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Minutes of Executive Board Meeting 10/63-1

10:00 a.m., June 25, 2010

1. Togo - Fourth Review Under the Three-Year Arrangement Under the Extended Credit Facility and Requests for Waivers of Performance Criteria and Augmentation of Access

Documents: EBS/10/117

Staff: Mills, AFR; Dorsey, SPR

Length: 25 minutes

Executive Board Attendance

N. Shinohara, Acting Chair

Executive Directors	**Alternate Executive Directors**
S. Itam (AE)	M. Majoro (AE)
	K. Assimaidou (AF)
	B. Lischinsky (AG), Temporary
	M. Di Maio (AU), Temporary
	O. Demirkol (BE), Temporary
	A. Maciá (BR), Temporary
	Y. Luo (CC)
	L. Jimenez (CE), Temporary
	P. McGoldrick (CO), Temporary
	A. Ducrocq (FF)
	S. Meyer (GR), Temporary
	N. Choudhary (IN), Temporary
	J. Cardoso (IT), Temporary
	M. Makino (JA), Temporary
	S. Maherzi (MD), Temporary
	W. Abdelati (MI), Temporary
	D. Lezhava (NE), Temporary
	B. Ólafsson (NO), Temporary
	Y. Ustyugova (RU), Temporary
	S. Alnefaee (SA), Temporary
	P. Phan (ST), Temporary
	S. Antic (SZ), Temporary
	L. Hull (UA), Temporary
	R. Ward (UK), Temporary

L. Hubloue, Acting Secretary
F. Gimbel, Assistant

Also Present
African Department: M. Atingi Ego, A. David, M. Kabedi-Mbuyi, C. Mills, R. Nord, L. Ocampos Balansa, A. Sayeh. Legal Department: C. Ogada, N. Rendak. Secretary's Department: H. Malothra, M. Yslas. Strategy, Policy, and Review Department: T. Dorsey, C. Gicquel. Senior Advisors to Executive Directors: S. Bah (AF), R. N'Sonde (AF), B. Saidy (AE), M. Sidi Bouna (AF). Advisors to Executive Directors: H. Do (ST), L. Lephoto (AE), T. Nguema-Affane (AF), A. Terracol (FF).

1. TOGO—FOURTH REVIEW UNDER THE THREE-YEAR ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY AND REQUESTS FOR WAIVERS OF PERFORMANCE CRITERIA AND AUGMENTATION OF ACCESS

The staff representative from the African Department (Mr. Mills) submitted the following statement:

> This statement provides information that has become available since the staff report was issued to the Executive Board on June 11, 2010. The new information does not alter the thrust of the staff appraisal.
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> The promissory notes that triggered the nonobservance of the external debt performance criterion have been canceled (paragraph 6 of the staff report and paragraph 14 of the Letter of Intent). The restitution of the promissory notes was part of the authorities' agreement with the supplier to cancel the contract, which also included some costs.
>
> The authorities raised the prices for petroleum products by 15–22 percent on June 19, 2010. They also publicly explained their intention to strengthen the pass-through of international prices with a smoothing mechanism, as envisioned under the program (paragraph 13 of the staff report and paragraph 33 of the Letter of Intent). A technical assistance mission from FAD conducted discussions on the petroleum product pricing mechanism on June 13–24, 2010.
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> Some steps in the restructuring of the financial sector are taking longer than expected in the original timetable, including updating the legal framework for privatization and issuing a pre-qualification notice (paragraph 14 of the staff report and paragraphs 17 and 31 of the Letter of Intent). While it remains feasible to issue the final call for bids by the end of September (as envisioned in the structural benchmark), expeditious action by the authorities will be necessary to maintain the original timetable.

Mr. Rutayisire and Mr. Assimaidou submitted the following statement:

> We would like to express our Togolese authorities' appreciation of the continued engagement of Fund staff with Togo and their quality policy advice, notably through the current ECF-supported program. We also thank the Executive Board and Management for maintaining a constructive dialogue with our authorities throughout the recent years of a challenging domestic and external environment. Our authorities share the thrust of the staff report.

Following the food and fuel price shocks in 2007-08 and the adverse impact of flood in 2008 which destroyed critical road and bridge infrastructure, the economy of Togo has been hit by the effect of the global economic recession in 2009, notably through decreased exports and remittances and lower-than-expected FDI. This has prevented growth from reaching its estimated potential, government revenues from reaching target, and thus leading to missing two performance criteria for end-December 2009 (fiscal balance and domestic financing). Weak administrative capacities contributed to the contracting of a loan that does not meet the concessionality requirement. Upon realizing this deficiency, our authorities have taken a corrective action after consulting with Fund staff. Moreover, the external financing needs identified earlier in the program still remain.

Despite the challenging circumstances facing the country, our authorities have broadly met the program objectives under the current review. All other performance criteria have been observed and all structural reforms through 2009 have been implemented while the ambitious structural benchmarks at end-March 2010, including the implementation of the domestic arrears clearance strategy, have been effectively satisfied.

Our Togolese authorities remain strongly committed to a rigorous implementation of the program. They also continue to see the HIPC completion point—toward which they continue to make progress—as a central milestone in their strategy to ensure stronger and sustainable growth and reduce poverty. Based on their good policy and reform implementation, despite difficult circumstances, and the corrective actions they have taken to remedy the missed criteria, our authorities request the completion of the Fourth Review under the ECF arrangement and waivers for the nonobservance of performance criteria. Furthermore, they have endeavored to close part of the financing gap through external budget support and the Food Facility instrument of the EU. Nevertheless, a residual financing gap remains, for which our authorities are requesting an augmentation of access under the ECF amounting to SDR 11 million and equivalent to 15 percent of quota.

Continued Track Record of Policy and Reform Implementation

Since the last review under the current ECF arrangement, our authorities have pursued countercyclical macroeconomic policies—notably on the fiscal front—to mitigate the effects of the global recession, while maintaining the program objectives.

In this context, fiscal policy continues to strengthen notwithstanding difficult conditions. Although revenues at end 2009 fell short due to the economic slowdown and lower-than-expected exceptional nontax revenues, our authorities had to preserve planned expenditures and faced unexpected personnel costs related to the health and education sectors, and security for the March 2010 presidential elections. This led to exceeding the target for the domestic primary fiscal deficit by 0.2 percent of GDP and, combined with more successful-than-envisaged efforts in clearing domestic arrears vis-à-vis the private sector, contributed to exceeding the net domestic financing ceiling. Our authorities believe that the ongoing implementation of the domestic arrears clearance strategy will help rekindle private sector activity. They also continue to meet the PC regarding the non-accumulation of external arrears.

Concerning external borrowing, there has been a contracting of external credit early this year aimed at modernizing the TV broadcasting system, which did not meet the concessionality requirement under the program owing to insufficient capacities on the part of the authorities. After consultation with Fund staff, the authorities have since taken a forceful corrective action by cancelling the promissory notes by mutual agreement with the external supplier. Having also cancelled the related project, they are now seeking collaboration from development partners to implement a more suitable rehabilitation and extension project consistent with the country's debt sustainability.

The implementation of structural reforms has continued satisfactorily, with all structural benchmarks and performance criteria through 2009 having been observed. These include the reduction in tax and customs exemptions and strengthening of tax and customs controls; the operationalization of new Treasury structures based on WAEMU directives; the restructuring/recapitalization of a bank, BTCI; the launching of a process to identify strategic investors for state-owned banks; and the preparation of a development strategy for the phosphates sector based on the results of the strategic audit. The latter measure was observed with delay due to the initial delay in the completion of the audit (insufficient number of firms responding to the initial tender) as noted during the second review under the program last year.

Policies for the Remainder of 2010 and for 2011

In pursuing efforts to boost the economy, our Togolese authorities remain determined to enhance fiscal governance; maintain macroeconomic stability and program objectives; pursue prudent debt management through external financing based on grants and highly concessional loans; and advance structural reforms in key growth-oriented sectors, notably banks, cotton, phosphates and telecommunications. They understand the importance of revitalizing these sectors, both for fiscal sustainability and growth purposes.

Fiscal Policy and Debt Management

In the difficult economic environment still dominated by the effects of the global crisis, fiscal policy will continue to be geared towards supporting economic activity notably through higher investment and poverty reducing expenditure, building on improvements in the execution of public investment and priorities defined in the country's PRSP. Motivated by the continuing impact of the global crisis on Togo's exports and remittances, this policy stance will require the mobilization of adequate financial resources. In this vein, our authorities hope that they can count on additional financial assistance from development partners. On their part, the authorities have revised upward their domestic revenue objectives, based on additional efforts in tax collection and increased effectiveness in nontax revenue mobilization. All these efforts will be supported by continuing public financial management reforms, notably in the implementation of the mechanism for managing cash flows and monitoring budget execution and the completion of the financial and organizational audit of Caisse de Retraite du Togo (Togo's retirement fund).

Over the medium term, the fiscal policy stance will be guided by a tighter target of domestic primary balance which will involve a gradual adjustment starting in 2011.

Our authorities remain committed to strengthening debt management through improved public finances, reliance on concessional external financing, the pursuit of securities and bonds issue program, and improvement in debt management capacity with Fund assistance. At the same time, they intend to continue settling the outstanding domestic arrears balance.

Financial Sector Reform

Our Togolese authorities remain committed to restructuring and privatizing the four state-owned banks, with the aim of restoring confidence and vivacity in the sector while at the same time improving debt dynamics with debt repayment using privatization revenues. To this end, they plan to publish a call for bids by September 2010. In the meantime, they will maintain, in collaboration with the regional banking commission, a close oversight of the banks' management throughout the restructuring process. The government will also set up a mechanism for managing and collecting the NPLs of state-owned banks by end-December 2010.

Other Structural Reforms

Reforms of state-owned enterprises will also be pursued as scheduled, with a view to restoring their financial health and promote production and productivity gains. In the phosphates sector, the strategy will proceed in accordance with the strategic audit. In the electricity sector, the government is adopting a cost-recovery approach and a price adjustment mechanism. In the telecommunications sector, the authorities intend to strengthen the regulatory framework with the assistance of partners, following regional directives, with the view to ensure competition and economic efficiency. They also aim at developing a medium-term strategy to increase the sector's contribution to growth. Regarding the Port Autonome de Lomé, the authorities seek to take advantage of its regional position to promote it as a trade hub by creating a one-stop window for foreign trade to facilitate all administrative procedures for exports and imports at one location.

Regarding the petroleum sector, the Togolese government has undertaken a restructuring of the domestic pricing mechanism, with the view to limiting fiscal risks by institutionalizing automatic adjustments of petroleum product prices. In this vein, an FAD mission is currently visiting Lomé to provide advice and technical assistance. Already, the authorities have increased domestic petroleum prices in recent days.

Poverty Reduction Strategy and HIPC Process

As our authorities have emphasized, Togo is determined to fulfill all the conditions for meeting the HIPC completion point triggers as early as end-2010. The process of preparing the full PRSP in a large participatory setting involving all segments of society, including the government, the civil society, the business community, development partners and the National Assembly, was completed a year ago and implementation is proceeding.

Other requirements for the HIPC completion point are also advancing well. Among the completion point triggers, the decree on the Procurement Regulatory Agency was adopted in November 2009 and the amounts of approved contracts are being published; the Cour des Comptes has been made operational with regular Treasury Balances and the Loi de Règlement for 2007 and 2008 prepared and transmitted; and an annual report on the revenues from, and payments to, the phosphate company, in line with the EITI criteria, will be published.

Our Togolese authorities fully understand that the attainment of greater growth rates in the medium run is predicated on reaching the completion point to make Togo's debt outlook sustainable and their capacity to close the country's infrastructure gaps, boost productivity by taking advantage of moderate wages and a competitive, well-educated labor force, and create a business-friendly environment. They acknowledge the weaknesses in these areas, and agree with the recommendations of Fund staff. In fact, their approach, embodied in the PRS, focuses on three pillars: (i) rehabilitating infrastructure; (ii) improving the quality of education and making it more accessible; and (iii) addressing the factors that impede a good business environment, notably the investment code, the corporate tax system, business registration, property rights, and the judicial system.

Conclusion

Togo continues to face capacity and infrastructural challenges. Nevertheless, our Togolese authorities are determined to do their utmost to meet the HIPC completion point requirements. These include maintaining a good implementation of the ECF-supported program, putting in place the full poverty reduction strategy and meeting the trigger points under the enhanced HIPC Initiative. They will do so while promoting a climate of political and social stability, and peace. All the economic efforts made and committed by the authorities, especially in the context of an unfavorable environment, will require the continued support of the international community. Fresh resources to finance investments and reforms are critically needed to achieve the objectives laid out in the ECF-supported program and the country's PRSP.

Based on our authorities' continued good track record and their renewed determination to pursue sound policies and reforms going forward, we call on the Executive Board to support the proposed decisions.

Mr. Prader and Mr. Demirkol submitted the following statement:

We thank staff for the paper and Messrs. Rutayisire and Assimaidou for their helpful buff statement. We agree that the program remains broadly on track despite the slippages on the fiscal balance and domestic financing performance criteria. We also agree with staff that the program generally continues to meet its goals. It is noteworthy that public investment reached an all time high, the clearing of domestic arrears has started and structural reforms gained momentum. However, from a broader perspective, growth still remains relatively weak and the pace of recovery has been dismal despite the countercyclical fiscal policy. The success of the program hinges upon producing higher growth rates than those achieved so far. Having said that, we support the authorities' requests for waivers in light of the corrective actions taken, the completion of the fourth review under the Extended Credit Facility and augmentation of access for an amount equivalent to SDR 11 million (15 percent of quota).

We concur with staff that a relaxed fiscal policy stance should be pursued in 2010. Fiscal policy should continue to support economic activity and post crisis needs. We welcome that the net impact of the fiscal stance on debt levels will be muted because of external grants and clearance of arrears. Furthermore, we note that higher revenues are directed to close the financing gap and that lower priority spending was cut. Fiscal structural reforms including the action plan to improve public financial management, and an improved budget execution should help the authorities to deliver on the program commitments. The authorities deserve the international community's assistance to fill in the remaining financing gap given their commitment and proposed measures. It is particularly heartening that the authorities had secured financing with good terms from the World Bank and the European Union for the rest of 2010.

We welcome Togo's progress in clearing their domestic payment arrears. Even though the authorities did not meet the end-March structural benchmark of completion of the process, we note from Box 2 that substantial progress was achieved. We look forward to the completion of the clearance operation by June. Could staff elaborate more on the exceptional financing from the BCEAO and the role of the SDR allocation in facilitating the arrears clearance operation and if there are other examples as such in the region?

The restructuring of the financial sector and reforms of the state owned enterprises are crucial for the success of the program. The authorities should give careful consideration to the staff's advice given the ambitious reform agenda. We are concerned that the capacity constraints could inhibit the progress in these important reform areas.

We encourage the authorities to take the necessary measures to fulfill the conditions for the HIPC completion point triggers. The staff suggests that the authorities could qualify for the HPIC completion point as early as late 2010. The debt relief will help with the debt sustainability issues and enhance the authorities' policy implementation. The completion point could be a pivotal date for unlocking Togo's growth potential if supported by the structural reforms and right macroeconomic policy mix.

With these remarks, we wish the authorities the best in their challenging endeavors.

Mr. Itam submitted the following statement:

The Togolese authorities' satisfactory implementation of the program, despite the difficult economic circumstances, is commendable. We note the persistent adverse effect of the global recession on economic growth and the intensification of balance of payments pressures as a result of reduced exports, remittances and FDI. The recent slippages in program implementation are regrettable. However, given the corrective actions taken by the authorities, we support the requested waivers and completion of the fourth ECF review. We also support the augmentation of access under the ECF. We are in broad agreement with the thrust of the staff report and we have benefited from the informative buff statement by Messrs Rutayisire and Assimaidou.

Given the current economic conditions, the authorities' relaxed fiscal stance, which aims at supporting economic growth through increased public investment, safeguarding critical social spending, and clearing domestic arrears, is appropriate. We welcome the support of development partners in securing adequate financing for the current fiscal year. We also welcome the authorities' plans to improve revenue performance through the implementation of measures to widen the tax base and enhance non-tax revenue collections.

Furthermore, we agree with the measures being implemented to improve fiscal governance, strengthen public financial management and enhance the efficiency of budget execution. We welcome the progress made in this regard and encourage the authorities to fast track these reforms in order to realize results in a timely manner. Improving debt management capacity is also crucial and, in this regard, we urge the Fund and the World Bank to provide the assistance requested by the authorities.

On the structural front, we feel that the authorities' recognition of the role of the financial sector in facilitating growth is well placed. In this regard, we welcome their intention to restructure and strengthen the sector through privatization of state owned banks. We support the use of privatization proceeds to improve the debt position of the country. We also encourage the authorities to implement measures to strengthen the legal and regulatory frameworks for supervision of the banks as well as the non-bank financial institutions.

We wish the authorities success in their future endeavors.

Mr. Mojarrad and Mr. Maherzi submitted the following statement:

We thank the staff for a well-focused report and Messrs. Rutayisire and Assimaidou for their informative statement. Despite the difficult circumstances of the past years, including the food and fuel price shocks in 2007-08, the 2008 flood, and the impact of the global crisis, Togo continued to perform well under the Fund-supported program, although growth in 2009 and 2010 is estimated to remain below potential. Reflecting strong program ownership, commendable progress has been achieved in implementing structural reforms, as highlighted by Messrs. Rutayisire and Assimaidou, and prompt actions have been taken to correct the recent slippages which were driven by unexpected circumstances and weak administrative capacity. We are encouraged by the progress made in meeting the completion point triggers under the HIPC initiative and look forward to successful fulfillment of all remaining conditions by the end of this year as expected.

Notwithstanding these achievements, considerable challenges remain ahead, including anchoring sustained high and broad-based growth and substantially progressing toward achieving the MDGs, in line with the PRS objectives. The authorities' track record and renewed commitment to sound policies and implementation of the remaining ambitious reform agenda bode well for improved prospects. Continued assistance from the international community, including from the Fund, remains crucial. We support the proposed decisions.

While fiscal policy in 2010 remains appropriately supportive of economic activity, the intended return to a gradual tightening starting in 2011 while preserving pro-poor and pro-growth spending, as indicated in the authorities' Letter of Intent, should serve fiscal and debt sustainability objectives well. Ongoing efforts to strengthen revenue, including by improving tax and non-tax collection, are noteworthy as are plans to introduce an automatic price adjustment mechanism for domestic petroleum products and progress in implementing the domestic arrears clearance strategy. The authorities' determination to follow through on their action plan to enhance public financial management and further improve debt management, as indicated by Messrs. Rutayisire and Assimaidou, is encouraging.

Building on recent progress on the structural front, maintaining the reform momentum, including in the financial and public enterprises sectors, is key to support growth and poverty reduction objectives. We are encouraged by the authorities' resolve in this regard and wish them success in their endeavors.

Mr. Luo and Mr. Yung submitted the following statement:

We thank staff for the well-presented report and Messrs. Rutayisire and Assimaidou for a helpful buff statement.

We support the completion of the fourth review under the ECF arrangement, the request for waivers of performance criteria, and the augmentation of access for Togo. We concur that the program implementation has been generally satisfactory, even if the PCs for fiscal balance and domestic finance for end-December and continuous PC for nonconcessional external borrowing were not observed. We consider that prompt and reasonable remedial actions were taken to justify the request for waivers of the above PCs. With regard to the proposed augmentation of access, we agree that Togo's exceptional financing needs are genuine and deserve concrete support from the Fund as well as the international community. Going forward, we encourage the authorities to keep up the momentum in structural reforms, paving the way for reaching the HIPC completion point in the near future.

We are convinced that there is a need for Togo to keep a relaxed and countercyclical fiscal stance in 2010. As the lingering global recession is expected to continue to put pressure on the country's growth, an accommodative fiscal policy could be effective in supporting domestic economic activities and addressing post-crisis needs. Meanwhile, we are aware that the authorities have revised upward their domestic revenue objectives, with additional efforts in tax collection and enhanced effectiveness in nontax revenue mobilization, supported by continuing public financial management reforms. Furthermore, the authorities have identified savings in lower priority spending and a plan in raising financing in the regional market. We consider it meaningful for the Fund to complement these efforts.

We welcome the reassurance by Messrs. Rutayisire and Assimaidou that the authorities remain committed to strengthening debt management through improved public finances, reliance on concessional external financing, the pursuit of a securities and bonds issuance program, and improvement in debt management capacity with Fund assistance. We are also encouraged to note the progress in settling the outstanding domestic arrears balance.

We welcome that the restructuring of the financial sector is advancing on schedule. Notably, the authorities are committed in vitalizing the sector by privatizing the state-owned banks. Meanwhile, reforms are also under way in selected sectors like electricity, telecommunications, and agriculture to enhance Togo's growth potential.

We are heartened by the authorities' determination to achieve the HIPC completion point. It is encouraging to note from staff that Togo remains on track to qualify for the HIPC completion point as early as the end of 2010. We look forward to updates on the achievements soon.

With these remarks, we wish the authorities success in their reform efforts.

Mr. Hockin and Mr. McGoldrick submitted the following statement:

We thank staff for their report and Messrs. Rutayisire and Assimaidou for their buff. We support the fourth review and accept the waivers and request for augmentation. Togo looks set to meet the conditions triggering HIPC completion and we encourage the authorities to follow through on their significant achievements; a good performance under the program will prove helpful in this regard. Continued support from the international community is welcome, especially the support of the World Bank and the EU in filling the looming financing gap. While we broadly agree with staff's analysis, we would nonetheless like to comment on the deviations from the program.

In spite of better than expected growth, Togo has breached the performance criterion with respect to the fiscal balance. The staff assures us that sufficient corrective action has been taken and we accept this, but seek some further clarification. We understand that expenditure was higher than expected, partly due to clearance of arrears and partly due to unexpected expenditure on health and education. Could staff be more precise with regard to the nature of these expenditures and why these came as a surprise? In general, we would not like to see renewed slippage in this area and urge the authorities to remain conservative regarding the wage bill.

We note the delay in clearing of arrears but progress seems encouraging—we agree with staff that this issue must be dealt with completely and swiftly and we look forward to an update from staff on this.

The performance criterion specifying that non-concessional borrowing is to be avoided under the program was—unintentionally—breached; we understand the loan has since been cancelled. This begs two questions. First, is there room for technical assistance to help prevent such error in the future? Related to this, we support the authorities' request for an assessment of public debt management by the World Bank. Second, what costs were incurred with respect to the cancellation of this loan?

Finally, staff notes that the restructuring of the financial sector is showing signs of falling behind schedule. We urge the authorities to renew their efforts in this respect.

Mr. von Stenglin and Ms. Meyer submitted the following statement:

We thank the staff for their report and Mr. Rutayisire and Mr. Assimaidou for their buff statement. We commend the authorities for the progress made under the program and agree with the staff that strengthening public finances and completing structural reforms is of the utmost importance for sustained economic growth.

We support to the conclusion of the fourth review under the ECF. Acknowledging the corrective measures taken by the authorities to undo the contracting of external debt on non-concessional debt, we support the relevant waiver. However, not least with a view to the HIPC completion point, the weak capacities with regard to debt management and the prioritizing of investment projects are a cause of concern. Regarding the non-respect of the PCs on the fiscal balance and domestic financing, we regret that the authorities did not live up to their announcement in the context of the 3rd ECF review to cut spending plans should a revenue shortfall arise, but take into account the fact that the authorities identified savings in lower priority spending to offset fully the larger wage bill.

We consent to the proposed augmentation of the level of access under the program. However, we would have welcomed if the staff, in its assessment, had put more emphasis on the need for fiscal consolidation in an improving economic environment, as was done under the last review. Looking forward, we would caution against a continued recourse to the impact of the global financial crisis—which was moderate with regard to remittances and exports and somewhat more pronounced with regard to FDI—as an argument for using PRGT resources, when the challenges for a country's economy, including potential growth, largely stem from long-standing structural problems.

Mr. Guzmán and Mr. Jiménez submitted the following statement:

We thank staff for a concise yet informative report and Mr. Rutayisire for his insightful buff statement. We concur with the view that the ECF program objectives have been broadly met. This in itself is commendable in view of the challenges that the Togolese authorities faced last year. We can support the authorities' request for waivers (the first requested under the program) in view of the remedial actions that were discussed with staff. We can also support the augmentation of the program to help fill a residual financing gap of 1 percent of GDP for 2010, on account of the satisfactory performance so far.

Having said that, we are concerned by the country's aforementioned financing needs and debt distress, as well as by the heightened balance of payments pressures. The current account deficit reached 7 percent of GDP in 2009 and is expected to reach 7.6 percent in 2010, with import demand supported largely by fiscal policy. In this context, while the continuation of a relaxed fiscal stance may be granted for the current fiscal year, we wonder whether the authorities should consider a more cautious stance. An earlier tightening (instead of allowing for an increased overall deficit) should, however, not affect the necessary social spending, nor should it hurt the response to post-crisis needs. It should also be made compatible with the advancement of structural reforms to promote growth. We learn that gradual consolidation is not expected to start until 2011.

Apart from that, in 2010 it would be essential to avoid missing the fiscal balance objective for a second consecutive year. We agree that the slippages observed in 2009 were modest and that curtailment of expenditures was not possible, as revenue shortfalls were observed late in the year. Be it as it may, stricter supervision of budget execution will be essential for the current period. We praise authorities for their commitment to address these issues, and also for the cancellation of debt that triggered the nonobservance of the external debt PC.

We also praise authorities for the advancement of measures to restore sound public finances and enhance fiscal governance, as well as for the structural reforms in the financial sector and state-owned enterprises. They will greatly contribute to promote growth in the future. We would appreciate it if staff could provide more detail on structural components of the program, including petroleum product pricing and the required technical assistance.

Finally, we agree with the staff view on the need for enhanced monitoring of the program in view of recent slippages and challenges ahead.

Mr. Rediker and Ms. Hull submitted the following statement:

The staff report highlights the negative impact of the global economic crisis in Togo, with growth in 2009 falling short of the 4.0 percent of GDP projected at the time of the program request. However, we note and are pleased that growth has performed better than projected in the last review, and that 2010 growth has been revised upward. After strong performance in the three previous Extended Credit Facility (ECF) reviews, Togo's performance this review period was noticeably weaker. Given Togo's delicate economic situation, we urge the authorities to re-double their efforts to meet their commitments under the ECF program.

Fiscal Policy

Slippages in budget execution resulted in the failure to meet the end-December fiscal balance and domestic financing PCs. The authorities explain in paragraph 12 of the Letter of Intent that a significantly larger-than-expected wage bill is the main reason for the overrun of expenditures and attribute it to election-related security, and to health and education spending. We invite the staff to elaborate on the relative contribution of each of these factors, whether increased spending on election related security is fully reversed now that the elections are over, and why the increased spending on health and education was unforeseen. Public sector wages are projected to increase significantly as a share of GDP between 2008 and 2011, and we are concerned that the trend is unsustainable.

For 2010, we note that social spending will rise, and we understand from the staff that within this category of spending, health and education expenditure specifically will increase both nominally and as a share of GDP. On structural fiscal issues, we appreciate the addition of a structural benchmark that will institutionalize an automatic price adjustment mechanism for petroleum products.

We regret the contraction of nonconcessional debt for upgrading the television broadcasting system that resulted in a fiscal cost for cancelling the contracts. We urge the authorities to engage closely with the Fund staff in the future when considering externally financed projects and to put in place a process to systematically review external financing requests. We appreciate the measures taken to unwind the deal, which we understand have now been fully implemented, as well as the other corrective actions currently underway.

Financial Sector

We are concerned by delays in restructuring and privatizing the four state-owned banks as outlined in the staff statement. We are reassured by the authorities' ongoing commitment to this process and plans for 2010 as discussed in Messrs. Rutayisire and Assimaidou's statement. We urge the authorities to make every effort to stay on schedule with their plans.

Program Issues

We are not convinced that the persistent effects of the global recession have heightened balance of payments pressures. Relative to the third review, the projection for the 2010 overall balance of payments position has improved with a higher current account deficit offset by higher capital inflows. We also note that the balance of payments projections include an accumulation of central bank net foreign assets of CFA 21.6 billion that was not envisaged at the time of the last review. A change in format of the presentation of the balance of payments table (Table 2) prevents the comparison of indicators of reserve coverage relative to the third review, but we understand from the staff that reserves in 2010 would be 3.9 months of imports, taking into account the increase in central bank net foreign assets. This is lower than projected at the time of the last review, but higher than envisaged for 2010 at the time of the program request. Rather than smoothing adjustment to an external shock, IMF credit would appear to be effectively accommodating the endogenous fiscal slippages mentioned above. We invite the staff to comment.

The final test date for this arrangement is at the end of this year, and the staff report projects an external financing gap for 2011 that is larger than 2010. We invite the staff to comment on how it sees Togo moving toward a credible exit from Fund assistance.

In the absence of a functioning military audit system in Togo, under U.S. law we cannot support the request for completion of the fourth review under the Extended Credit Facility and ask to be recorded as abstaining on the proposed decisions.

Mr. Ducrocq and Mr. Talbot submitted the following joint statement:

We thank staff for their report and Messrs. Rutayisire and Assimaidou for their convincing buff statement.

At the outset, we would like to commend the authorities for the considerable progress made since the beginning of the ECF program and the re-engagement of the international financial community in Togo after a long domestic crisis. This progress has been broadly maintained, despite the challenges created by the need to deal with a succession of adverse shocks.

On the fiscal side, we agree with staff that the program has broadly continued to meet its goal, despite slippages in 2009 leading to two missed performance criteria. We can go along with the requested waivers, in light of the corrective measures underway and considering that the missed performance criterion on domestic financing is essentially due to larger domestic arrears clearance—something that we would see as a positive step. Looking ahead, we share staff's appraisal on the need to maintain a countercyclical policy stance in 2010 in order to underpin a recovery which remains sluggish so far.

On the structural side, we are pleased to see the significant progress made to date in numerous areas (public financial management, banking sector, SOEs) and welcome the strengthened commitment by the authorities. We consider structural reforms as crucial in Togo to boost growth to its potential level and reduce poverty. In this regard, we would like to underline the following:

Strengthening public financial management (PFM) is a cornerstone of the program. As shown in Box 1, expenditure execution for public investment has improved and the ongoing efforts to further reinforce the expenditure chain are welcome. We particularly welcome the ambitious Togolese action plan to enhance PFM and to move towards a single Treasury account. We also encourage the authorities to pursue close dialogue with the IMF and the donors in order to achieve these objectives.

In our view, the completion of the ongoing process for clearing domestic arrears is crucial and we commend the authorities for their strong commitment to settle this long-standing issue despite its complexity. This can also help to bolster private-sector activity, as part of a broader countercyclical policy effort.

The adoption of a strategy for the phosphate sector is a major step. The priority now should be to build on this to revive sector dynamics. We welcome the new structural benchmark linked to the design of a roadmap for the creation of a one-stop window at the Port Autonome de Lomé, with the assistance of the World Bank. It could be a key step towards enhancing Togolese competitiveness, regional integration and revenue mobilization.

Turning now to the debt issue, we regret the nonobservance of the criterion regarding non-concessional external borrowing, but we agree with the requested waiver in light of the corrective measures taken by the authorities. Above all, this slippage underlines the need to further strengthen the debt management capacity, which is central to facilitate debt relief. In this regard, we are pleased to see that the country remains on track to qualify for the HIPC completion point by year-end, which will require strong implementation of the program.

In sum, we support the completion of the fourth review under the Extended Credit Facility. Moreover, given the difficult macroeconomic context, the commitment of the authorities to reduce the financing gap as well as the clear catalytic effect of Fund financing, we support the proposed augmentation of access.

The staff representative from the African Department (Mr. Mills), in response to comments and questions from Executive Directors, made the following statement:

Let me first address fiscal-related questions. There was a question on the exceptional financing from the BCEAO, the regional central bank, for the domestic arrears clearance process. This was part of a WAEMU-wide initiative started in July 2009 that was linked to the SDR allocation. All member states received a line of credit in local currency from the central bank which was dedicated to clear arrears and thereby support economic activity. The amount of the credit line was the local currency equivalent of the general allocation of SDRs.

All countries in the sub-region are participating in this initiative and have begun drawing on these lines of credit. In Togo’s case, the line of credit amounts to 2.5 percent of GDP, and we expect it to roughly cover the cost of clearing the validated arrears to private sector suppliers.

Concerning an update on the domestic arrears clearance process, we propose to offer one to Board members once we have received data from the authorities on the status of the process as of the end of this month.

On expenditures, there were questions on the unforeseen increase in the wage bill in 2009. First, let me explain that overall spending last year remained within the program's envelope. The deviation from the PC for the fiscal balance was 0.2 percent of GDP and was equal to the shortfall in total revenue, which materialized in December.

The point about the unexpected increase in the wage bill was that it made it difficult for the authorities to curtail spending to offset the revenue shortfall, as they had initially intended under the program. This increase in the wage bill is mainly attributable to two factors. First, a number of education and health workers who were contractual or auxiliary workers were incorporated last year into the payroll of the civil service after having completed the probationary period. Unfortunately, the wage bill projections had not anticipated this change.

The second main factor is that a new security force was recruited and trained to police the presidential elections. This initiative came about after discussions with international partners that concluded after the budget was finalized. According to observers, this initiative was effective in helping to ensure relatively peaceful presidential elections. These security personnel continue to be employed, including for managing any civil disturbances and the upcoming local elections expected at the end of this year, or the beginning of next year.

The authorities are acting to mitigate the impact of this increase in the wage bill on the 2010 fiscal framework. Although the updated wage bill projection is higher than the budget, the authorities have identified savings and other current spending items to fully offset the increase. I would also note that the revised wage bill projection for 2010 is lower than the 2009 outturn, reflecting some further savings there.

Moving on to the issue of the nonconcessional borrowing, there was a question on debt management capacity and technical assistance. The authorities are undertaking a strengthening of their debt management capacity, including naming a new Director and recruiting new staff to the department responsible.

Togo currently benefits from targeted ongoing technical assistance from AFRITAC-West, and the authorities have also requested an update of their Debt Management Performance Assessment that was conducted by the World Bank in mid-2008. Finally, the authorities have arranged for the IMF country team to provide advice on any external financing plans this year, and this intention is reflected in their Letter of Intent. The staff expects that these measures will greatly reduce the risk of the authorities inadvertently contracting non-concessional financing again.

As noted in the staff report, the authorities decided to cancel the non-concessional borrowing as a corrective measure, as well as the related project. The cost of this cancellation amounted to 0.2 percent of GDP, or $5.7 million. While this cost is not insubstantial, the staff considers that the authorities' decision was reasonable under the circumstances. The authorities hope to recoup some or all of these costs by meeting the objectives of the project at a lower cost with technical input from development partners.

Concerning the program's structural measures, I would highlight the twin objectives of strengthening fiscal governance and enhancing growth potential. Public financial management reforms and the audit of the Civil Service Pension Fund clearly target the first objective. Financial sector restructuring aims to revive financial intermediation to support growth while limiting fiscal risks.

The two new structural measures likewise contribute to both objectives. Reforms at the Port of Lomé will boost its competitiveness as a trade hub, while helping mobilize additional customs revenue.

Concerning the petroleum product pricing mechanism, which was mentioned in the question, the move toward a more automatic pass-through of world prices is intended to maintain incentives for distributors, improve the efficiency of this sector, and limit fiscal risks.

A smoothing formula in the mechanism is intended to protect the population from excessive volatility, without jeopardizing fiscal prudence. A technical mission from FAD is currently in Togo, wrapping up yesterday in fact, and we would be happy to discuss this issue further bilaterally once we have the results of their mission.

There was also a question on assessing Togo's balance of payments needs. Given that Togo is a member of the WAEMU monetary union, the staff believes that the current account deficit is the best gauge of protracted BOP needs. We note that the latest projection for the current account deficit in 2010, at 7.6 percent of GDP, is 0.4 percentage points higher than the projection from the last review and 1.2 percentage points higher than the projection from the original request in 2008.

> I would also note that exports fell last year both in nominal terms and as a percentage of GDP, and we expect them to fall again this year as a proportion of GDP. This outcome contrasts with what one would normally expect for a country like Togo that is emerging from a prolonged domestic crisis. I propose that my colleague address the question on the exit strategy.

The staff representative from the Strategy, Policy, and Review Department (Mr. Dorsey), in response to comments and questions from Executive Directors, made the following statement:

> On the strategy for exit from the use of Fund resources, there are a couple of policy considerations. First, Togo is an interim HIPC. While it is expected that it will get to the completion point before the end of this arrangement, if for some reason this does not happen, then a successor arrangement in the form of an ECF or an SCF would become a requirement, in order to get to the completion point.
>
> Second, Togo is some ways from qualifying as a prolonged user of Fund resources and triggering the requirement for an EPA that would explicitly consider a possible exit strategy. The most recent arrangement prior to the current one was an ESAF arrangement approved in 1994 that had been fully paid back before the current arrangement began. Given this, Togo would only fall under the policies on members with longer-term program engagement if it had an additional four years of Fund arrangements in the seven years following the conclusion of this arrangement.

Mr. McGoldrick, pointing to the breach of the performance criterion on external debt, sought the staff's view on possible improvements in the ECF framework. He noted the authorities' intention to consult the staff prior to any further contracting of external borrowing, and wondered whether this should be an ex-ante condition when allocating a program.

The staff representative from the Strategy, Policy, and Review Department (Mr. Dorsey) noted that this problem should not have occurred, given the zero-limit on non-concessional debt under the program. An alternative program design would not have directly addressed the main factor behind the breach, namely capacity limitations. However, the provision of technical assistance could have been helpful.

Mr. McGoldrick, seeking to clarify his previous statement, repeated his question to the staff—whether prior consultations on debt contracting could be outlined ex ante.

The staff representative from the African Department (Mr. Mills) considered that ex-ante consultations would only be appropriate in cases involving severe capacity constraints, which may have been the case in Togo.

Mr. Itam, seeking further clarification from the staff, wondered whether this ex-ante consultation would also apply to countries without Fund programs.

The staff representative from the Strategy, Policy, and Review Department (Mr. Dorsey) informed the Board that this prior consultation was not part of the Fund's standard practice under program or non-program circumstances. He explained that such a move might be warranted in a case like Togo, given the country's track record in contracting external debt. He noted that such prior consultation would lead to an increase in bureaucratic burden on the authorities and the staff.

Mr. Assimaidou made the following concluding statement:

> I would like to thank the Executive Board and management for their continued support for my Togolese authorities' efforts under the Fund-supported program. I also would like to express my authorities' appreciation for the dedication and policy advice provided by the Mission Chief, Mr. Mills, and his team. I also thank the staff for the answers to the questions raised by Directors. Directors have made useful comments and recommendations both in their grays and during this discussion, which I will faithfully convey to my Togolese authorities.
>
> Directors have expressed a number of concerns related to investment projects and the financial sector. Regarding investment projects, my authorities have begun to improve the execution of public investment, which was significantly increased in 2009. Public investment as a ratio of GDP has also increased. Nevertheless, my authorities recognize that more needs to be done on this front, in order to achieve their infrastructural objectives.
>
> In this vein, I take good note of Directors' recommendation to further improve administrative capacities and the recommended expeditious action on the part of the authorities to maintain the timetable in the restructuring of the financial sector.
>
> I would like to assure the Board that my authorities are working in the direction of resolving the remaining legal issues regarding the completion of the privatization process. They continue to see the restructuring and privatization of the four state-owned banks as the best way to restore

confidence and viability in this sector, while at the same time improving debt dynamics through debt repayment using privatization revenues.

Moreover, regarding non-concessional borrowing, my authorities have cancelled the loan once they realized the lack of sufficient concessionality. Going forward, they remain committed to contracting external debt on concessional terms, and will consult with the staff beforehand.

Finally, Directors have expressed support for my authorities' intention to meet all requirements for the completion point under the HIPC Initiative by the end of this year. In light of the debt distress facing Togo, my authorities view the completion point as a central milestone to freeing up significant resources, realizing the country's development objectives, and meeting the MDGs. I hope that they can continue to count on the Fund's assistance.

The Acting Chair (Mr. Shinohara) made the following summing up:

Directors commended the Togolese authorities for the satisfactory implementation of economic reforms under the ECF-supported program, although there were modest deviations from program targets for the first time. Togo's economy has been negatively affected by the global crisis, and external conditions are likely to remain challenging. The authorities' countercyclical fiscal policies and progress in implementing structural reforms are supporting a modest pick-up in growth.

Directors endorsed the continuation of a countercyclical fiscal stance for 2010, in particular the increased levels of domestically-financed public investment and domestic arrears clearance in cash. They welcomed the corrective actions for the deviations from program targets, particularly the adjustment of the 2010 fiscal framework and tighter monitoring of budget execution. The authorities' cancellation of the nonconcessional external borrowing and plans to enhance debt management underscore their strengthened commitment in this area.

Directors looked forward to a timely completion of the clearance of domestic arrears. They also encouraged the authorities to sustain their efforts to strengthen public finances by increasing domestic revenue, and to embark on a gradual fiscal consolidation starting 2011. Disciplined growth in current spending, especially the wage bill, will also be critical.

Directors commended the authorities for the progress in implementing the structural reforms. They stressed that completing the reforms underway will be necessary to enhance the growth potential. Directors welcomed the adoption of a new strategy for the phosphate sector, plans to reform petroleum products pricing, and establishment of a “one-stop-window” for trade and customs procedures.

Directors observed that while the restructuring of the financial sector is advancing, some steps are taking longer than expected. They emphasized the need to take expeditious actions to update the legal framework for privatization and encouraged the authorities to remain on schedule with preparations for privatizations of state-owned banks.

Directors noted that a return to the disciplined program implementation seen earlier in the arrangement is important, especially given the difficulty of financing any fiscal slippages. In this connection, they also welcomed the authorities’ determination to fulfill the conditions necessary to reaching the HIPC completion point by the end of the year.

The Executive Board took the following decision:

Togo—Fourth Review Under the Three-Year Arrangement Under the Extended Credit Facility and Requests for Waivers of Performance Criteria and Augmentation of Access

1. The Republic of Togo has consulted with the Fund in accordance with paragraph 4.C(b) of the arrangement for the Republic of Togo under the Extended Credit Facility (the "ECF Arrangement") (EBS/08/41, 03/31/08) and paragraph 24 of the letter dated April 1, 2009 from the Minister of Economy and Finance of the Republic of Togo, to review program implementation.

2. The letter dated June 10, 2010 from the Minister of Economy and Finance of the Republic of Togo (the "June 2010 Letter") shall be attached to the ECF Arrangement, and the letters dated March 28, 2008, September 12, 2008, April 1, 2009, and October 30, 2009 from the Minister of Economy and Finance of the Republic of Togo, together with their attachments, shall be read as supplemented and modified by the June 2010 Letter.

3. Accordingly, the ECF Arrangement for the Republic of Togo shall be amended as follows:

(a) Paragraph 1(a) shall be revised to read as follows:

“(a) For a period of three years from the date on which this arrangement becomes effective, the Republic of Togo will have the right to obtain disbursements from the Trustee in a total amount equivalent to SDR 95.41 million, subject to the availability of resources in the PRG Trust."

(b) In paragraphs 2(e) and 2(f) "SDR 8.80 million" shall be replaced with "SDR 14.30 million."

(c) A new paragraph 2(g) shall be added to read as follows:

"(g) the seventh disbursement in an amount equivalent to SDR 8.80 million, will be available on or after April 30, 2011, at the request of the Republic of Togo and subject to paragraphs 4 and 5 of this Arrangement;"

(d) In Paragraph 4.D(a) references to "Table 1 of the October 2009 Letter" shall be replaced with references to "Table 1 of the June 2010 Letter."

(e) A new section 4.E shall be included after section 4.D in paragraph 4 of the Arrangement to read as follows:

"E. the seventh disbursement under this Arrangement specified in paragraph 2(g) above:

(a) if the Managing Director of the Trustee finds that with respect to the seventh disbursement, the data as of December 31, 2010, indicate that:

(i) the floor on domestic primary fiscal balance, or

(ii) the ceiling on net domestic financing,

as set out in Table 1 of the June 2010 Letter and further specified in the TMU as supplemented and modified by the October 2009 TMU, was not observed; or

(b) until the Trustee has determined that the sixth program review referred to in paragraph 36 of the June 2010 Letter, has been completed."

(f) In Paragraph 5(a) of the Arrangement the reference shall be to "Table 1 of the June 2010 Letter."

4. The Fund decides that the fourth program review contemplated in paragraph 4.C(b) of the ECF Arrangement for the Republic of Togo is completed, and the Republic of Togo may request the fifth disbursement referred to in paragraph 2(e) of the Arrangement, notwithstanding the non-observance of the end-December 2009 quantitative performance criteria on domestic primary fiscal balance and net domestic financing, specified in paragraphs 4.C(a)(i) and 4.C(a)(ii) of the Arrangement, respectively, and of the continuous performance criterion on contracting of nonconcessional external debt specified in paragraph 5(a)(i) of the Arrangement, on the condition that the information provided by the Republic of Togo on its performance under these criteria is accurate. (EBS/10/117, 6/11/10)

Decision No. 14667-(10/63), adopted
June 25, 2010

APPROVAL: August 9, 2010

SIDDHARTH TIWARI
Secretary