

BUFF/07/180

December 21, 2007

**The Acting Chair's Summing Up
Democratic Republic of São Tomé and Príncipe—
Fifth Review Under the Poverty Reduction and Growth Facility and
Request for Waiver of Performance Criterion
Executive Board Meeting 07/112
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Executive Directors welcomed São Tomé and Príncipe's good performance under the PRGF-supported program. Economic activity has remained robust, inflation has fallen significantly, the domestic primary deficit is contained, and official reserves exceed the program target. Directors commended the authorities for raising the domestic prices of petroleum products and utilities to reflect the rising oil import costs. They noted, however, that the rapidly growing public sector wage bill complicates program implementation and could jeopardize medium-term fiscal sustainability, especially within the context of uncertain oil revenue.

To consolidate the stabilization gains and safeguard fiscal sustainability, Directors encouraged the authorities to continue to improve public financial management and to further reduce the domestic primary fiscal deficit in 2008. In particular, Directors emphasized the importance of containing personnel costs and non-priority expenditure, protecting social and infrastructure spending, and pressing ahead with the direct taxation reforms to reduce distortions and broaden the tax base.

Directors noted that inflationary pressures remain, and welcomed the authorities' commitment to reducing inflation using base money as the anchor under a flexible exchange rate regime. They encouraged the authorities to continue their proactive monetary policy to curb liquidity growth, while stressing that this policy will need to be backed by continued fiscal adjustment. Directors supported the authorities' plans to deepen the foreign exchange market, put in place an anti-money laundering regime, and further strengthen banking supervision.

Directors emphasized the importance of accelerating structural reforms, particularly to stimulate private sector-led growth, strengthen fiscal performance, and diversify the economy to improve its resilience to shocks. Improving the business climate, particularly by reducing administrative costs and delays in starting a business, should be a high priority. Directors welcomed the authorities' efforts to further strengthen the institutional framework for transparent management of oil exploration and receipts, including the adoption of

legislation consistent with the Extractive Industries Transparency Initiative. They encouraged the authorities to upgrade the country's infrastructure, accelerate reforms in key economic sectors, and pay due attention to structural problems in the labor market.

Directors noted that São Tomé and Príncipe's medium-term economic outlook depends critically on the prospects for oil exports and revenue. As these prospects remain uncertain at present, Directors underscored the need for continued prudent fiscal and external financing strategies. They encouraged the authorities to further improve debt management, and to refrain from new external borrowing on non-concessional terms so as to ensure long-term debt sustainability. Directors also encouraged the authorities to maintain a constructive dialogue with the country's creditors, with a view to concluding bilateral agreements with the remaining creditors on terms comparable with those of the HIPC Initiative.