authorities' tax proposals address the issue of transparency and accountability and promote a fairer and more competitive business environment.*
7. *We take positive note of revenue outperforming expectations in 2018, given resource mobilization was identified as a key risk at program inception; could staff elaborate on whether they see these increases as sustainable, given both the authorities' level of ambition and the fact that much of the increase comes from non-tax sources?*
  - Revenue reform efforts have focused on improving administration and transparency. Examples include implementing the Treasury Single Account (largely reflected in improved "non-tax" revenue), and the suspension and review of duty exemptions.

The ongoing upgrade to a new tax information system (ITAS) will also help enhance compliance. Looking ahead, plans to modernize the governance of the National Revenue Authority (NRA) and amend the NRA Act will also promote accountability. Consistent tax enforcement will not only sustainably raise revenue but also reduce uncertainty and strengthen the business environment.

- The authorities are aware that maintaining reform momentum is crucial—both to “lock in” the gains achieved so far and provide a foundation for further progress (including more emphasis on policy reforms). The program cautiously relies on a revenue mobilization assumption more conservative than the authorities’ stated medium-term goal. We encourage their ambitions and, should revenue overperform, that could be used to increase the envelope for infrastructure and social spending.

### **Domestic arrears and debt sustainability**

8. *It is hard to understand the huge discrepancies in arrears figures, which are described in Box 3. The initial figure of arrears was 4 percent of GDP when the ECF was requested, and today’s potential figure is up to 14 percent of GDP/.../ The magnitude of the fiscal liability and associated risks with this level or arrears are too high, therefore, we would like to hear from staff whether these outcomes put the completion of the program at risk.*
9. *We would be grateful for more information on the impact the increase in estimated domestic arrears is expected to have on the fiscal strategy in the program.*
10. *Could the staff clarify how the uncertainty about the level of arrears is impacting the program parameters and the private sector in general and provide an update on current discussions between the authorities and the World Bank on using additional financial support for arrears clearance?*
11. *We note that the government is discussing with the World Bank the possibility of scaling up budget support to US\$ 100 million, of which US\$ 60 million would be used to clear arrears. Could staff discuss the alternatives in case the discussions do not produce the desired support?*
12. *As the “inability to clear and prevent new arrears poses a sizeable risk to securing debt sustainability”, we would have appreciated an update on the risk of debt distress. Staff’s comments are welcome.*
  - Staff will respond to these questions during the Board meeting
13. *With regard to domestic arrears, the buff stated that the “IMF assistance is expected to help ascertain the scope for securitization.” We welcome staff’s elaboration on it.*

- The Fund is providing TA in two complementary areas. One, FAD provided comprehensive advice to support efforts to determine the final stock of existing arrears and to prevent new arrears by strengthening expenditure controls. The authorities are now finalizing the arrears figure. Two, MCM TA focuses on formulating a strategy for resolving and clearing arrears (via a mix of donor financial support, hair-cuts, securitization etc.), as well as actions to enhance debt management.

#### **Public investment and infrastructure needs**

14. *Could the staff comment on the Presidential infrastructure initiative (including a recently announced tender for up to \$2 billion for an airport connector bridge) and whether the PPP unit and the Ministry of Planning's public investment unit have adequate capability to manage this large-scale investment, without crowding out other worthwhile investment projects? Also, can staff offer preliminary comments on the possible impact on debt sustainability?*
- Staff will respond to this question during the Board meeting

#### **Monetary policy and conditions**

15. *While we are comforted by the authorities' commitment under the program to reduce domestic bank borrowing to around 2 percent of GDP, could staff clarify why banks' appetite for T-bills is declining?*
- Banks' limited appetite for T-bills is most noticeable at the short end of the maturity profile. This likely reflects the very steep yield curve of T-bills with 3- and 6-month T-bills at 7-8 percent compared to above 20 percent for one-year T-bills. This impacts the government's ability to use shorter-term T-bills to smooth liquidity pressure, for instance, in response to delays in donor support.
16. *Given the high degree of fiscal dominance apparent in the regular recourse to bridge loans from the BSL to finance budgetary shortfalls, and the resort to scarce foreign exchange reserves to counter depreciation pressures, we would be interested in staff's view whether the new BSL Bill can effectively ensure an adequate level of central bank independence in Sierra Leone. Does staff propose additional measures in this regard?*
- The new BSL Act, developed with the benefit of Fund TA, received Presidential assent last week. The Act establishes the legal framework for the BSL to independently exercise its functions. The priority now is to ensure the new law is implemented effectively.
  - The ECF also supports a number of other reforms to strengthen the BSL's governance and operational effectiveness. These include: (i) implementation of the safeguards recommendations; (ii) the forensic audit and forthcoming remedial action plan to address its findings; and (iii) NDA targets to limit BSL financing to the government.

All these should help strengthen BSL's internal controls and procedures, and build trust in the BSL's integrity.

**17. *We wonder how can BSL improve the transmission mechanism of monetary policy? We welcome staff's elaboration.***

- While money aggregates continue to be the monetary policy operating target, the BSL has adopted a multipronged approach, supported by IMF TA, to improve the transmission mechanism including (i) developing indirect instruments; (ii) improving money markets; and (iii) enhancing BSL's analytical capacity and liquidity management. This is complemented by the goal of the ECF-supported program to bring government's domestic bank borrowing down to 2 percent of GDP over the program period, which will lessen the impact of large government borrowing on the conduct of the monetary policy. Staff plans to look more closely at this issue during the coming Article IV consultation.

**18. *We take into consideration the authorities' concern of higher depreciation of the domestic currency if the BSL proactively accumulate reserves, and its impact of inflation. We would appreciate further details from staff on the pass-through process in Sierra Leone.***

- Imports account for around 30 percent of GDP and over 70 percent of the CPI basket is either directly or indirectly import-based, therefore, the pass-through of exchange rate depreciation on inflation is significant. Having said that, to attract foreign investment and trade flows, and to help limit vulnerability to external shocks, the BSL needs to shore up its FX reserves buffers. FX reserves in months of import coverage declined from 4.2 in 2016 to 3½ in 2018. The program aims to strike a balance by maintaining reserve buffers and, to this end, the authorities should limit FX sales to smoothing excessive volatility.

**19. *Can the staff elaborate on the approach to supporting gradual reserve accumulation during the program, as we note the quantitative targets have reserves falling over the next several quarters and a modest increase at year end.***

- The quarterly reserve target path is based on the projected quarterly FX cashflow. This reflects the seasonality of cashflows, with inflows typically higher in the latter part of the year. In addition, the modest increase of the year-end reserve target reflects staff's policy advice for the BSL to start FX purchase auctions, while limiting FX sales to smooth excessive volatility.

## **Financial sector**

**20. *Could the staff elaborate more on the situation of the delayed forensic audit of BSL? What is the main takeaway from the audit report, which is due to publish by end-August 2019?***

- The delay was procedural. The data for the forensic audit process required substantially more manual processing than originally anticipated, adding around 6 weeks to the audit process. Key recommendations relate to upgrading IT systems and physical security that require urgent remediation. The forensic audit report also noted several control failures which point to the need to improve the effectiveness of oversight by the BSL’s Audit Committee. In addition, the report identified a number of transactions that need further investigation to fully understand their potential impact, if any. While the BSL has already started to address some of the control weaknesses, the remedial action plan (structural benchmark for end-August) will need to establish a timebound strategy to address all the findings.
21. ***We call on the authorities to work towards setting state-owned banks on a firm commercial and financial footing. Could staff comment on the merits of privatizing said banks?***
22. ***With regards to the two state-owned banks, could staff elaborate on the preliminary prospects for privatization?***
23. ***We would appreciate staff comments on the privatization of these two banks to address the fiscal risks and foster the development of a sound banking system.***
- The most important consideration in dealing with the two state-owned banks is to limit fiscal risks. Encouragingly, immediate fiscal risks have abated since the introduction of enhanced supervision in 2016, as the two banks have become profitable and capital adequacy has strengthened.
  - Independent from privatization considerations, the planned diagnostic report, with technical assistance by the World Bank, will provide the necessary information for the government to take a decision about how best to make the two banks commercially viable.
  - In deciding the path forward, including on ownership, the authorities will need to weigh other factors. For instance, the role of the two banks’ unique networks in rural areas in meeting the needs of the otherwise under-served population, and possible difficulty in finding strategic investors given the small market and the two banks’ large size may be considerations against privatization.

### **Structural issues**

24. ***We would welcome information on any good models or lessons from peers who have successfully implemented an education-focused strategy.***
- While there is no silver-bullet strategy, the 2018 World Development Report “Learning to Realize Education’s Promise” highlights the following three ingredients for successful education reform: (i) Assessing, measuring and tracking learning through credible and reliable data and solid monitoring systems; (ii) Using evidence

to guide innovation and practice, based on a vast amount of accepted studies; and (iii) Aligning actors to tackle competing interests of players and technical barriers in systems that are complex due to, e.g., a large number of actors and interdependence of reforms (e.g. links between health, infrastructure and education programs).

### **Fund engagement and program design**

25. *The ECF program ended in 2018 and this review is about a successor program after that. What were the main lessons from the previous one, good or bad? How were those lessons incorporated in the current program? Can staff highlight the main differences between the two programs?*
- The previous arrangement was short-lived, going off-track before the early 2018 election. Nevertheless, the core goals of that program—revenue mobilization, building reserve buffers, bringing down inflation—remain valid. After coming to power, the current government adopted much of that reform agenda, which has been incorporated in this program. A key lesson is that political economy and the political cycle play an important role. This also demonstrates the importance of the authorities’ ownership of the program goals, which we believe is quite strong.
26. *We would be interested in a stock taking of structural benchmarks that in retrospect proved to be overly ambitious in design and/or needed technical assistance and additional time to complete.*
- Staff does its best to set timelines for structural benchmarks that are realistic and that also achieve macro-critical reforms as quickly as possible. For some reforms, it can be difficult to estimate ex ante how long it will take to complete the reform. In cases where the initial timetable is revealed to be unachievable despite good efforts by the authorities, staff aims to adjust program conditionality accordingly, as has been done in Sierra Leone. In terms of stocktaking, one lesson from the recent Review of Conditionality is that staff should apply greater realism in implementation timetables. Staff continues its efforts toward achieving this objective, including in the revised structural reform timetable in the Sierra Leone program.
27. *We would be interested in staff’s view on measuring program performance in fiscal borrowing from the BSL by flows rather than stocks.*
- The two BSL bridge loans since the start of the program have been used to smooth liquidity constraints due to procedural delays in budget support. As current conditionality is set based on cumulative flows, consistent with stocks and accounting for the starting point, there has not been a material difference between stock and flow concepts in terms of their implication of compliance to conditionality (the authorities missed the end-December NDA target). At this stage, we do not see a need to change the conditionality based on the authorities’ commitments to monitor more closely

adherence to program targets. However, we may revisit conditionality in the future based on program performance.

**28. *Concerning the IT on poverty-related spending, could staff elaborate in which way the absorption capacity of the poor became a binding constraint for the authorities?***

- The authorities are committed to reducing poverty. Safeguarding pro-poor spending remains essential, especially since poverty rates have not yet returned to pre-Ebola levels. Poverty-related expenditure in Sierra Leone is not always smooth, with stronger execution in some quarters than in others. While this reflects structural challenges in budget execution common in low-income and fragile economies, the authorities' overall focus on pro-poor spending remains appropriate.

### **Capacity development and technical assistance**

**29. *While we appreciate the information in Annex I, for future reports, we would like to see more detailed information on capacity development strategies, such as timing and sequencing, and potential coordination with other organizations.***

**30. *We would appreciate staff comments on the need and sequencing for technical assistance in relation to other medium-term objectives under the authorities' NDP for accelerating growth and reducing poverty.***

**31. *We encourage staff to complement the annex with information on past TA and training of officials by topic, assess if past CD activities were effective, and spell out priorities for training. Finally, staff could also relate CD activities to the program criteria and benchmarks. Staff's comments are welcome.***

**32. *We would be interested in staff views on the success of CD missions to date. We would also like to know more on the timing and quantity of CD planned and the extent to which this has been coordinated with other donors, particularly given staff concerns about absorptive capacity.***

- Staff will respond to these questions during the Board meeting.