FOR AGENDA

EBS/10/143

July 12, 2010

To: Members of the Executive Board

From: The Secretary

Subject: **Burundi—Staff Report for the 2010 Article IV Consultation, Fourth Review Under the Three-Year Arrangement Under the Extended Credit Facility, and Request for Modification of Performance Criteria**

Attached for consideration by the Executive Directors is the staff report for the 2010 Article IV consultation with Burundi, the fourth review under the three-year arrangement under the Extended Credit Facility, and Burundi's request for a modification of performance criteria, which is tentatively scheduled for discussion on **Friday, July 23, 2010**. A draft decision appears on page 21. Unless an objection from the authorities of Burundi is received prior to the conclusion of the Board's consideration, the document will be published. Any requests for modifications for publication are expected to be received two days before the Board concludes its consideration.

Questions may be referred to Mr. Akitoby (ext. 36646), Mr. Ioannou (ext. 37851), Mr. Thomas (ext. 39007), and Mr. Rayner (ext. 38524) in AFR.

Unless the Documents Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the WTO Secretariat on Tuesday, July 20, 2010; and to the African Development Bank and the European Commission, following its consideration by the Executive Board.

This document, together with a supplement providing an informational annex, will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities. The supplement, which is not being distributed in hard copy, will also be available in the Institutional Repository; a link can be found in the daily list (http://www-int.imf.org/depts/sec/services/eb/dailydocumentsfull.htm) for the issuance date shown above.

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BURUNDI

Staff Report for the 2010 Article IV Consultation and Fourth Review Under the Three-Year Arrangement Under the Extended Credit Facility and Request for Modification of Performance Criteria

Prepared by the African Department
(In consultation with other departments)

Approved by Michael Atingi-Ego and Dominique Desruelle

July 9, 2010

Discussions:	A mission comprising Messrs. Akitoby (head), Ioannou, Rayner, Thomas (all AFR), and Mr. Yao (Resident Representative) visited Bujumbura May 11–22, 2010, to conduct the 2010 Article IV consultation and the fourth review of the ECF arrangement. Mr. Itam, Executive Director for Burundi, participated in the policy discussions. The staff met with President Nkurunziza, First Vice-President Sahinguvu, Second Vice-President Ntisezerana, Minister of Finance Nizigama, Central Bank Governor Sindayigaya, other senior government officials, and representatives of labor unions, the private sector, civil society organizations, the donor community, and the media.
ECF Arrangement:	On July 7, 2008, the Executive Board approved a three-year Extended Credit Facility (ECF) Arrangement with access of SDR 46.2 million (60 percent of quota). The third review of the ECF-supported program was completed in February 2010.
Program Review:	All quantitative performance criteria for March 2010 were met, and structural reforms are on track. Staff recommends completion of the fourth review.
Publication:	The authorities consent to the publication of this report, the letter of intent, and the Memorandum on Economic and Financial Policies (MEFP).

Contents Page

Acronyms

BRA	Burundi Revenue Authority
BRB	Banque de la République du Burundi
CET	Common External Tariff
CIRR	Commercial Interest Reference Rates
DFID	Department for International Development
EAC	East African Community
ECF	Extended Credit Facility
FNL	Forces Nationales pour la Libération
FSAP	Financial Sector Assessment Program
FSRS	Financial Sector Reform Strategy
LEG	Legal Department
MCM	Monetary and Capital Markets Department
MDGs	Millennium Development Goals
MDRI	Multilateral Debt Relief Initiative
MESD	Marché des Enchères Symétriques en Devises
MEFP	Memorandum on Economic and Financial Policies
NSC	National Strategy Committee
PFM	Public Financial Management
PRSP	Poverty Reduction Strategy Paper
TA	Technical Assistance
TMU	Technical Memorandum of Understanding
VAT	Value Added Tax

Executive Summary

Recent developments and outlook

The global financial crisis has slowed the Burundian economy and contributed to a significant decline in inflation. Economic growth moderated to 3.5 percent in 2009, from 4.5 percent in 2008, mainly because of lower private transfers and foreign direct investment. Because of lower international oil and food prices, headline inflation (end of period) declined from about 26 percent in 2008 to about 4.5 percent in 2009. Supported by donor flows and the SDR allocation, gross official reserves remained steady at 6.5 months of imports in 2008–09. The economic outlook is generally positive but subject to risks from the security situation and external environment.

Article IV consultation

Against the background of the East African Community (EAC) integration, the Article IV consultation discussions focused on three fundamental themes: (i) accelerating growth and reducing poverty, (ii) accelerating financial sector reform, and (iii) safeguarding fiscal sustainability while progressing toward MDGs. The authorities generally agreed with staff recommendations.

Staff and authorities agreed on the need to pursue appropriate growth-enhancing reforms. Critical reforms intend to: (i) refocus capital spending on key infrastructure to help relieve major supply bottlenecks (for example, electricity and irrigation for agriculture); (ii) continue to remove economic distortions, especially in the agricultural sector, to boost total factor productivity; and (iii) accelerate EAC integration to improve competitiveness and the business environment. On financial sector reform, the authorities will adopt a comprehensive strategy in the first quarter of 2011.

Staff and authorities also agreed that achieving debt sustainability should anchor medium-term fiscal policy. Given Burundi's high risk of debt distress and low capacity, external financing of the budget should be limited to grants and highly concessional loans. However, the authorities noted that, in exceptional cases where such financing is not available for critical growth-enhancing investment included in the authorities' development strategy, recourse to nonconcessional financing will be discussed with the Fund and World Bank staffs, consistent with the new debt limits policy. The authorities and staff agreed on the need to continue reforms of wages and employment to bring the wage bill down to sustainable levels.

Program issues

Performance under the ECF-supported program has been satisfactory. All quantitative performance criteria and the structural benchmark for March 2010 were met. Structural reforms are on track. The revised program for 2010 takes into account: (i) a new law to address the security forces' dissatisfaction with pay; (ii) the cost of the 2010 general elections; (iii) drought-related emergency spending; and (iv) the authorities' decision to issue domestic bonds during 2010–11 to clear the liability (2.4 percent of 2010 GDP) from retroactive implementation of civil servant statutes.

Staff recommends completion of the fourth review based on Burundi's performance and the strength of the program.

I. General Context

1. **Burundi is one of the poorest countries in the world**. GDP per capita is about US$140, and more than two-thirds of the population lives below the poverty line. While the country is making some progress toward the Millennium Development Goals (MDGs), it is unlikely that any will be achieved by 2015 (Table 1).

2. **The country is emerging from more than a decade of civil conflict**. The power-sharing agreement signed in December 2008 by the government and the last rebel group, *Forces Nationales pour la Libération* (FNL), paved the way for a series of national elections, which run from May 24 to September 8, 2010. However, after the communal elections on May 24, the general security situation has deteriorated following the withdrawal of the opposition parties due to their dissatisfaction with the electoral process. The representatives of the international community in Burundi issued a statement highlighting that independent observers, both national and international, conveyed a generally positive assessment of the elections and invited the opposition parties to reconsider their withdrawal. On June 28, the incumbent president won the presidential elections in which the main opposition parties did not participate. Legislative elections, scheduled for July 23, represent a significant test for the peace process.

3. **In a difficult postconflict environment, Burundi has made steady, though uneven, progress in implementing its ECF-supported economic reforms**. At the conclusion of the 2008 Article IV consultation, Executive Directors urged the authorities to further strengthen public financial management (PFM) and move forward with structural reforms to improve the investment climate and spur growth. The HIPC decision point was reached in August 2005 and the completion point in January 2009. Burundi's PRSP was published in September 2006. The latest annual progress report was completed in December 2009.

4. **The World Bank's country assistance strategy focuses on structural reforms to further increase growth and reduce poverty**. The main priorities are to (i) promote sustainable and broad-based economic growth, (ii) improve access to social services and consolidate social stability, and (iii) strengthen governance.

II. Recent Economic Developments

5. **The global financial crisis has slowed the Burundian economy and contributed to a significant decline in inflation**. Economic growth moderated to 3.5 percent in 2009, from 4.5 percent in 2008, mainly because of lower private transfers and foreign direct investment. Because of lower international oil and food prices, headline inflation (end of period) declined from about 26 percent in 2008 to about 4.5 percent in 2009, well within the single-digit level targeted under the program.

6. **Fiscal performance in 2009 was broadly satisfactory** (Table 3). Despite the global financial crisis, total revenue was 0.6 percent of GDP higher than programmed, reflecting improved collections of income and indirect taxes. Total spending was contained below the programmed level, as externally-financed spending was lower than programmed. The wage bill was also kept within the envisaged budgetary envelope. Overall, the fiscal deficit

(excluding grants) was lower than programmed. Adjusted for the shortfall in external nonproject financial assistance, domestic financing of the budget was well within the programmed target (MEFP, Table I.1).

Text Table 1. Burundi: Government Operations, 2007–09

(In percent of GDP)

	2007	2008	2009	
			Prog.	Act.
Revenue	18.6	18.5	18.0	18.6
Total expenditure and net lending	38.5	44.1	46.1	39.3
Current Spending	24.6	25.8	24.6	25.8
Capital Expenditure and net lending	12.7	15.1	16.3	13.3
Externally financed special programs	1.2	3.2	5.3	0.1
Overall balance (commitment basis, after non-HIPC grants)	-3.3	-3.7	-4.1	-5.2
Change in arrears (reduction = -)	-2.1	-0.8	-0.2	0.0
Overall balance (cash basis, after non-HIPC grants)	-5.4	-4.5	-4.3	-5.2
Financing	24.0	26.5	28.3	20.6
External grants	20.9	24.9	86.5	80.8
Of which : HIPC relief	3.8	3.0	62.5	65.3
External Borrowing	-0.9	0.2	-59.6	-64.4
Privatization proceeds	0.0	0.0	0.1	0.0
Domestic financing	4.0	1.4	1.3	4.2
Errors and Omissions	-2.1	-0.1	0.0	0.1

Sources: Burundi authorities and IMF staff estimates and projections.

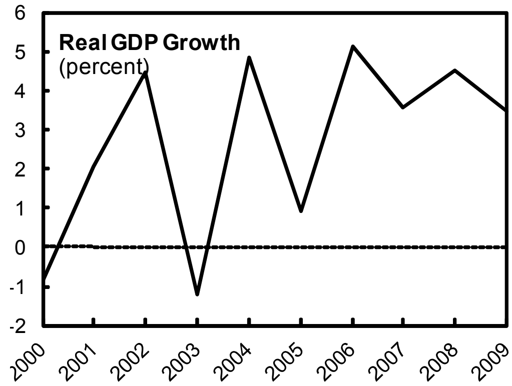
7. **Monetary policy has been geared toward achieving price stability while supporting economic recovery from the impact of two exogenous shocks**. In 2008 reserve money grew by about 25 percent as the central bank sought to accommodate the first-round effects of higher oil and food prices. With the onset of the global financial crisis in 2009, monetary policy was eased, without endangering the single-digit inflation objective.

8. **The global financial crisis did not have a significant impact on Burundi's banking system**. However, the Financial Sector Assessment Program (FSAP) report identified concentration risk as a key vulnerability of the banking system.

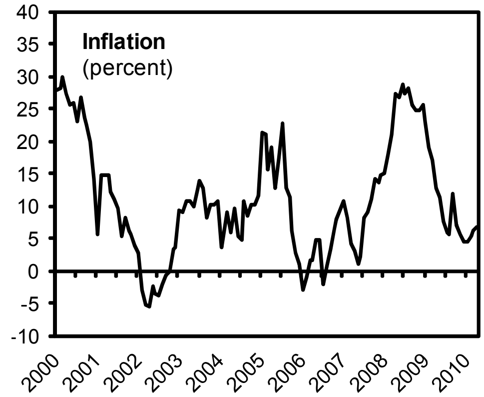
9. **Despite the food and oil shock and the global financial crisis, the external position was supported by Heavily Indebted Poor Country (HIPC) and Multilateral Debt Relief Initiative (MDRI) relief and the SDR allocation**. Notwithstanding the negative impact of the food and oil crisis on the trade balance, the external current account deficit improved in 2008 because of high transfers to mitigate the effects of the shock. In contrast, in 2009 the external current account deficit worsened, even as the terms of trade improved, because of lower donor support. Overall, the balance of payments position was supported by HIPC and MDRI relief and the SDR allocation. Gross reserves remained at a very comfortable level of 6.5 months of import cover.

Figure 1. Burundi: Macroeconomic Performance, 2000–09

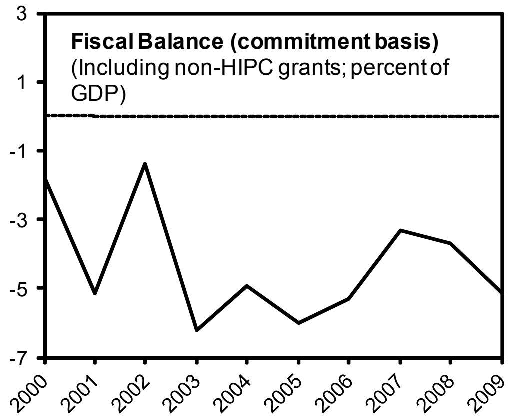
Growth was volatile but trended upward...



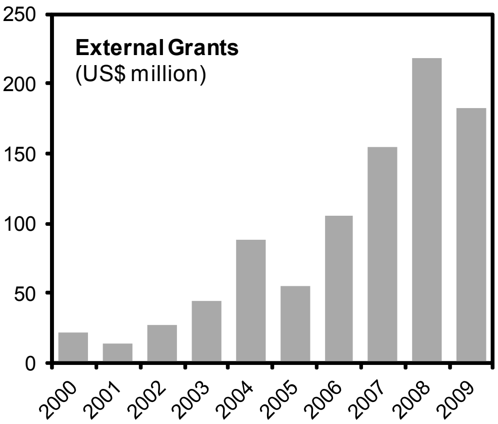
...while inflation decelerated in line with falling commodity prices.



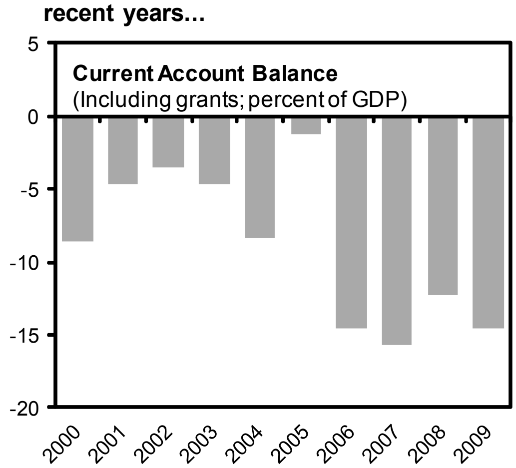
The recent improvement in the fiscal position was reversed in 2009...



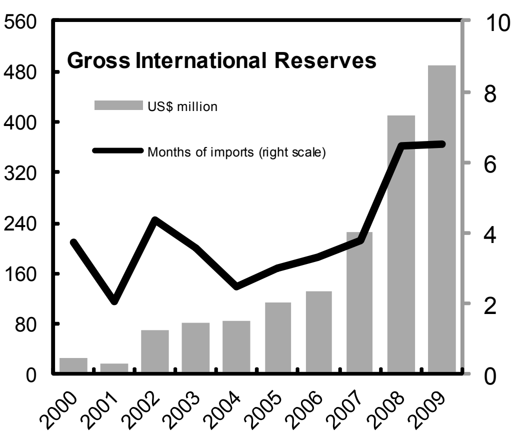
... because of a decline in donor support.



The current account deteriorated in recent years...



...but official inflows helped rebuild international reserves.



Sources: Burundi authorities and IMF staff estimates.

III. POLICY DISCUSSIONS

10. **Against the background of the EAC integration, the Article IV consultation discussions focused on three key themes**: (i) accelerating growth and reducing poverty, (ii) accelerating financial sector reform, and (iii) safeguarding fiscal sustainability while achieving progress toward MDGs. In addition, the mission discussed important issues related to the Article IV consultation. To set the stage for the policy discussions, staff presented the updated macroframework.

Box 1. Burundi: Main Recommendations of the 2008 Article IV Consultation

Advice	Status
Improve PFM.	Substantial progress has been achieved (see Table I.1, EBS/10/18). The authorities intend to maintain the momentum on PFM reforms.
Improve the composition of spending.	Social spending has increased. However, the wage bill remains high. Security spending is also still high, reflecting the uncertain security situation. There is room to improve budgetary forecasts of social spending.
Reform monetary and exchange operations.	Monetary policy has become more market based, but the central bank needs to make more active use of available policy instruments. A symmetrical foreign exchange auction has been created and liquidity auctions have been revamped by eliminating floor prices.
Maintain prudent debt management.	Debt management has been enhanced as a result of the reorganization of the debt unit at the ministry of finance and the upgrading of debt management software. There was no recourse to non-concessional loans.
Implement structural reforms to stimulate private sector.	The privatization of the coffee sector has been launched, but only 13 out of 117 washing stations have been privatized, owing to limited investor interest. Progress in the reform of the investment climate has been slow.

A. Macroeconomic Framework and Supporting Policy Mix

11. **The economy is expected to modestly recover from the global financial crisis in 2010**. Real GDP growth is projected to rise to 3.9 percent in 2010, from 3.5 percent in 2009, mainly because of a substantial increase in coffee production and donor-financed investment. Headline inflation in 2010 is projected to remain in single digits at 9.5 percent, although drought has put upward pressure on food prices. Gross official reserves would decline to 6 months of imports, as a result of sterilization.

12. **Provided the security and political situation continues to improve, Burundi's medium-term economic outlook is generally positive**: (i) GDP growth is expected to average about 5 percent in the medium term, up from about 4 percent from 2007–09; (ii) average inflation would decelerate to 5 percent by 2014; and (iii) gross official reserves would stabilize at six months of imports (Text Table 2), consistent with the EAC convergence criterion. Economic growth is expected to be driven by three main factors: (i) continued removal of major economic distortions, especially in the coffee sector, which will boost total factor productivity; (ii) a substantial increase in aid-financed investment, largely for infrastructure renovation, which will help relieve major supply bottlenecks; and (iii) with EAC membership, access to a bigger market and the possibility of attracting more investment in areas where Burundi has a comparative advantage (for example, agriculture and tourism). The UN Policy for Post-Conflict Employment Creation, Income Generation and Reintegration (UN-PCEIR) could also drive growth by promoting stability. There is scope for a significant increase in growth in the medium term, should potential investments in the mining sector materialize.

13. **The medium-term fiscal outlook is expected to improve.** The overall fiscal deficit (on a commitment basis, including non-HIPC grants) is projected to decline from an average of 4.7 percent of GDP in 2005–09 to about 1.5 percent by 2013, supported by gradual improvement in revenue collections. Driven by spending on PRSP priority areas, current spending would average about 25 percent of GDP in 2010–15, broadly unchanged from recent years. The wage bill is projected to decline gradually to 11 percent of GDP by 2015, taking into account demobilization and the need to accommodate hiring in priority sectors. Acknowledging the need for significant investment in public infrastructure and in agriculture, the macroframework shows an increase in capital spending, supported by project grants.

14. **A coherent policy mix will support the above macroframework**. Appropriate growth-enhancing reforms will underpin the growth strategy. Achieving debt sustainability should anchor medium-term fiscal policy. Given Burundi's high risk of debt distress and low capacity (Joint DSA, Supplement I), improving export capacity and relying on grants and highly concessional loans to finance the budget is critical for achieving debt sustainability. Ongoing fiscal reforms will also help in this regard. These include the new budget law and reforms of tax policy, revenue administration, expenditure policy, treasury management, and debt management.

15. **Monetary policy is geared toward stabilizing prices while allowing sufficient scope for improved economic growth**. To this end, the central bank will continue to use the reserve money as an operating target, and broad money as intermediate target. To affect its operating target, the central bank relies on liquidity auctions. Close collaboration between the central bank and the ministry of finance is critical for effective monetary policy. Coordination of monetary and fiscal policies has been strengthened by the creation of the cash flow management committee and regular monthly meetings between the BRB and the ministry of finance (EBS/10/18, MEFP ¶21). A smooth transition from the current auction system to an interbank-based market will introduce greater exchange rate flexibility, thus enhancing monetary policy. In the medium-term, efforts to achieve EAC monetary union convergence criteria will also help consolidate macroeconomic stability.

Text Table 2. Burundi: Medium-Term Outlook, 2009–15

	2009	2010	2011	2012	2013	2014	2015
				Proj.			
	(Annual percentage change, unless otherwise indicated)						
National income and prices							
Real GDP growth	3.5	3.9	4.5	4.8	5.0	5.0	5.0
Consumer prices (end of period)	4.6	9.5	7.0	6.5	5.0	5.0	5.0
	(Percent of GDP, unless otherwise indicated)						
General government							
Revenue (excluding grants)	18.6	18.3	18.8	19.4	19.7	19.9	20.2
Total expenditure and net lending	39.3	49.5	47.0	46.8	44.4	43.1	43.0
Overall balance							
Commitment basis (after non-HIPC grants)	-5.2	-3.1	-3.1	-1.8	-1.3	-1.3	-1.3
Cash basis (after non-HIPC grants)	-5.2	-4.3	-4.2	-1.8	-1.3	-1.3	-1.3
External sector							
Current account balance	-14.5	-9.0	-10.6	-10.5	-10.4	-10.2	-10.1
Overall balance of payments	4.1	-0.8	0.1	-0.1	1.3	1.1	0.4
Gross official reserves							
In US$ million	323.0	310.7	327.9	342.5	362.3	378.2	392.7
In months of imports	6.5	6.0	6.0	6.0	6.0	6.0	6.0

Sources: Burundi authorities and IMF staff estimates and projections.

16. **There are, however, significant downside risks to the medium-term outlook**. Besides the possible deterioration in the political and security situation, risks include (i) delays in macrocritical structural reforms that underpin the growth objectives, (ii) an uncertain external environment, and (iii) slow progress toward EAC integration. Weak institutional capacity could also endanger policy implementation.

B. Accelerating Growth and Reducing Poverty

Background

17. **Extended conflict lasting for 17 years has been the biggest constraint on growth through its negative impact on investment**. Consequently, the government will need to undertake a major infrastructure rehabilitation program, with the help of development partners.

18. **The reform of the coffee sector is of great economic importance**. The sector is the principal source of income for nearly 800,000 households, and coffee accounts for about two-thirds of total exports. It is expected that the recent privatization of 13 coffee washing stations will have positive spillover effects on the entire sector. Because interest from foreign investors was initially limited, the government has decided to reissue the invitations to bid at the end of the current coffee campaign.

19. **Regional integration is critical for achieving medium-term growth objectives.** EAC membership could spur growth, because it would give Burundi access to a bigger market (a population of 120 million) and increase the possibility of attracting more investment in areas where Burundi has a comparative advantage (for example, agriculture and tourism). Aware of these potential advantages, the government has already established an interministerial committee to coordinate and facilitate decision making in the context of the EAC. In addition, a national strategy and action plan, prepared with the assistance of development partners, will be examined by a technical team by end-July and submitted to the new government for endorsement.

Staff advice

- Refocus capital spending on key infrastructure that will help relieve major supply bottlenecks (for example, electricity and irrigation). All investment projects should be subject to rigorous cost-benefit and cost-effectiveness analyses. The authorities should seek World Bank technical assistance (TA) to strengthen the system of appraisal, selection, and monitoring of investment projects. Staff underscored that external financing should be limited to grants and highly concessional loans to avoid unsustainable debt.

- Continue to reform the coffee sector. Staff considers coffee sector privatization critical for boosting total factor productivity. The authorities will also pursue reform of other key sectors including tea and telecommunications, in consultation with the World Bank.

- Accelerate implementation of the EAC national strategy and action plan to achieve nominal convergence and spur structural reforms that would improve competitiveness and the business environment. Staff also discussed the authorities' plan to liberalize the capital account by 2014, in line with EAC requirements. Together with structural reforms, this should further improve competitiveness and the business environment. MCM could provide TA if requested.

Authorities' views

20. **The authorities concurred that political instability has been a major impediment to economic growth, and they therefore expect a rapid economic turnaround following peaceful elections**. They emphasized that their growth strategy stands on four sectoral pillars (agriculture, tourism, energy and water, and transport and communication infrastructure) and capitalizes on EAC membership. They pointed out that the creation of an agency to promote investment will contribute to strengthening the confidence of national and foreign investors (MEFP ¶14).

21. **The authorities agreed with staff's recommendations** and made the following points:

- Efforts are underway to refocus capital spending on the identified four pillars of growth. The authorities asked for donors to help them pursue this goal. In addition, the project planning unit at the ministry of planning would be strengthened by centralizing technical expertise on project analysis that is currently scattered across ministries.
- The privatization of coffee washing stations will be relaunched by the end of the ongoing coffee season. Although the coffee sector is important for growth and poverty reduction, stabilizing the population growth and reforming land tenure are also critical.
- Every effort will be made to rely on grants and highly concessional financing. However, in exceptional cases, where such financing is not available for critical growth-enhancing investment included in the authorities' development strategy, recourse to nonconcessional financing will be discussed with the Fund and World Bank staffs to ensure consistency with Fund policy on debt limits.
- Institutional capacity is still inadequate, despite substantial TA. It is therefore critical to identify and focus on the most urgent technical assistance needs.

C. Accelerating Financial Sector Reform

Background

22. **Access to financial services is limited, reflecting the underdeveloped payments system.** Based on data from 2007–08, only 2 percent of the total population has a bank account, and less than 0.5 percent use bank credit services. Consequently, cash transactions predominate, and payment instruments are physically exchanged. Moreover, most small and medium-size enterprises find it difficult to obtain credit, mainly because of lack of adequate information on the creditworthiness of prospective borrowers, the unavailability of real guarantees, and weak capacity of project preparation.

23. **The FSAP report is expected to guide reform in the financial sector**. In January 2009, staffs from the Fund and the Bank conducted the Financial Sector Assessment Program (FSAP) for Burundi. The Financial Sector Stability Assessment report (SM/09/266) was issued to the Executive Board in October 2009. The authorities plan to use the FSAP report findings to guide their financial sector reform strategy. Work in this area has been

launched with the creation of the National Strategy Committee by order of the ministry of finance.

24. **Consequent to the global financial crisis, the central bank took steps to enhance banking supervision** (MEFP, ¶12). Although the FSAP mission detected no obvious sign of imminent systemic stress as a result of the crisis, the authorities have taken steps to implement MCM recommendations on banking supervision, particularly those related to risk-based supervision, and have raised minimum capital requirements. The central bank is also taking steps to address concentration risk, a key vulnerability of the banking system (Table 7). To mitigate this risk, the BRB will continue to scrutinize bank risk management practices and lending standards and conduct stress tests, with the help of Central AFRITAC TA.

Staff advice

25. **Staff emphasized the need to accelerate financial sector reform**, drawing on the FSAP report and consistent with EAC requirements. Priority reforms include:

- Defining a strategy and policy for modernizing the infrastructure for the payment system, in keeping with EAC action plans and international standards.
- Modernizing the payment system's legal framework.
- Developing a complete clearing and settlement infrastructure, with the automation of exchanges of small values (checks and automatic transfers) within an electronic clearing system.

Authorities views

26. **The authorities agreed with the staff's assessment and policy advice.** They emphasized that the main objective of the financial sector reform is to broaden access to financial services. With the newly established steering committee, work on financial sector reform will accelerate, to enable the council of ministers to adopt a comprehensive strategy in the first quarter of 2011.

27. **The authorities pointed out that urgent reforms are already underway**, in close coordination with World Bank technical and financial assistance. These urgent priorities include: (i) modernizing the payment systems (which entails computerization of check clearing); (ii) introducing electronic banking services; (iii) improving regulation and supervision of commercial banks and microfinance institutions; (iv) setting up a credit bureau to ensure effective assessment of borrowers' creditworthiness; and (v) developing domestic financial markets to provide long-term and stable sources of funds for banks.

D. Safeguarding Fiscal Sustainability While Achieving Progress Toward MDGs

Background

28. **To modernize the tax system, the government has introduced a series of major reforms**, including a VAT and the EAC common external tariff. However, given the authorities' limited administrative capacity and delays in setting up the Burundi Revenue

Authority (BRA), staff adopted a conservative revenue projection, until the gains from VAT materialize. Staff will discuss the first-year implementation of VAT during the fifth review and update the medium-term projections accordingly. At around 18.5 percent, the revenue to GDP ratio is above the average of 17.3 percent of GDP for fragile states in Sub-Saharan Africa.

29. **Expenditures are dominated by wages and security spending.** At around 12 percent of GDP, the wage bill is above the authorities' medium-term target of 11 percent of GDP. Since recruitment in education and health sectors affects progress toward the MDGs, the wage bill in these sectors will continue to grow owing to enormous needs for teachers and health personnel. Achieving the medium-term target for the wage bill, while continuing to recruit in priority sectors, will therefore hinge critically on reducing the size of security forces.

Staff advice

- Manage carefully the establishment of the BRA and broaden the tax base by implementing the recommendations of recent FAD technical assistance. The BRA, which was supposed to start operations in January 2010, is not yet fully functional because of staffing delays. The authorities are taking all the necessary steps to expedite the process, in order to safeguard government revenue.
- In consultation with key donors including the World Bank, continue reforms of wage and employment including wage policy and demobilization after the elections to bring down the wage bill to sustainable levels.
- Make spending more efficient by implementing recent PFM reforms and enhancing governance and accountability in the use of public resources. Public tracking expenditure surveys could help identify leakages and obstacles to effective service delivery.
- Implement the above policies in order to crowd in social spending and accelerate progress toward achieving the MDGs.

Authorities' views

30. **The authorities agreed with the staff's assessment and policy advice** and emphasized that:

- In coordination with the Department for International Development (DFID), steps will be taken to shorten the transition from the old tax administration to the BRA. The focus will be on quick staffing and a clear time-bound action plan.
- Integration of former rebel groups has put pressure on the wage bill. They saw demobilization as a critical component of their strategy to bring the wage bill down, but cautioned that this has to be tackled with great care and only after elections, given the political and social implications.
- The medium-term debt profile could improve with future growth in the mining sector.

E. Other Article IV Issues

31. **The mission discussed other Article IV issues**:

- *Trade policy*. Significant reforms have been implemented to promote external trade. These include external tariff reform in line with EAC requirements, a new investment code consistent with best international practices, a new bankruptcy law, and a commercial arbitration law. Looking forward, key priorities are easing administrative obstacles to trade, establishing a single trade platform, and completing the reform of the coffee and tea sectors.

- *Assessment of the exchange rate.* Analysis of the official exchange rate suggests there is no clear indication of significant misalignment. However, there is evidence that structural factors are a constraint on competitiveness (Box 2). The mission informed the authorities that MCM has reclassified their exchange rate system from "floating" to "stabilized." Staff urged the authorities to introduce more flexibility in the exchange rate to help the economy adjust to external shocks and the EAC required capital account liberalization planned for 2014.

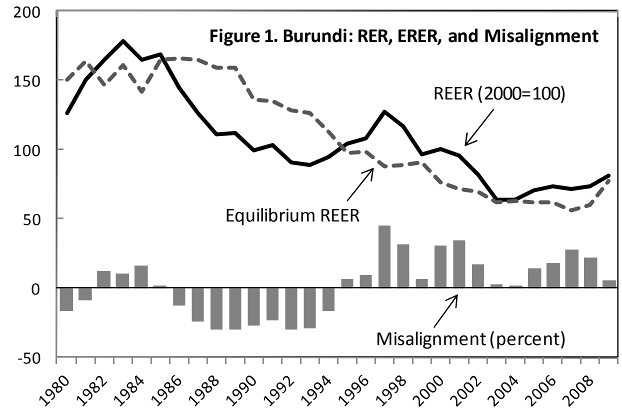
- *Multiple currency practice subject to Article VIII issues*. The authorities have requested MCM and LEG TA to assist them to resolve the remaining multiple currency practice.

32. **Serious shortcomings in data provision significantly hamper surveillance.** While some improvements in the fiscal area have been achieved, there are acute shortcomings in national accounts and balance of payments statistics (Informational Annex, Supplement II) that introduce uncertainty into estimates and projections. The statistical office suffers from lack of qualified personnel and resources. With TA from the Fund and other donors, the authorities are continuing efforts to strengthen economic and financial data.

Box 2. Burundi: Exchange Rate and Competitiveness Assessment

The general finding of the assessment is that there is no clear sign of significant misalignment of the real exchange rate. However, there is substantial evidence that nonprice structural factors are a major constraint on competitiveness.

Quantitative assessment of Burundi's real exchange rate (RER) is complicated by data limitations in the national accounts and balance of payments. The price and volume volatility of the undiversified export sector and the lack of an interbank foreign exchange market further hinder the effort to separate underlying trends from temporary fluctuations.

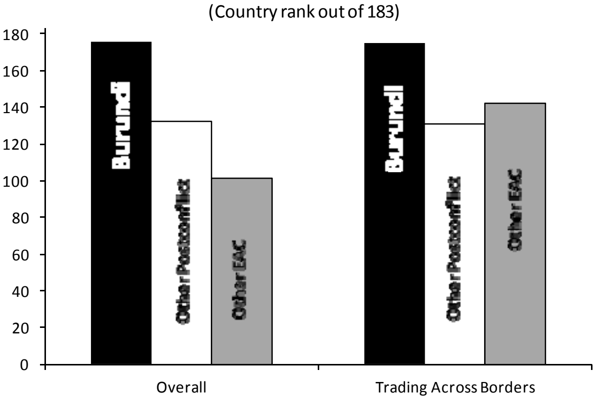


Source: INS database and IMF Staff estimates.

Nevertheless, the RER shows no clear signs of significant misalignment. Using the equilibrium real exchange rate (ERER) methodology, staff estimates that the RER was overvalued by 5.8 percent at end-2009 (Figure 1). Estimates based on the external sustainability methodology generally confirm this finding. According to the latter approach, the medium-term current account balance is approximately 1.3 percentage points of GDP below its underlying norm, implying that the RER is modestly overvalued.

The authorities are taking steps to make the exchange rate more flexible. The recent launch of symmetrical foreign exchange auctions and the creation of an interbank foreign exchange market in the near future will increase the flexibility of the exchange rate.

Figure 2. Burundi: Cost of Doing Business Indicators
(Country rank out of 183)



Source: World Bank's Doing Business Indicators.

Structural factors have been a major constraint on competitiveness. Burundi has one of the least friendly business environments in the world, ranking 176 out of 183 countries in the World Bank's 2010 *Doing Business* report and well below other postconflict and EAC countries. Burundi ranks particularly low on the efficiency of procedures to trade externally (Figure 2).

Integration to the EAC will help broaden the market for exports and decrease the time and costs associated with trading across borders. Recent privatizations in the coffee sector should increase productivity and realign incentives.

IV. Program Issues

33. **Program implementation through March was generally satisfactory**. All quantitative performance criteria and structural benchmarks for end-March were met. External assistance in the first quarter of 2010 was higher than programmed because of the late disbursement of budget support initially planned for 2009. These disbursements were used to pay down central bank advances temporarily extended in 2009 as bridge-financing for delayed budget support.

34. **Fiscal policy in 2010 will continue to be geared toward addressing debt sustainability concerns**. Given Burundi's high risk of debt distress and low capacity, external financing of the budget will be limited to grants and highly concessional loans. The fiscal reforms of the past three years will also help ensure debt sustainability. These include the new budget law and the reforms of tax policy, revenue administration, expenditure policy, treasury management, and debt management (EBS/10/18, MEFP Table I.1).

35. **The authorities recognize that mobilizing domestic revenue is critical for fiscal sustainability and increased poverty-reducing expenditure** (MEFP, ¶16). The revised revenue target for 2010 is 18.3 percent of GDP, 0.2 percentage point of GDP lower than originally programmed because of delays in staffing the BRA. To safeguard the revenue target, staff urged the authorities to continue their efforts to broaden the revenue base by reducing exemptions and strengthening tax and customs administration. In particular, the authorities will take all the necessary steps to expedite the staffing of the BRA.

36. **The primary objective of expenditure policy in 2010 is to significantly improve the composition of public spending in favor of priority sectors** (MEFP, ¶17). Accordingly, propoor spending is expected to increase by about 1.8 percent of GDP. In line with Burundi's poverty reduction strategy, MDRI resources will be spent on agriculture, water, rural infrastructure, health, and education.

37. **The program for 2010 has been revised** (Table 3) to take into account: (i) a new law to address the security forces' dissatisfaction with pay; (ii) the government's contribution of 0.8 percent of GDP to the cost of the 2010 general elections (3.3 percent of GDP); (iii) drought-related emergency spending; and (iv) the authorities' decision to issue domestic bonds to clear during 2010–11 the liability (2.4 percent of 2010 GDP) from retroactive implementation of the civil servant statutes (EBS/10/18; MEFP, ¶17).

38. **Staff and authorities agreed on the following**:

- Finance the impact of the new law on the security forces' pay (about 0.7 percent of GDP) by using the budgeted reserve fund (0.5 percent of GDP) and by cutting nonpriority spending on goods and services (0.2 percent of GDP) while guarding against accumulation of arrears.

- Accommodate drought-related emergency spending of 0.5 percent of GDP through increased domestic borrowing.

- Accommodate domestically financed elections spending of 0.8 percent of GDP. It is likely that additional donor financing for the elections will be provided, thus reducing the government's contribution. Staff urged donors to honor their commitments to finance most elections-related spending to avoid crowding out domestic funding for high-priority spending.
- The macro framework incorporates the authorities' decision to issue domestic bonds to clear during 2010–11 the liability (2.4 percent of 2010 GDP) from retroactive implementation of the civil servant statutes. This one-time operation was motivated by the need to: (i) end more than two months of strike by teachers and to forestall social instability ahead of the elections, and (ii) cement peace after 17 years of conflict. This reinforces the need to pursue structural reforms to bring down the wage bill.

V. Staff Appraisal

39. **In a difficult postconflict environment, Burundi has made steady, though uneven, progress**. Most monetary and fiscal reforms have progressed. However, structural reform has generally been slow, because of limited institutional capacity and political instability.

40. **Burundi's medium-term economic outlook is positive as long as the security situation continues to improve**. Near-term growth is projected to rise, supported by a good coffee harvest, though inflation would remain high, driven by rising food prices. Economic growth in the medium term would be markedly higher, propelled by improved political conditions, EAC membership, and increased donor assistance.

41. **Staff urges the authorities to anchor medium-term fiscal policy to debt sustainability**. Given the high risk of debt distress and low capacity, the budget should be financed only by grants and highly concessional external financing. Improvements in governance will be critical for donor support. In this regard, the authorities should further strengthen PFM and manage public expectations of a peace dividend, especially for public employees.

42. **Staff encourages the authorities to continue their efforts to reform the financial sector** by improving banking supervision, modernizing the payment system, and addressing weaknesses in the banking system, notably concentration risk.

43. **Sustained growth depends on accelerating structural reforms**. Staff urges the authorities to pursue appropriate growth-enhancing reforms by refocusing capital spending on key infrastructure, accelerating EAC integration, and advancing financial sector reform.

44. **The exchange rate seems to be broadly in line with its equilibrium rate**. Analysis of the real exchange rate suggests there is no clear indication of significant misalignment, but there is significant evidence that structural factors are a major constraint on competitiveness.

45. **Burundi maintains one multiple currency practice inconsistent with Article VIII, Section 3**. The authorities have not sought, and staff does not recommend, approval.

46. **The data provided to the Fund are generally inadequate for effective surveillance,** especially national accounts and balance of payments data. Priority should be given to improving statistics in these areas.

47. **Staff recommends completion of the fourth review under the three-year ECF arrangement** based on Burundi's performance and the strength of the program. Staff also recommends approval of the modification of performance criteria, which stems from the factors outlined in paragraph 38. Risks to the program can be mitigated by sound policies and reforms, in coordination with Burundi's development partners.

48. **The authorities' intention to make public the staff report, the letter of intent, and the MEFP is welcome**. Staff recommends that the next Article IV consultation with Burundi be held on the 24-month consultation cycle in accordance with Decision No. 12794-(02/76) of July 2002, as amended by Decision No. 12854-(02/96) of September 12, 2002, and Decision No. 13562-(05/85), October 5, 2005.

Proposed Decision

The following draft decision, which may be adopted by a majority of votes cast, is proposed for adoption by the Executive Board:

1. Burundi has consulted with the Fund in accordance with paragraph 2.I.D(b) of the three-year arrangement for Burundi under the Extended Credit Facility (the "ECF arrangement") (EBS/08/77, 6/24/08) in order to review program implementation.

2. The letter dated July 7, 2010 from the Second Vice-President, the Minister of Finance, and the Governor of the Bank of the Republic of Burundi (the "July 2010 Letter"), together with its attached Memorandum on Economic and Financial Policies (the "July 2010 MEFP") and Technical Memorandum of Understanding (the "July 2010 TMU"), shall be attached to the ECF arrangement for Burundi, and the letter dated June 24, 2008 from the Second Vice-President, the Minister of Economy, Finance and Cooperation for Development and the Governor of the Bank of the Republic of Burundi and its attachments, as modified and supplemented, shall be read as modified and supplemented by the July 2010 Letter and its attachments.

3. Accordingly, the ECF arrangement for Burundi shall be modified as follows:

   a. Paragraphs 2.I.E(a), 2.II.A(e), (f), and (g) shall be modified by replacing the references to "Table I.3 of the January 2010 MEFP" and "January 2010 TMU" with "Table I.2 of the July MEFP" and "July 2010 TMU" respectively.

4. The Fund decides that the fourth program review contemplated in paragraph 2.I.D(b) of the ECF arrangement is completed, and that Burundi may request the fifth disbursement referred to in paragraph 1(c)(v) of the ECF arrangement.

Table 1. Burundi: Millennium Development Goals

	1990	1995	2000	2005	2008	Target
Goal 1: Eradicate extreme poverty and hunger						
Employment to population ratio, 15+, total (%)	84	85	85	83	83	..
Employment to population ratio, ages 15-24, total (%)	*74*	76	77	74	73	..
GDP per person employed (annual % growth)	-1	-9	-3	-4	0	..
Income share held by lowest 20%	8	..	5	9	9	..
Malnutrition prevalence, weight for age (% of children under 5)	..	..	39	..	..	..
Poverty gap at $1.25 a day (PPP) (%)	*40*	..	*47*	*36*	*36*	..
Poverty headcount ratio at $1.25 a day (PPP) (% of population)	*84*	..	*86*	*81*	*81*	..
Prevalence of undernourishment (% of population)	44	57	..	63	..	..
Vulnerable employment, total (% of total employment)	..	..	..	..	..	..
Goal 2: Achieve universal primary education						
Literacy rate, youth female (% of females ages 15-24)	48	..	70	..	75	100
Literacy rate, youth male (% of males ages 15-24)	59	..	77	..	77	100
Persistence to last grade of primary, total (% of cohort)	..	..	53	*58*	*54*	..
Primary completion rate, total (% of relevant age group)	41	..	25	36	45	..
Total enrollment, primary (% net)	..	..	43	63	99	100
Goal 3: Promote gender equality and empower women						
Proportion of seats held by women in national parliaments (%)	..	..	6	31	31	..
Ratio of female to male enrollments in tertiary education	36	..	35	38	46	..
Ratio of female to male primary enrollment	80	80	80	86	95	..
Ratio of female to male secondary enrollment	58	..	..	74	71	..
Share of women employed in the nonagricultural sector (% of total nonagricultural employment)	14	..	..	..	..	..
Goal 4: Reduce child mortality						
Immunization, measles (% of children ages 12-23 months)	74	80	76	87	84	..
Mortality rate, infant (per 1,000 live births)	113	111	107	104	102	37.7
Mortality rate, under-5 (per 1,000)	189	184	178	171	168	63.1
Goal 5: Improve maternal health						
Adolescent fertility rate (births per 1,000 women ages 15-19)	..	40	34	24	19	..
Births attended by skilled health staff (% of total)	..	..	25	34	..	..
Contraceptive prevalence (% of women ages 15-49)	..	..	16	9	..	..
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	1,100	..	..
Pregnant women receiving prenatal care (%)	..	..	78	92	..	..
Unmet need for contraception (% of married women ages 15-49)	..	..	..	..	..	..
Goal 6: Combat HIV/AIDS, malaria, and other diseases						
Children with fever receiving antimalarial drugs (% of children under age 5 with fever)	..	..	31	30	..	..
Condom use, population ages 15-24, female (% of females ages 15-24)	..	..	..	..	..	..
Condom use, population ages 15-24, male (% of males ages 15-24)	..	..	..	..	..	..
Incidence of tuberculosis (per 100,000 people)	154	223	321	387	367	..
Prevalence of HIV, female (% ages 15-24)	..	..	..	*1.3*	*1.3*	..
Prevalence of HIV, male (% ages 15-24)	..	..	..	*0.4*	*0.4*	..
Prevalence of HIV, total (% of population ages 15-49)	1.7	5.2	3.8	2.4	2.0	..
Tuberculosis cases detected under DOTS (%)	..	20	30	25	27	..
Goal 7: Ensure environmental sustainability						
CO2 emissions (kg per PPP $ of GDP)	0.1	0.1	0.1	0.1	..	..
CO2 emissions (metric tons per capita)	0.0	0.0	0.0	0.0	..	..
Forest area (% of land area)	11.3	9.5	7.7	5.9	*5.2*	..
Improved sanitation facilities (% of population with access)	44	43	42	41	41	..
Improved water source (% of population with access)	70	70	71	71	71	..
Marine protected areas, (% of surface area)	..	..	..	..	..	..
Nationally protected areas (% of total land area)	..	..	..	6	6	..
Goal 8: Develop a global partnership for development						
Aid per capita (current US$)	46	47	14	49	59	..
Debt service (PPG and IMF only, % of exports, excluding workers' remittances)	42	27	38	34	7	..
Internet users (per 100 people)	0	0	0.1	0.5	0.8	..
Mobile cellular subscriptions (per 100 people)	0	0	0	2	6	..
Telephone lines (per 100 people)	0	0	0	0	0	..
Other						..
Fertility rate, total (births per woman)	7.0	6.0	6.0	5.0	5.0	..
GNI per capita, Atlas method (current US$)	200	150	120	100	140	..
GNI, Atlas method (current US$) (billions)	1.1	0.9	0.8	0.7	1.1	..
Gross capital formation (% of GDP)	15	6	6	11	16	..
Life expectancy at birth, total (years)	46	45	47	49	50	..
Literacy rate, adult total (% of people ages 15 and above)	37	..	59	..	66	..
Population, total (millions)	5.7	6.2	6.5	7.4	8.1	..
Trade (% of GDP)	35.6	40.2	27.7	56.7	57.7	..

Source: World Development Indicators database.

Table 2. Burundi: Selected Economic and Financial Indicators, 2007–15

	2007	2008	2009		2010		2011	2012	2013	2014	2015
			Prog. EBS/09/108	Act.	Prog.	Rev. Prog.			Proj.		
			(Annual percentage change)								
National income and prices											
Real GDP growth	3.6	4.5	3.2	3.5	3.9	3.9	4.5	4.8	5.0	5.0	5.0
GDP deflator	8.2	25.1	20.3	14.1	8.5	8.3	9.4	8.0	6.5	5.0	5.0
Consumer prices (period average)	8.3	24.4	12.9	10.7	8.0	7.0	8.2	6.8	5.8	5.0	5.0
Consumer prices (end of period)	14.7	25.7	9.1	4.6	7.5	9.5	7.0	6.5	5.0	5.0	5.0
External sector											
Exports, f.o.b. (US$)	-9.7	15.1	-0.4	21.5	16.8	20.2	-0.6	12.5	4.2	14.0	5.6
Imports, f.o.b. (US$)	20.6	16.0	-32.3	-21.5	17.8	32.3	8.0	3.0	4.0	6.2	6.2
Export volume	-1.7	5.2	35.5	16.0	20.6	26.4	7.2	20.4	5.5	16.5	5.5
Import volume	6.0	4.1	6.0	4.7	8.5	8.0	6.6	5.0	5.0	5.0	5.0
Terms of trade (deterioration = –)	-23.4	3.4	15.0	39.8	-10.9	-22.4	-8.4	-4.7	-0.3	-3.3	-1.1
			(Change in percent of beginning of period M2, unless otherwise indicated)								
Money and credit											
Net foreign assets	11.5	21.9	0.3	-2.9	0.5	3.0	...	...	...	...	...
Domestic credit	6.6	18.8	15.7	27.8	11.9	11.3	...	...	...	...	...
Government	-0.2	5.8	4.9	17.1	4.1	0.7	...	...	...	...	...
Private sector	7.6	8.5	6.2	13.7	7.9	10.6	...	...	...	...	...
Money and quasi-money (M2)	10.1	34.2	14.4	19.8	12.0	12.0	...	...	...	...	...
Reserve money (12–month growth rate)	17.4	25.1	13.5	26.6	11.5	10.6	...	...	...	...	...
			(Percent of GDP)								
General government											
Revenue (excluding grants)	18.6	18.5	18.0	18.6	18.5	18.3	18.8	19.4	19.7	19.9	20.2
Total expenditure and net lending	38.5	44.1	46.1	39.3	48.3	49.5	47.0	46.8	44.4	43.1	43.0
Overall balance (commitment basis)											
Excluding grants	-19.8	-25.6	-28.1	-20.7	-29.8	-31.2	-28.2	-27.4	-24.7	-23.2	-22.8
Including grants (excl. HIPC)	-3.3	-3.7	-4.1	-5.2	-4.0	-3.1	-3.1	-1.8	-1.3	-1.3	-1.3
External sector											
Current account balance	-15.7	-12.3	-9.5	-14.5	-10.2	-9.0	-10.6	-10.5	-10.4	-10.2	-10.1
Overall balance of payments	3.1	7.4	-2.5	4.1	-1.5	-0.8	0.1	-0.1	1.3	1.1	0.4
Savings-investment balance	-15.7	-12.3	-9.5	-14.5	-10.2	-9.0	-10.6	-10.5	-10.4	-10.2	-10.1
Private	-12.4	-8.5	-5.4	-9.4	-6.2	-5.9	-7.6	-8.7	-9.1	-8.9	-8.8
Public	-3.3	-3.7	-4.1	-5.2	-4.0	-3.1	-3.1	-1.8	-1.3	-1.3	-1.3
			(US$ million, unless otherwise indicated)								
External sector											
Gross official reserves											
US$ million	177.3	266.6	231.8	323.0	302.2	310.7	327.9	342.5	362.3	378.2	392.7
Months of imports	3.8	6.5	5.5	6.5	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Debt-service to exports ratio (percent)	6.8	3.5	2.3	1.9	3.2	2.5	5.4	9.1	10.2	10.1	9.3
Memorandum item:											
GDP at current market prices (BIF billion)	1060	1386	1711	1637	1836	1841	2104	2381	2662	2936	3238

Sources: Burundi authorities and IMF staff estimates and projections.

Table 3. Burundi: General Government Operations, 2007–15

	2007	2008	2009		2010		2011	FY 2012[1]	FY 2013	FY 2014	FY 2015
			Prog. EBS/09/108	Act.	Prog. EBS/10/18	Rev. Prog.		Proj.			
						(Percent of GDP)					
Revenue	18.6	18.5	18.0	18.6	18.5	18.3	18.8	19.4	19.7	19.9	20.2
Tax revenue	17.2	16.6	16.3	17.0	17.0	16.8	17.2	17.8	18.1	18.3	18.5
Income tax	5.0	4.7	4.5	5.2	4.6	4.6	4.8	4.8	5.0	5.1	5.2
Taxes on goods and services	8.7	8.8	8.4	9.0	8.8	8.9	9.0	9.2	9.2	9.2	9.2
Taxes on international trade	3.2	2.9	3.1	2.7	3.3	3.0	3.1	3.3	3.4	3.5	3.6
Other tax revenue	0.3	0.2	0.3	0.1	0.3	0.3	0.4	0.5	0.5	0.5	0.5
Nontax revenue	1.4	1.9	1.7	1.6	1.5	1.5	1.6	1.6	1.6	1.6	1.6
Expenditure and net lending	38.5	44.1	46.1	39.3	48.3	49.5	47.0	46.8	44.4	43.1	43.0
Current expenditure[2]	24.6	25.8	24.6	25.8	25.6	27.0	25.8	25.5	24.8	24.4	24.2
Salaries	10.7	11.4	11.2	11.7	11.6	12.2	12.0	11.9	11.5	11.2	11.0
Of which : priority sectors	5.3	6.1	6.7	7.1	7.4	7.3	7.3	7.4	7.5	7.6	7.8
Of which: security related	4.4	3.6	3.3	3.4	3.1	3.8	3.8	3.6	3.3	2.9	2.5
Of which : others	1.0	1.8	1.2	1.3	1.1	1.1	1.0	0.9	0.8	0.7	0.7
Other current expenditures	13.9	14.4	13.4	14.1	14.1	14.8	13.8	13.6	13.3	13.2	13.2
Of which : Election					0.1	0.8					
Externally financed special programs[3]	1.2	3.2	5.3	0.1	5.5	5.5	3.5	3.0	0.9	0.1	0.1
Of which : Election					2.5	2.5					
Capital expenditure & Net lending	12.7	15.1	16.3	13.3	17.1	17.0	17.8	18.3	18.6	18.6	18.7
Of which : MDRI-related			2.3	0.0	1.3	1.2	0.0	0.0	0.0	0.0	0.0
Overall balance (commitment basis)	-19.8	-25.6	-28.1	-20.7	-29.8	-31.2	-28.2	-27.4	-24.7	-23.2	-22.8
Overall balance (after grants, excl. HIPC)	-3.3	-3.7	-4.1	-5.2	-4.0	-3.1	-3.1	-1.8	-1.3	-1.3	-1.3
Change in arrears (reduction = –)	-2.1	-0.8	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liability related to new statutes for civil servants					0.0	-1.1	-1.1	0.0	0.0	0.0	0.0
Overall balance (cash basis)	-21.9	-26.4	-28.3	-20.7	-29.8	-32.3	-29.3	-27.4	-24.7	-23.2	-22.8
Overall balance (after grants, excl. HIPC)	-5.4	-4.5	-4.3	-5.2	-4.0	-4.3	-4.2	-1.8	-1.3	-1.3	-1.3
Financing	24.0	26.5	28.3	20.6	29.8	32.3	28.5	26.5	24.7	23.2	22.8
External grants	20.9	24.9	86.5	80.8	25.8	28.0	24.3	24.7	23.4	21.9	21.5
Of which : HIPC relief	3.8	3.0	62.5	65.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: MDRI grant from IMF	0.0	0.0	2.3	1.8	2.1	2.1	0.0	0.0	0.0	0.0	0.0
External borrowing, net	-0.9	0.2	-59.6	-64.4	2.7	2.7	2.2	2.2	2.0	1.9	1.9
Privatization proceeds	0.0	0.0	0.1	0.0	0.1	0.1	0.2	0.2	0.3	0.3	0.3
Domestic	4.0	1.4	1.3	4.2	1.2	1.5	1.7	-0.6	-1.0	-0.9	-0.9
Banking sector	3.1	1.4	1.3	4.6	1.2	0.2	0.6	-0.6	-1.0	-0.9	-0.9
Nonbank sector	0.9	0.0	0.0	-0.4	0.0	1.3	1.1	0.0	0.0	0.0	0.0
Financing gap and errors and omissions[4]	-2.1	-0.1	0.0	0.1	0.0	0.0	0.8	0.9	0.0	0.0	0.0
						(BIF billion)					
Total revenue	197.6	256.7	308.1	304.6	339.3	336.9	396.0	461.8	523.9	584.2	653.5
Total expenditure and net lending	407.9	611.7	789.6	642.7	886.6	910.8	989.7	1114.5	1180.7	1265.2	1391.8
Of which : salaries	114.0	158.4	192.2	191.8	212.4	224.5	253.1	283.7	307.1	327.6	356.7
Financing gap and errors and omissions[4]	-22.3	-0.8	0.0	1.0	0.0	0.0	17.3	21.8	0.0	0.0	0.0
Total financing	237.7	366.8	485.1	337.1	547.3	595.0	600.0	630.9	656.8	681.0	738.3
						(US$ million, unless otherwise indicated)					
Memorandum items:											
MDRI stock relief from IDA and AfDB	...	...	84.8	84.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
MDRI savings from IDA and AfDB:											
Amortization	...	...	2.3	2.3	3.0	3.0	3.2	3.3	3.3	3.3	3.4
Annual interest payments	...	...	0.5	0.5	0.6	0.6	0.6	0.6	0.6	0.5	0.5
Propoor expenditure (percent of GDP)	12.0	15.1	9.9	16.8	18.6	18.6	18.9	19.2	19.2	19.6	20.1
Public debt (percent of GDP)	178	154	49	48	51	51	51	47	44	41	39
GDP at current market prices (BIF billion)	1060	1386	1711	1637	1836	1841	2104	2381	2662	2936	3238

Sources: Burundi authorities and IMF staff estimates and projections.

1 The authorities plan to move from a calendar year to a fiscal year in line with the EAC requirement.

2 The medium-term current spending projections are mostly driven by health, education, food security, and agriculture expenditures.

3 These are externally financed expenditures, which include spending on elections (in 2010), demobilization, and one-off temporary social safety net programs.

4 Expected to be financed by additional donor support.

Table 4. Burundi: Monetary Survey, 2007–10

	2007	2008	2009		2010	
			Proj. EBS/09/108	Act.	Prog. EBS/10/18	Rev. Prog.
			(BIF billion)			
Net foreign assets	109.1	181.5	182.9	168.8	192.0	184.6
Central bank	75.6	139.4	87.3	118.7	113.3	129.8
Deposit money banks	33.5	42.0	95.6	50.0	78.7	54.8
Net domestic assets	298.7	368.9	438.9	500.3	516.4	570.7
Domestic credit	374.1	436.1	505.5	559.2	574.4	619.1
Net claims on the government	157.4	176.5	198.1	252.4	219.4	255.9
Of which: on the Treasury				268.8	…	272.3
Credit to the economy	216.6	259.7	307.4	306.8	355.0	363.1
Other items, net (assets = +)	-75.4	-67.2	-66.6	-58.9	-58.0	-48.4
M3	407.8	550.4	621.9	669.1	708.3	755.3
Foreign currency deposits	77.7	107.3	115.0	138.3	124.0	160.8
M2	330.1	443.1	506.9	530.8	584.3	594.5
Currency in circulation	84.2	112.6	135.2	120.9	137.9	136.9
Local currency deposits	245.9	330.5	371.7	409.9	446.4	457.6
Demand deposits	151.2	223.3	244.7	283.5	304.9	314.9
Quasi-money	94.7	107.2	127.0	126.4	141.5	142.7
	(Change as percent of beginning of period M2)					
Net foreign assets	11.5	21.9	0.3	-2.9	0.5	3.0
Central bank	11.4	19.3	-11.7	-4.7	-0.4	2.1
Deposit money banks	0.1	2.6	12.1	1.8	1.0	0.9
Net domestic assets	7.0	21.3	15.8	29.7	13.2	13.3
Domestic credit	6.6	18.8	15.7	27.8	11.9	11.3
Net claims on the government	-0.2	5.8	4.9	17.1	4.1	0.7
Credit to the economy	6.8	13.0	10.8	10.6	7.9	10.6
Of which: private sector	7.6	8.5	6.2	13.7	7.9	10.6
Other items, net (assets = +)	0.4	2.5	0.1	1.9	1.3	2.0
M3	18.5	43.2	16.1	26.8	13.7	16.2
Foreign currency deposits	8.5	9.0	1.7	7.0	1.7	4.2
M2	10.1	34.2	14.4	19.8	12.0	12.0
Currency in circulation	5.2	8.6	5.1	1.9	3.1	3.0
Local currency deposits	4.8	25.6	9.3	17.9	8.9	9.0
Demand deposits	1.2	21.8	4.8	13.6	6.1	5.9
Quasi-money	3.6	3.8	4.5	4.3	2.8	3.1
Memorandum items:						
Reserve money (12–month percent change)	17.4	25.1	13.5	26.6	11.5	10.6
Velocity (GDP/M2; end of period)	4.2	3.1	3.4	3.1	3.1	3.1

Sources: Burundi authorities and IMF staff estimates and projections.

Table 5. Burundi: Central Bank Accounts, 2008–10

	2008				2009				2010			
	Mar.	June	Sep.	Dec.	Mar.	June	Sep.	Dec.	Mar.	June	Sep.	Dec.
									Act.	Rev. Prog.		
	(BIF billion)											
Net foreign assets	68.1	63.4	75.1	139.4	105.1	148.8	113.0	118.7	105.3	95.0	100.1	129.8
Net domestic assets	50.2	71.6	71.4	17.0	33.6	13.9	44.8	79.3	49.8	83.3	91.5	89.2
Domestic credit	127.5	149.0	146.9	114.1	108.0	119.4	122.5	187.5	136.1	172.7	186.4	193.9
Net claims on the government	124.0	143.3	141.4	120.8	110.3	113.3	116.4	191.7	151.8	178.1	190.1	190.1
Other credit	3.4	5.6	5.4	-6.6	-2.3	6.2	6.1	-4.2	-15.7	-5.3	-3.6	3.8
Other items, net (assets = +)	-77.3	-77.3	-75.6	-97.2	-74.4	-105.5	-77.7	-108.2	-86.3	-89.4	-94.9	-104.7
Reserve money	118.3	135.1	146.5	156.4	138.7	162.7	157.9	198.0	155.1	178.3	191.6	219.0
Currency in circulation	80.6	99.3	110.4	112.6	99.9	108.0	104.5	120.9	109.5	104.5	115.5	136.9
Bank reserves	23.5	18.9	17.3	25.0	22.2	37.2	35.9	53.9	26.4	60.3	58.6	58.8
Cash in vault	9.1	9.9	12.6	11.6	12.7	12.6	13.4	15.3	15.9	13.4	13.4	15.3
Other nonbank deposits	5.1	7.1	6.2	7.2	3.8	4.9	4.1	7.9	3.3	0.1	4.1	7.9
Memorandum items:												
Net foreign assets of BRB (US$ million)	57.8	53.1	63.1	112.9	85.1	120.9	91.8	96.5	85.6	76.2	79.3	101.5

Sources: Burundi authorities and IMF staff estimates and projections.

Table 6. Burundi: Balance of Payments, 2007–15

	2007	2008	2009	2010	2011	2012	2013	2014	2015
						Proj.			
				(US$ million)					
Current account	-153.4	-142.7	-193.4	-132.2	-168.5	-176.4	-186.9	-196.5	-207.6
(excluding official transfers)	-364.4	-379.6	-335.4	-426.9	-457.5	-460.6	-474.7	-488.0	-506.7
Trade balance	-242.0	-281.3	-194.4	-266.2	-295.0	-295.3	-307.0	-318.0	-338.6
Exports, f.o.b.	52.9	60.9	74.0	89.0	88.5	99.6	103.7	118.2	124.9
Of which: coffee	32.6	40.1	47.3	61.7	63.3	73.4	76.4	89.2	93.7
Imports, f.o.b.	-295.0	-342.2	-268.5	-355.2	-383.5	-394.9	-410.8	-436.3	-463.5
Of which: petroleum products	-58.4	-105.2	-80.6	-108.0	-120.2	-131.9	-140.1	-148.4	-157.2
Services (net)	-145.6	-186.3	-214.2	-227.4	-232.5	-237.4	-243.5	-249.9	-252.3
Income (net)	-5.9	-4.3	6.3	-6.9	-6.9	-8.4	-8.7	-8.9	-9.1
Current transfers (net)	240.1	329.3	209.0	368.3	365.9	364.7	372.3	380.3	392.4
Of which: official (net)	211.0	237.0	141.9	294.8	289.0	284.2	287.8	291.4	299.1
Capital account[1]	127.4	143.9	1224.6	143.2	161.3	167.5	166.0	179.1	190.8
Of which: HIPC relief	39.4	39.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: debt forgiveness			1057.1						
Of which: other transfers (MDRI grant)	0.0	0.0	51.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	65.5	51.0	-974.5	-22.6	9.5	8.1	43.5	38.1	25.0
Direct investment	0.5	13.6	10.2	12.7	12.7	12.6	12.6	13.2	13.8
Other investment	65.1	37.4	-984.8	-35.3	-3.2	-4.6	31.0	25.0	11.2
Assets	-45.0	-30.8	-41.0	-31.7	-35.2	-32.1	-32.4	-29.9	-31.2
Liabilities	110.0	68.2	-943.8	-3.7	31.9	27.6	63.3	54.9	42.4
Of which: SDR allocation			95.1						
Errors and omissions	-9.5	33.5	-2.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	30.0	85.8	54.7	-11.6	2.3	-0.9	22.6	20.7	8.2
Financing (increase in assets = –)	-30.0	-85.8	-54.7	11.6	-15.3	-14.6	-22.6	-20.7	-8.2
Of which: change in official reserves	-47.2	-89.8	-54.7	12.4	-17.3	-14.6	-19.8	-15.9	-14.5
Of which: SDR allocation			-95.1						
Financing gap[2]	0.0	0.0	0.0	0.0	13.1	15.4	0.0	0.0	0.0
				(Percent of GDP, unless otherwise indicated)					
Memorandum items:									
Current account	-15.7	-12.3	-14.5	-9.0	-10.6	-10.5	-10.4	-10.2	-10.1
Gross official reserves									
US$ million	177.3	266.6	323.0	310.7	327.9	342.5	362.3	378.2	392.7
Months of imports	3.8	6.5	6.5	6.0	6.0	6.0	6.0	6.0	6.0
Total external debt	155	134	27	29	31	31	30	30	29
Coffee price (US cents per lb)	123	138	142	133	127	116	115	112	112
Nominal GDP (US$ million)	975	1165	1330	1467	1583	1684	1804	1922	2048

Sources: Burundi authorities and IMF staff estimates and projections.

[1] Based on preliminary information provided by donors.

[2] Expected to be financed by additional donor support.

Table 7. Burundi: Banking System Soundness Indicators, 2005–10

(percent, unless otherwise indicated)

	2005 Dec.	2006 Dec.	2007 Dec.	2008 Dec.	2009 Dec.	2010 Jan.	2010 Feb.	2010 Mar.
Capital Requirement								
Capital requirement over weighted assets (solvency ratio)	18.3	13.5	13.5	15.2	19.1	19.5	18.9	18.8
Core capital (Tier 1 capital) over weighted assets [1]	16.6	7.5	10.9	12.7	15.5	15.8	15.4	15.4
Quality of assets								
Nonperforming loans (percent of total gross loans granted)	20.6	18.6	18.8	14.6	13.0	13.0	12.6	12.7
Provisions (percent of nonperforming loans)	83.0	92.4	91.4	90.2	88.7	87.1	86.3	82.2
Nonperforming loans net of provisions (percent of capital)	20.4	7.5	7.4	7.4	5.4	6.0	6.3	8.4
Large exposures (percent of capital)	34.3	48.6	41.6	39.3	28.2	27.7	33.0	21.3
Profitability rates								
Return on assets	1.9	1.7	2.3	2.3	2.6	1.2	0.4	0.5
Return on equity capital	14.1	17.5	26.4	29.7	22.8	0.1	3.3	4.7
Net interest (percent of gross results)	172.7	177.4	167.6	171.8	207.0	233.8	211.5	219.2
Costs excluding interest (percent of gross outturn)	193.6	188.9	156.6	155.8	172.3	192.8	186.8	174.4
Liquidity								
Liquid assets (percent of all loans granted)	75.6	68.1	83.5	86.9	91.4	80.0	99.4	84.2
Liquid assets (percent of short-term commitments)	118.1	106.8	135.2	137.9	168.8	158.1	191.1	150.9

Sources: Burundi authorities and IMF staff estimates.

[1] The decrease is due to the revision of Article 2 in Directive No. 2/06 of November 24, 2006.
It is related to the calculation of basic equity capital, which no longer includes general provisions for risks.

Table 8. Burundi: Actual and Projected Schedule of ECF Disbursements and Reviews, 2008–11

Date	Disbursement (SDR million)	Conditions
July 15, 2008	6.6	Executive Board approval
February 9, 2009	6.6	Completion of first review, based on observance of performance criteria at end-September 2008.
July 13, 2009	6.6	Completion of second review, based on observance of performance criteria at end-March 2009.
February 10, 2010	6.6	Completion of third review, based on observance of performance criteria at end-September 2009.
July 19, 2010	6.6	Completion of fourth review, based on observance of performance criteria at end-March 2010.
January 15, 2011	6.6	Completion of fifth review, based on observance of performance criteria at end-September 2010.
June 30, 2011	6.6	Completion of sixth review, based on observance of performance criteria at end-March 2011.
Total for the ECF arrangement	46.2	

Source: IMF staff.

APPENDIX I
TRANSLATED FROM FRENCH

BURUNDI
LETTER OF INTENT

Bujumbura, July 7, 2010

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C., 20431

Dear Mr. Strauss-Kahn:

1. On July 7, 2008, the Executive Board of the International Monetary Fund (IMF) approved a three-year arrangement under the Extended Credit Facility (ECF) for the Republic of Burundi. This agreement supports of the medium-term program (from April 1, 2008 to March 31, 2011) to consolidate the macroeconomic stabilization process, reduce poverty, promote structural reforms and strengthen governance. In accordance with the terms of this arrangement, the government discussed program implementation for the fourth review under the arrangement with a mission from the IMF. The discussions focused on the implementation of the program during the period from October 1, 2009 to March 31, 2010, as well as the outlook and economic and financial measures to be implemented in 2010.

2. On the political front, the government continues to make every effort to consolidate the peace process. Within this framework and assisted by development partners, the government of Burundi has taken all the necessary steps to ensure the success of the elections to be held between May 24 and September 8, 2010.

3. On the economic and social front, the government is pleased to report that implementation of the program has been satisfactory, despite the difficult international situation resulting from the global financial crisis, and the domestic situation marked by teachers' strikes and drought in the northern part of the country. In particular, all quantitative performance criteria and the structural benchmark for end-March 2010 were met.

4. The government is resolved to continue implementing the policies and measures described in the Poverty Reduction Strategy Paper (PRSP). The Memorandum on Economic and Financial Policies (MEFP) attached to this letter complements those preceding it since June 24, 2008.

5. The government believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of its program. It will take any further measures that may become appropriate for this purpose. The Burundian authorities will consult the IMF on the adoption of such measures in advance of revisions to the policies contained in the MEFP, in accordance with IMF policies on such consultations.

6. The government of Burundi will provide the IMF with such information as it may request to monitor the progress made in economic and financial policy implementation. It will also carry out reviews of the ECF-supported program with the IMF every six months. The fifth review should be completed no later than January 2011 and the sixth and final review no later than June 2011.

7. In view of the considerable progress made in implementing the ECF-supported program, the government is requesting completion of the fourth review and the fifth ECF disbursement in an amount equivalent to SDR 6.6 million. The government is also requesting modification of the end-September performance criteria to reflect the revised program.

8. As in the past, the Burundian authorities wish to make this letter available to the public, along with the attached MEFP and the Technical Memorandum of Understanding (TMU), as well as the IMF staff report on the fourth ECF review. We therefore authorize their publication and posting on the IMF website, subject to Executive Board approval. These documents will also be posted on the official sites of the government of Burundi.

Sincerely yours,

/s/
Clotilde NIZIGAMA
Minister of Finance

/s/
Gaspard SINDAYIGAYA
Governor, Bank of the Republic of Burundi

/s/
Gabriel NTISEZERANA
Second Vice President, Republic of Burundi

Attachments: Memorandum of Economic and Financial Policies (MEFP)
Technical Memorandum of Understanding (TMU)

APPENDIX I
ATTACHMENT I
TRANSLATED FROM FRENCH

BURUNDI
MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

Bujumbura, July 7, 2010

I. INTRODUCTION

1. This Memorandum of Economic and Financial Policies (MEFP) complements the preceding MEFPs since June 24, 2008. It reviews program implementation and updates the medium-term outlook and economic and financial policies that will be implemented in 2010 within the framework of the program covering April 1, 2008 to March 31, 2011. The measures and objectives contained in this MEFP are compatible with the Poverty Reduction Strategy Paper (PRSP) published in September 2006 and the findings of the annual PRSP implementation report sent to the IMF and the World Bank in December 2009.

2. Economic policy will continue to be guided by the following objectives: (1) maintain single-digit inflation; (2) improve the composition of public spending to the benefit of priority sectors, while preserving fiscal sustainability; (3) strengthen public financial management (PFM) and good governance; and (4) strengthen the internal control systems of the central bank.

3. With the continued improvement in the security situation, the macroeconomic objectives are as follows for the period of the ECF: (1) GDP growth should average approximately 5 percent over the medium term, compared to the 2007–09 average of approximately 4 percent; (2) average inflation should slow to about 5 percent in 2014; and (3) gross official reserves should stabilize at about six months of import coverage in the medium term, in accordance with the convergence criteria of the East African Community (EAC).

II. PROGRAM IMPLEMENTATION

4. The global financial crisis has slowed Burundi's economy and contributed to a strong decline in inflation. Economic growth slowed to 3.5 percent in 2009 from 4.5 percent in 2008, mainly due to a decline in remittances and foreign direct investments. In line with falling world food and fuel prices, end-of-period inflation fell from about 26 percent in 2008 to about 4.5 percent in 2009. The current account deficit widened, reaching 14.5 percent of GDP, with the delays in donor support outweighing the positive effect of lower food and fuel prices. Gross official reserves in 2009 remained broadly stable, at about 6.5 months of import coverage.

5. The overall fiscal deficit (cash basis, including non-HIPC grants) is estimated at about 5.2 percent of GDP, above the target of 4.3 percent. Domestic revenues accounted for 18.6 percent of GDP, compared to the program target of 18 percent of GDP. Total spending was lower than programmed by about 7 percentage points of GDP, due to lower externally-financed spending. The 2009 wage bill was kept within the envisaged budgetary envelope.

6. The monetary situation was characterized by stronger than expected growth of broad money, due to strong growth in domestic credit. Reserve money was also larger than expected because net foreign assets of the central bank declined by less than expected.

7. Performance of the ECF-supported program was generally satisfactory. All indicative targets for end-December 2009 were met, with the exception of the indicative target on reserve money. All quantitative performance criteria for end-March 2010 were met.

8. In close collaboration with development partners, the government is strongly pursuing structural reform, notably the promotion of transparency and good fiscal management, financial sector reform, coffee sector reform, and the improvement of the business environment. In addition to the achievements described in the preceding memoranda, significant progress has been achieved in all of these areas since the third review.

9. In the area of PFM, the action plan of the PFM strategy for 2010 and 2011 has been revised. In accordance with the new Organic Law on Public Finance, a new convention between the government and the BRB has been signed and a draft General Regulation on Public Budget Management has been finalized and sent to the Cabinet. To strengthen cash flow management, a Cash Flow Management Committee has been created and the "Office of Cash Flow Management" has been reorganized. This has allowed the regular preparation of monthly and weekly cash flow plans, which are now harmonized with the commitment plan. Rationalization of government accounts is making steady progress, without interfering with the smooth operation of the units concerned. In this context, a new government account inventory operation was launched, allowing identification of 55 accounts to be closed before end-June 2010 and 34 others to be closed by end-December 2010 at the latest. To modernize revenue administration, efforts are under way to make the Burundi Revenue Authority (BRA) fully operational. Specifically, 22 key posts have been filled, including those of commissioner general and assistant commissioner general, as well as tax commissioners and customs commissioners. With respect to customs, the SYDONIA++ computer system has been expanded to other customs posts, and installation of the RADDEX system will allow better accounting of customs revenues at the EAC level.

10. Significant steps have been taken to continue to improve transparency in PFM. In the area of public procurement, an Executive Director and support personnel have been named to the Public Procurement Regulatory Authority. Moreover, annual plans for procurement have been prepared to facilitate transparent budget implementation. Regarding budget classification, a new nomenclature was introduced with the 2010 budget to make it consistent with the new chart of accounts. In the areas of control and audit, the final report of the auditor general on implementation of the 2008 budget has been finalized.

11. In the financial sector, the process of developing the Financial Sector Reform Strategy (FSRS) has been launched with the creation of the National Strategy Committee (NSC) by order of the Minister of Finance. Adoption of the FSRS by the Cabinet is expected in the first quarter of 2011. A plan to develop the financial market in Burundi is also being prepared. In the area of foreign exchange, improvements have been made to the symmetrical foreign exchange auction market (*Marché des Enchères Symétrique en Devises (MESD)*). Accordingly, the central bank now systematically publishes complete information after each MESD session in order to

increase the representativeness of the exchange rate, reduce its rigidity and increase its transparency. Likewise, the MESD room has been computerized to increase the efficiency of the daily sessions. In the area of monetary policy, the central bank is preparing to introduce REPO trading as an instrument of monetary policy. For this purpose, the associated regulatory texts (Global Master Repurchase Agreement, Code of Conduct and Operations Guide) have been drafted and discussed with the banks.

12. In the area of banking supervision, on-site inspections are now conducted according to risk-based supervisory procedures, but a detailed supervisory handbook remains to be prepared to better guide the supervisors. All banks and all financial institutions respect the minimum capital requirements of BIF 5 billion and BIF 4 billion respectively. Moreover, the process to mobilize funds in order to increase capital to 10 billion BIF by end-December 2010 has advanced. In the area of safeguard measures, an international auditor was recruited at end-June, 2010 to (1) track the complete implementation of all recommendations formulated by the special audits of 2008, based on the September 2009 action plan prepared by the BRB and the Ministry of Finance; and (2) perform special audits of the controls on important disbursements and transfers on behalf of the government or its creditors during the first half of 2010.

13. With respect to the reform of the coffee sector, invitations to bid for 117 coffee washing stations, grouped together into 29 lots, were published on June 5, 2009, and the bids were opened on August 6, 2009. Investors showed limited interest and only 13 washing stations were sold as the result of this process. The government has already decided to reissue the invitations to bid at the end of the current coffee campaign.

14. Significant measures have been taken to improve the business environment. In particular, the revision of the Commercial Code now underway is intended to facilitate business by simplifying procedures and increasing alignment with international standards with regard to business law. The competition law, which focuses on the required harmonization of taxes within COMESA and the EAC, defines and provides sanctions for unfair practices in the conduct of business. Finally, the creation of the Agency to Promote Investments (API) will contribute to strengthening the confidence of national and foreign investors by guaranteeing respect for the application of Investment Code directives.

III. Economic Prospects and Policies for 2010

15. The revised macroeconomic framework for 2010 is as follows: (1) GDP growth is expected to pick up slightly to 3.9 percent; (2) end-of-period inflation is expected to be around 9.5 percent; and (3) gross official reserves are expected to stabilize at six months of import coverage. The government will implement all tax, public spending, monetary and foreign exchange and structural policies as described below and in the January 21, 2010, MEFP.

16. It is essential to raise sufficient domestic revenue to ensure fiscal sustainability and to increase poverty-reducing expenditures. Accordingly, the government will take special measures to make the BRA fully operational as soon as possible. To ensure that the revenue target is achieved, major fiscal and administrative policy measures will also be taken. In particular, the government has already increased the VAT taxable base on petroleum products to comply with the law on the VAT. The general tax base will also be expanded by: (1) rigorous monitoring of exemptions; (2) establishment of the investigation and research unit; (3) strengthening of cross-

checking between customs and government procurement; and (4) recovery of arrears and rigorous monitoring of tax filing obligations of enterprises. The government will also expedite the implementation of IMF technical assistance recommendations on VAT implementation. In the area of customs, the ex ante controls of customs valuations and post-declaration audits will be strengthened with assistance from an import verification firm.

17. The primary objective of expenditure policy in 2010 is to significantly improve the composition of public spending in favor of priority sectors in order to accelerate progress toward the MDGs. Accordingly, pro-poor spending is expected to increase by about 1.8 percent of GDP. To protect priority spending, the government has identified non-priority spending that will be cut if there is a decline in revenues or financing.

18. In consultation with IMF staff, the program has been revised to take into account: (1) the new law on security force remuneration; (2) the cost of the 2010 general elections; and (3) emergency spending due to the drought. These three elements have resulted in an increase in public spending of about 1.2 percent of GDP compared to the initial program and in an increase in domestic financing. The program revision also reflects the government's decision to issue bonds to eliminate the liabilities resulting from the retroactive implementation of the civil service statutes (2.4 percent of 2010 GDP) during 2010–11.

19. The 2010 government wage bill is currently expected to be 12.2 percent of GDP. The government will continue its objective of bringing the wage bill below 11 percent over the medium term. Since recruitment in the education and health sectors affects progress towards the MDGs, the wage bill for these sectors will continue to grow, due to the enormous needs for teachers and health personnel. Thus, achievement of the medium-term wage bill target will depend on continued demobilization. In light of the political and social implications of this operation, it may not be possible to address these issues until after the 2010 elections.

20. In support of fiscal policy, the government will strengthen the implementation of the sliding quarterly cash flow plan. Harmonization of expenditure commitment and cash flow plans will take place at the beginning of each quarter and the results will be submitted to the Minister of Finance for approval. In this context, all budget spending will require the prior authorization of the Minister of Finance and be executed strictly on the basis of financing availability. A quarterly budget allocation will be defined for each ministry, with strict expenditure prioritization.

21. Given the high risk of debt distress and low capacity, Burundi will seek only concessional external financing or grants. The government will not contract any nonconcessional foreign debt and will ensure that all loans contracted have a grant element of at least 50 percent.

IV. Program Monitoring

22. Program implementation will continue to be subject to half-yearly reviews, performance criteria, indicative targets, and structural benchmarks as specified in Tables I.1 to I.4. The information to be reported to the IMF and the definitions of the pertinent variables can be found in the attached TMU. The government is also ready to adopt, in consultation with IMF staff, any new financial or structural measures necessary for the program's success.

Table I.1. Burundi: Performance Criteria and Indicative Targets for 2009

(BIF billion, unless otherwise indicated)

	2008	2009											
	Dec.	Mar.			Jun.[1]			Sep.			Dec.[1]		
	Act.	Prog.	Prog. Adj.	Act.	Prog.	Prog. Adj.	Act.	Prog.	Prog. Adj.	Act.	Prog.	Prog. Adj.	Act.
Performance Criteria													
Net foreign assets of the BRB (floor; US$ million) [2]	112.9	15.4	-17.9	85.1	35.0	4.1	120.9	40.0	-20.0	91.8	69.0	22.0	96.5
Net domestic assets of the BRB (ceiling)[2]	17.0	126.7	166.3	33.6	122.6	159.8	13.9	127.4	200.0	44.8	90.2	149.7	79.3
Net domestic financing of the government (ceiling) [2]	19.0	36.5	76.1	-7.9	46.9	84.1	-3.3	61.2	133.8	6.9	21.7	81.2	68.7
External payments arrears of the government (ceiling; US$ million) [3]	0.0	0.0		0.0	0.0		0.0	0.0		0.0	0.0		0.0
Short-term external debt of the government (ceiling; US$ million) [3]	0.0	0.0		0.0	0.0		0.0	0.0		0.0	0.0		0.0
Nonconcessional external debt contracted or guaranteed by the government or the BRB (ceiling; US$ million; cumulative from beginning of calendar year; US$ million) [3]	0.0	0.0		0.0	0.0		0.0	0.0		0.0	0.0		0.0
Indicative targets													
Accumulation of domestic arrears (ceiling; cumulative from beginning of calendar year)	2.3	0.0		1.2	0.0		0.0	0.0		0.0	0.0		0.0
Reserve money (ceiling)	…	145.0		138.7	164.7		162.7	175.8		157.9	177.5		198.0
Memorandum item:													
External nonproject financial assistance (US$ million; cumulative from beginning of calendar year)	113.3	33.3		0.0	33.7		2.8	64.2		2.8	105.8		58.8

Sources: Burundi authorities and IMF staff estimates.

[1] Indicative targets.

[2] The ceiling or the floor will be adjusted as indicated in the TMU.

[3] Continuous performance criterion.

Table I.2. Burundi: Performance Criteria and Indicative Targets for 2010

(BIF billion, unless otherwise indicated)

	2009	2010								
	Dec.	Mar.			Jun.[1]		Sep.		Dec.[1]	
	Act.	Prog.	Prog. Adj.	Act.	Prog.	Rev. Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.
Performance Criteria										
Net foreign assets of the BRB (floor; US$ million) [2]	96.5	59.6	59.6	85.6	52.8	76.2	67.4	79.3	86.1	101.5
Net domestic assets of the BRB (ceiling) [2]	79.3	74.8	74.8	49.8	87.6	83.3	90.5	91.5	88.1	89.2
Net domestic financing of the government (ceiling) [2]	68.7	58.0	58.0	-34.6	89.6	71.1	80.7	83.7	21.2	27.5
External payments arrears of the government (ceiling; US$ million) [3]	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Short-term external debt of the government (ceiling; US$ million) [3]	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Nonconcessional external debt contracted or guaranteed by the government or the BRB (ceiling; US$ million, cumulative from beginning of calendar year) [3]	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Indicative targets										
Accumulation of domestic arrears (ceiling; cumulative from beginning of calendar year)	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Reserve money (ceiling)	198.0	150.9		155.1	155.8	178.3	178.2	191.6	201.4	219.0
Propoor spending (floor; cumulative from beginning of calendar year)	274.8	50.1		64.5	105.4	105.4	200.7	200.7	342.2	342.2
Memorandum item:										
External nonproject financial assistance (US$ million; cumulative from beginning of calendar year)	58.8	11.2		35.0	11.2	46.2	72.2	107.2	151.0	186.0

Sources: Burundi authorities and IMF staff estimates and projections.

[1] Indicative targets.

[2] The ceiling or the floor will be adjusted as indicated in the TMU.

[3] Continuous performance criterion.

Table I.3. Burundi: Performance Criteria and Structural Benchmarks for 2009

Measures	Condition type and date	Status	Macroeconomic Rationale
Fiscal management			
Resumption of payroll management by the Ministry of Finance by taking charge of the payroll database.	Performance criterion (March 31, 2009)	Completed	Efficient wage bill management is essential for focusing spending in priority areas, while enhancing fiscal sustainability. Wage bill management is being reinforced through the creation of a single wage data management and elimination of ghost employees.
Close and transform into sub accounts for special allocation from the general treasury account the off-budget accounts mentioned in the finance minister's letter No. 540/4904/2008 of November 12, 2008.	Structural benchmark (September 30, 2009)	Completed	Implementation of a single treasury account is key to sound public financial management.
Close the accounts mentioned in the finance minister's letter No. 540/4768/2008 of October 31, 2008.	Structural benchmark (September 30, 2009)	Completed	Implementation of a single treasury account is key to sound public financial management.
Prepare and implement a sliding quarterly cash-flow plan.	Structural benchmark (June 30, 2009)	Completed with delay.	Enhance budget execution and ensure coordination of monetary and budget policies.
Revenue administration and tax policy			
Introduce VAT and the common external tariff.	Structural benchmark (July 31, 2009)	Completed	To raise the efficiency of tax collection, and offset potential losses on customs revenue due to the accession to EAC.
Fiscal governance			
In accordance with the laws of Burundi, the BIF 6 billion and the deeds for 25 properties belonging to INTERPETROL that have been placed under seal will remain in place until a court decision has been reached on the INTERPETROL case.	Structural benchmark (continuous)	Completed	Enhance fiscal governance to ensure continuation of budget support.

Table I.4. Burundi: Structural Benchmarks for 2010

Proposed Measures	Dates	Status	Rationale
Public Financial Management			
Adopt a new “convention” between the Ministry of Finance and the BRB redefining the role of the central bank in public financial management, as stipulated under the new budget organic law.	March 31, 2010	Completed	Key to implementing the new budget organic law.
Prepare a final report on the closing of government accounts.	December 31, 2010[1]		Implementation of a single treasury account is key to sound public financial management.
Central Bank and Treasury Safeguard measures			
Recruit an international auditor to: (i) monitor the full implementation of all the recommendations formulated in Deloitte's 2008 special audit reports (consistent with the September 2009 agreed-upon action plan between Burundi's central bank and the Ministry of Finance); and (ii) verify on a test basis the controls on significant domestic disbursements and transfers executed by the central bank on behalf of the government or its creditors during the first half of 2010.	June 30, 2010	Completed	To enhance the safeguard measures in force at the central bank and the Treasury.
Submit to the General Council, the audit committee, and the Minister of Finance the report on special audits of the controls on important domestic disbursements and transfers—on behalf of the government or its creditors— that took place in the first half of 2010.	December 31, 2010		To enhance the safeguard measures in force at the central bank and the Treasury.
Fiscal Governance			
In accordance with the laws of Burundi, the BIF 6 billion and the deeds for 25 properties belonging to INTERPETROL that have been placed under seal will remain in place until a court decision has been reached on the INTERPETROL case.	Structural benchmark (continuous)	Completed	Enhance fiscal governance to ensure the continuation of budget support.

[1] The date of this structural benchmark has been changed from September to December to ensure that the final report does cover the closing of government accounts that will take place in the last quarter of 2010.

APPENDIX I
ATTACHMENT II
TRANSLATED FROM FRENCH

BURUNDI
TECHNICAL MEMORANDUM OF UNDERSTANDING

Bujumbura, July 7, 2010

1. This technical memorandum of understanding covers the agreements on monitoring implementation of the program supported by the Extended Credit Facility (ECF) Arrangement. It sets out the definitions of program variables to monitor implementation of the program and the reporting requirements for the government of Burundi and the Bank of the Republic of Burundi (BRB). It defines quantitative performance criteria, indicative targets, and applicable adjusters.

A. Quantitative Program Targets

Quantitative performance criteria and indicative targets

2. **The quantitative performance criteria for the program as shown in the MEFP are as follows**:

- net foreign assets of the BRB (floor);
- net domestic assets of the BRB (ceiling);
- net domestic financing of the government (ceiling);
- external payment arrears of the government (ceiling, continuous);
- stock of short-term external debt (maturity of less than one year) of the government and the BRB (ceiling, continuous); and
- new nonconcessional medium- and long-term external debt contracted or guaranteed by the government or the BRB (ceiling, continuous).

3. **The quantitative indicative targets for the program, shown in the MEFP, are as follows**:

- accumulation of domestic arrears (ceiling);
- propoor spending (floor); and
- reserve money (ceiling).

Definitions and measurement

4. **The net foreign assets of the BRB** are defined as the difference between (i) gross official reserves (valued at market prices) and other claims; and (ii) foreign exchange liabilities to nonresident entities (including the use of Fund resources, and liabilities arising from the use of any SDR allocation). The gross official reserves of the BRB are defined as those foreign assets that are liquid and freely available to the BRB.

5. **The net domestic assets of the BRB** are defined as the difference between (i) reserve money, comprising currency in circulation, reserves of commercial banks, and other deposits held at the BRB; and (ii) net foreign assets of the BRB.

Adjuster for changes in the compulsory reserves coefficients

6. The ceiling on net domestic assets of the BRB will be adjusted symmetrically for any change in the compulsory reserves coefficient applied to deposits in commercial banks by the amount of the new coefficient minus that stipulated in the program, multiplied by bank deposits subject to compulsory reserves. The rate stipulated in the program is currently 3 percent.

7. **Net domestic financing of the government** is defined as the change in (i) outstanding loans, advances, and other credit to the government from the BRB and all of Burundi's commercial banks; (ii) plus the stock of all government securities held by the nonbank public denominated in Burundi francs, including that held by nonresidents; (iii) less government deposits held in the BRB or in Burundi's commercial banks. The coverage of government is defined as central government and any other special funds or operations that are part of the budgetary process or have a direct impact on the government's financial position.

8. The stock of **external payment arrears** for program monitoring purposes is defined as the end-of-period amount of external debt service due and not paid within the grace period defined by a creditor, including contractual and late interest, for which a clearance agreement is not in place or for which arrears are not reschedulable. For arrears to exist, a creditor must claim payment of amounts due and not paid. Amounts in dispute are not considered arrears. Arrears for which a clearance framework has been agreed with the creditor or which are subject to rescheduling or restructuring are not considered arrears for program monitoring purposes. Program arrears would include any debt service due under such agreements that has not been paid.

9. The program includes a ceiling on **new nonconcessional external debt** contracted or guaranteed by the government and the BRB. This performance criterion applies to the contracting or guaranteeing by the central government, local governments, or the BRB of new nonconcessional external debt (as specified below) with an original maturity of one year or more, including commitments contracted or guaranteed for which value has not been received. Debt contracted by state-owned enterprises is included in the overall ceiling, if guaranteed by the government. The term "debt" shall be understood as defined in the

Executive Board Decision No. 12274, Point 9 as revised on December 1, 2009, (Decision No. 14416-(09/91). Debt rescheduling and restructuring are excluded from the criterion. Included are financial leases and other instruments giving rise to external liabilities, contingent or otherwise, on nonconcessional terms. In determining the level of concessionality of these obligations, the definition of concessional borrowing shall apply. Concessional debt is defined as having a grant element of 50 percent or more. The grant element of debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of contracting is calculated by discounting the future stream of payments of debt service due on this debt. The calculation of concessionality will take into account all aspects of the loan agreement, including maturity, grace period, payment schedule, upfront commissions, and management fees. For loans with a maturity of at least 15 years, the 10-year average commercial interest reference rates (CIRRs) published by the OECD should be used as the discount rate for assessing the level of concessionality, while the 6-month average CIRRs should be used for loans with shorter maturities. To both the 10-year and the 6-month average CIRRs, the following margins should be added: 0.75 percent for repayment periods of less than 15 years; 1 percent for 15–19 years; 1.15 percent for 20–29 years; and 1.25 percent for 30 years or more. The performance criterion is defined to exclude the use of Fund resources and any Burundi franc-denominated treasury securities held by nonresidents.

10. **The stock of short-term external debt** with a maturity of less than one year owed by the central government is to remain at zero under the program. Normal import credits are excluded from this ceiling. Loans with an initial maturity, as recorded in the original loan agreement, of one year or more are considered medium-term or long-term loans. This performance criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt, adopted August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received (including leases). Excluded from this performance criterion are rescheduling arrangements, borrowing from the IMF, and any Burundi franc-denominated treasury securities held by nonresidents. As of September 2007, the stock of short-term debt outstanding was nil.

11. Consistent with the PRSP, the authorities' definition of propoor spending is based on three criteria: (i) social character of spending, based on the administrative classification of spending (this includes "social services" spending and part of "general services" and "economic services" spending if it has a social character component); (ii) consistency with one of the four PRSP pillars; and (iii) propoor investment spending, financed by donors.

12. **The accumulation of domestic arrears** is measured by the accumulation of non-executed payment orders older than 60 days.

External financial assistance adjustor

13. The program provides for adjusters to allow higher than expected external assistance to be spent (with a cap) and shortfall of external assistance to be financed domestically (with a cap).

14. Any financing excess up to US$60 million will be spent on expenditure priorities defined in the PRSP. The floor on the stock of net foreign assets of the BRB will be adjusted upward, and the ceilings on the net domestic assets of the BRB and on net domestic financing to the government will be adjusted downward to accommodate 100 percent of any financing excess above US$60 million.

15. The floor on the stock of net foreign assets of the BRB will be adjusted downward, and the ceilings on the net domestic assets of the BRB and on net domestic financing to the government will be adjusted upward to accommodate a financing shortfall up to a maximum of US$60 million. External financial assistance will be converted to Burundi francs using the program-specified BIF/US$ exchange rate. The average program exchange rate in 2010 is 1290.

16. External financial assistance (measured in US$) is defined to include the following: (i) nonproject loans and grants to the budget (including payments made through the multi-donor trust fund managed by the World Bank for current debt service to multilaterals); plus (ii) debt relief on current maturities; minus (iii) any cash payments for external arrears clearance operations. Donor disbursements into blocked accounts for the purpose of clearing arrears will not be considered foreign assistance for program monitoring purposes.

B. Provision of Information to IMF Staff

17. To facilitate the monitoring of program implementation, the authorities will prepare and forward to the IMF African Department a monthly progress report on the program, within six weeks of the end of each month, containing

18. The following weekly data:

- foreign exchange auction market (MESD) transactions;
- the balance sheet of the BRB (weekly statement) (BRB Research Department).

19. The following monthly data, with a maximum lag of six weeks:

- a monitoring table (*tableau de bord*) containing the most recent weekly and monthly data on the main financial indicators (REFES);
- a table on foreign exchange cash flow (BRB Foreign Banking Operations Department);
- the monetary survey, including the breakdown of the BRB and of commercial banks (BRB Research Department);
- monthly exchange-rate data (official and parallel markets, end-of-month and monthly average) (BRB Research Department);
- a detailed breakdown of government revenue (Ministry of Finance);
- a detailed breakdown of government expenditure on a commitment basis, including propoor spending (Ministry of Finance);
- a detailed breakdown of the servicing of domestic and external public debt, including amounts due and paid, on interest and principal, as well as the

breakdown by creditor and any accumulation of arrears on domestic or external debt (Ministry of Finance);

- a detailed breakdown of the stock of domestic payment arrears for the current fiscal year (Ministry of Finance);
- the amount of new debts contracted or guaranteed by the government, including detailed information on the terms (such as currency denomination, interest rate, grace period, maturity) (Ministry of Finance);
- actual disbursements of nonproject financial assistance, including new loans and debt relief granted by Burundi's external creditors (Ministry of Finance); and
- an update on the implementation of structural measures planned under the program (REFES).

20. The following quarterly data, with a maximum lag of six weeks:

- progress reports on the BRB's internal reforms, including each unit's action plans for the coming month (Reform Monitoring Committee, BRB).

21. SP/REFES/Ministry of Finance and BRB will also provide the IMF African Department with any information that is deemed necessary to ensure effective monitoring of the program.

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IMF Executive Board Concludes the Article IV Consultation and Completes the Fourth Review Under the ECF Arrangement for the Republic of Burundi

On July [xx], 2010, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation and completed the fourth review with Burundi.[1]

Background

Burundi is emerging from more than a decade of civil conflict. The power-sharing agreement signed in December 2008 by the government and the last rebel group (FNL), paved the way for national elections, which run from May 24 to September 8, 2010. GDP per capita is about US$140, and more than two-thirds of the population lives below the poverty line. Although the country is making some progress toward the Millennium Development Goals (MDGs), it is unlikely that any of the targets will be achieved by 2015.

Economic growth moderated to 3.5 percent in 2009, from 4.5 percent in 2008, mainly because of lower private transfers and foreign direct investment. Because of lower international oil and food prices, headline inflation (end of period) declined from about 26 percent in 2008 to about 4.5 percent in 2009, well within the single-digit level targeted under the program.

Fiscal performance in 2009 was broadly satisfactory. Despite the global financial crisis, total revenue was 0.6 percent of GDP higher than programmed, reflecting improved collections of income and indirect taxes. Total spending was contained below the programmed level, as externally-financed spending was lower than programmed. The wage bill was also kept within the envisaged budgetary envelope. Overall, the fiscal deficit (excluding grants) was

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

lower than programmed. Adjusted for the shortfall in external nonproject financial assistance, domestic financing of the budget was well within the programmed target.

Despite the food and oil shock and the global financial crisis, the external position was supported by HIPC and MDRI relief and the SDR allocation. Notwithstanding the negative impact of the food and oil crisis on the trade balance, the external current account deficit improved in 2008 because of high donor support to mitigate the effects of the shock. In contrast, in 2009 the external current account deficit worsened, even as the terms of trade improved, because of lower donor support. Overall, the balance of payments position was supported by HIPC and MDRI debt relief and the SDR allocation. Gross reserves remained at a comfortable level of 6.5 months of import cover.

Executive Board Assessment

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Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Burundi: Selected Economic and Financial Indicators, 2007–09

	2007	2008	2009
	(Annual percentage change)		
Real Economy			
Real GDP	3.6	4.5	3.5
Consumer prices (period average)	8.3	24.4	10.7
Consumer prices (end of period)	14.7	25.7	4.6
	(Change in percent of beginning of period M2)		
Money and credit			
Net foreign assets	11.5	21.9	-2.9
Domestic credit	6.6	18.8	27.8
Money and quasi money (M2)	10.1	34.2	19.8
	(Percent of GDP)		
General government			
Revenue (excluding grants)	18.6	18.5	18.6
Total expenditure and net lending	38.5	44.1	39.3
Overall balance (commitment basis)			
Excluding grants	-19.8	-25.6	-20.7
Including grants (excl. HIPC)	-3.3	-3.7	-5.2
External sector			
Current account balance (incl. grants)	-15.7	-12.3	-14.5
Gross official reserves			
US$ million	177.3	266.6	323.0
Months of imports	3.8	6.5	6.5

Sources: Burundi authorities and IMF staff estimates and projections.