

**FOR
AGENDA**

EBD/10/29
Correction 1

June 15, 2010

To: Members of the Executive Board
From: The Secretary
Subject: **Chad—Poverty Reduction Strategy Paper—Joint Staff Advisory Note**

The attached corrections to EBD/10/29 (5/3/10) have been provided by the staff:

Factual Error Not Affecting the Presentation of Staff's Analysis or Views

Page 7, para. 23, line 1: for “economically active population” read “agricultural workforce”

Evident Ambiguity

Page 4, para. 11, line 2: for “will decline steadily until reserves are depleted”
read “will decline steadily until reserves of fields currently in production are depleted”

Questions may be referred to Mr. Josz (ext. 34021), Mr. Ladd (ext. 37554), and Mr. Kinda (ext. 39538) in AFR.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (2)

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Department Heads

B. Lessons Learned from SNRP I

7. The document recognizes that progress under the SNRP I was mixed at best. Growth has been mainly led by activities in the oil sector. The unstable security situation hampered government activity and, combined with weak governance and lack of commitment, resulted in major deviations of budgetary spending from SNRP I objectives, a situation continuing since the adoption of SNRP II. Significant resources were spent on military equipment; and on education and health infrastructure, at high unit costs, and without the human capital to put them to use for providing basic social services. Little progress has been made to date toward the MDGs (with the exceptions of access to an improved water supply and HIV prevalence) and Chad remains well below the critical path toward achievement of the MDGs by 2015.³

8. The staffs agree that the government's priorities identified in SNRP I remain valid. Despite the disappointing performance under SNRP I and continued security concerns, the focus should now be on implementation of the strategy and putting to use the infrastructure that has been built. In this regard, the SNRP II's emphasis on strengthening the implementation and tracking mechanism is welcome.

9. Based on the lessons learned, the SNRP II pays particular attention to the restoration of security, the diversification of the economy, the improvement of governance and the promotion of human development. Rural development rightly gets more attention. The government also intends to pursue its policy of investing in human capital in order to enable the population to participate in and fully benefit from the country's economic development.

10. However, the SNRP II reproduces the shortcomings of the previous strategy, namely a lack of focus on a manageable number of actions and a weak monitoring and evaluation (M&E) system. The staffs encourage the government to streamline the scope and number of priority programs and actions. In addition, the SNRP II has had little influence on the design and implementation of economic policies, programs and projects. Going forward, the staffs encourage the government to better align the annual budget with the SNRP II.

III. MACROECONOMIC POLICIES AND FINANCIAL MANAGEMENT

A. Sustainability of the Macroeconomic Framework and Fiscal Policy

11. In 2008-09, revenue was sufficient to fully fund the SNRP II's higher-spending scenario. This scenario set out a comprehensive medium-term expenditure plan to attain the MDGs. The authorities projected that this plan would require additional external financial resources over the period 2009-11. So far, the spike in international oil prices in 2008 and higher-than-expected oil production have yielded sufficient resources to fully fund the SNRP II, but annual budgets were not well-aligned with the SNRP II. There were significant overruns in military and investment expenditure. Going forward, current estimates for

³ SNRP II Figure 2-2, pg. 37 and World Bank, World Development Indicators database.

2010-11 suggest that resources will continue to be sufficient to fund the SNRP II. However, annual oil output peaked in 2004 and will decline steadily until reserves of fields currently in production are depleted over 20 years, driving a steady decline of government revenue over the same period.

12. The staffs agree that the non-oil primary deficit as a percentage of non-oil GDP (NOPD) is the appropriate fiscal policy anchor for Chad. Large oil revenues, while offering a windfall of additional resources with which to pursue the MDGs, are highly volatile and on a downward trend. The challenge is to insulate annual spending from this volatility, while taking full account of the long-term financing constraint. While the SNRP II states that the sustainable level of the NOPD is 10 percent, the staffs consider that it is in the low single digits.⁴ A prudent fiscal policy that gradually reduces the NOPD to a sustainable level over the medium term would allow both the transformation of oil revenue into a higher level of physical and human capital than before the oil era and a buildup of financial savings, the income from which could sustain a higher level of spending beyond the oil era. Fiscal consolidation need not come at the expense of development priorities; it can be achieved while focusing spending on priority areas (IV B. below).

13. The adoption of a sustainable fiscal policy could pave the way for resumption of a Fund-supported program and debt relief. Chad reached the Decision Point under the Enhanced HIPC Initiative in May 2001 but has not yet reached the Completion Point. Successful execution of a Fund-supported program, accompanied by the achievement of other Completion Point triggers, would lead to debt relief under the Enhanced HIPC and Multilateral Debt Relief Initiatives in an amount of about US\$ 1 billion in nominal terms, freeing up about US\$40 million per year for poverty-reducing expenditures for about 20 years. In this regard, the authorities' decision to access lending with a grant element of only 15 percent for financing the 2010 budget and to guarantee a commercial loan for an oil refinery has been a setback (paragraph 2).

IV. PUBLIC FINANCIAL MANAGEMENT REFORMS IN THE SNRP II

A. Oil Revenue

14. The SNRP II calls for a permanent, transparent mechanism for managing direct and indirect oil revenues to smooth the expenditure path and build savings. To implement such a mechanism, the staffs recommend:

- maintaining the current level of oil-revenue transparency and enhancing it by adherence to the Extractive Industries Transparency Initiative (EITI);
- consolidating the “oil” and “non-oil” budgets into a single, properly-managed budget and;
 - closely aligning expenditure, in planning and execution, with the SNRP II.

⁴ For estimations of the sustainable NOPD in Chad, see [IMF Country Report No. 09/68; Chad: 2008 Article IV Consultation - Staff Report; Box 1, p.13](#) and [IMF Country Report No. 09/67; Chad--Selected Issues; Chapter II.](#)

recent Rural Development Intervention Plan (PIDR), identify its successes and weaknesses, and establish priorities for funding and implementation going forward. The evaluation of the PDIR should also include the institutional apparatus set up to implement it.

23. Half of Chad's agricultural workforce is engaged in growing cotton, which until the discovery and development of oil was the most significant export. The SNRP II acknowledges that productivity in the cotton sector has fallen well behind that observed in other Sub-Saharan cotton exporters and it recognizes that action plans for improving farmers' access to inputs, transportation services and markets have not yet been implemented. Improving productivity in the sector and raising the incomes of cotton farmers depend critically on the long-delayed restructuring of the state-owned company, Cotontchad. Reforming Cotontchad has been on the government's agenda since 1999, yet little progress has been achieved: Cotontchad's output continues to decline and the company services its debts only thanks to fiscal transfers. Cotontchad is engaged in several business lines that may not necessarily yield economies of scope and unless it refocuses its activities, financial losses are likely to continue.

D. Water and Electricity

24. A comprehensive sector reform is urgently needed to improve access to drinking water and sanitation services in Chad. The SNRP II rightly identifies lack of maintenance as a major problem. In addition, it is particularly important to restructure the National Water and Electricity Company (STEE), as its operational performance has declined considerably over the past years. The staffs would recommend splitting STEE into two autonomous water and electricity companies, improving governance in these sectors and strengthening the financial situation of these companies.

E. Education

25. The strategy for education adopted in the SNRP II is appropriate, focusing on an increase of the level of schooling for the overall population. Particularly, it will enable poor students to get out of the cycle of poverty. For primary education, the objective is to meet the Universal Primary Education MDG by 2015 and for junior secondary education, the objective is to expand access and improve quality. Therefore, the enrollment of students from poor families in primary education is expected to increase and access to junior secondary education will discourage them from relapsing, like many of those who drop out after completing only the primary cycle. In light of the significant disparities across regions, priority is given to 25 lagging communities in the implementation of the SNRP II. Specific actions are also targeted to minority groups, poor families, and girls.

26. Access to primary education will be improved by reducing distance to schools, identified as a main cause of the low student retention rate. The staffs would recommend, however, that efforts also be made to reduce the current high repetition rates, which explain the student drop-out rate. In this regard, among other measures, time spent actually teaching and learning should be increased, the relevance of the curriculum enhanced, and school management strengthened. The language of instruction should correspond to the language used in the home and the local labor market.

27. A strategy for cost-effective school construction needs to be developed, including standard designs, planning and monitoring mechanisms. So far only 500 classrooms have been built per year on average within the existing financial constraints (compared to the SNRP II objective of building 1,200 new classrooms per year). The high unit construction cost does not allow financing a larger school construction program.⁶

28. The staffs recommend greater attention to the management of human resources in education. In particular, the low hiring of trained primary teachers (7,000 of whom were unemployed in 2009) should be addressed. While training programs for community teachers are needed, the strategy should also include appropriate incentives to encourage teachers to accept assignments in remote areas.

29. Budgetary funding for education needs to be enhanced. Despite the regulation requiring mandatory and free of charge basic education, operating costs of public schools are primarily financed by local communities and parents. The recurrent accumulation of salary arrears to community teachers represents a problem.

30. There is a need to strengthen procurement and expenditure control at the Ministry of Education to avoid leakages. The SNRP II requirement that only 50 percent of ordered school supplies and services reach their destination is inadequate, as it implies that the loss of half of procured school supplies and services is tolerated.

F. Health

31. The national health sector policy was updated in April 2007 with the objectives of improving the effectiveness of the health system, strengthening preventive measures, and better responding to the needs of the most vulnerable. In addition, the Ministry of Health prepared and adopted a road map for the reduction of maternal and infant mortality by 2015. However, management and implementation of the health policy remain weak, resulting in poor health outcomes. The percentage of total funding allocated to the health sector has increased; however, additional resources have not been spent on the highest priority needs, but rather on an ambitious construction program.

32. Implementation of the government's health program suffers from a number of weaknesses, including:

- *Shortage of human resources:* The sector faces a chronic shortage of qualified health personnel, especially in rural areas, and the ratio of health personnel to population is far below WHO standards. Moreover, existing staff is unequally distributed throughout the country, with the majority of personnel located in N'Djamena, which only represents 9 percent of the total population. An estimated 900 additional health workers will be needed to staff new and planned facilities, not including the staff

⁶ For the Government social infrastructure program, the classroom unit cost is about US\$60,000, compared to US\$15,000 for Bank-funded Education Project.