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July 19, 2018

**Statement by Mr. Mahlinza and Mr. Essuvi on Democratic Republic of São Tomé and
Príncipe
(Preliminary)
Executive Board Meeting
July 23, 2018**

We thank staff for their insightful report and Messrs. Sembene and Carvalho da Silveira for their informative Buff statement.

The Democratic Republic of Sao Tome and Principe has made progress in fiscal consolidation and structural reforms under extenuating circumstances. Overall program performance under the Extended Credit Facility (ECF) was mixed, with three out of five end-2017 performance criteria missed and structural reforms broadly on track. We note that the authorities have taken steps to implement corrective measures. Consequently, we **support completion of the fifth Review under the Extended Credit Facility and the authorities' request for Waivers of Nonobservance of Performance Criteria, and Financing Assurances Review.**

Economic activity decelerated slightly after a recovery in 2016. The performance of the economy was affected by a more restrictive fiscal policy and delays in external disbursements that impacted construction projects in 2017. At the same time, inflation rose, driven by increases in the import tariffs on some goods and a low agricultural outcome, due to unfavorable weather conditions. Nonetheless, medium term prospects appear positive, with growth estimated to rise to 5 percent as new infrastructure programs come on stream. Downside risks however abound, including pre-election pressures that could delay implementation of structural reforms, delays in external disbursements, tighter conditions in the external financial markets, and weaknesses in the banking sector. Going forward, we encourage the authorities to maintain fiscal consolidation and implement their structural reform agenda.

Continued fiscal consolidation will improve the fiscal position and bring debt to sustainable levels. We commend the authorities for implementing revenue and expenditure measures to reduce the domestic primary deficit over the last few years. Significant progress

has been made in cutting public spending, particularly the wage bill, transfers, and goods and services. At the same time, progress has been made in increasing revenue through collection of tax arrears and introduction of a new consumption tax on imported alcoholic beverages. However more effort is required to improve domestic revenue mobilization in order to reduce the debt burden and meet the large investment needs. We therefore welcome the authorities' commitment to implement revenue enhancing measures, including the collection of tax arrears. In this connection, we support the authorities for undertaking preparatory activities towards the introduction of VAT in 2019. *We would appreciate comments by staff on the feasibility of meeting the VAT implementation timeline of early 2019.* We also commend the authorities for their commitment to effectively apply the automatic fuel price adjustment mechanism.

A stable financial system is critical for sustained and inclusive growth. We note that stringent bank supervision has strengthened asset classification and urge the authorities to expedite implementation of the recommendations of the last safeguards assessment. We are encouraged by the authorities' efforts to step up recoveries and write-offs by banks, enforce collateral guidelines, and ensure strict oversight of banks' credit risk management frameworks and lending policies. We welcome the swift measures taken by BCSTP to intervene in Banco Privado and successfully completing the process of redenomination of the local currency. Further, we note that there is no information on the implementation of the AML/CFT framework in the staff report. *Could staff provide an update as well as information on the status of correspondent banking relationships?*

Structural reforms are essential to achieving strong and sustainable growth. In this respect, we welcome the completion of the tourism development strategy and the approval of the National Development Plan (NDP) for 2017–2022. We encourage the authorities to accelerate the implementation of the priorities reflected in the plan with a view to promote a diversified economy and inclusive growth. Further, we urge the authorities to expedite implementation of strategies to address the unreliable supply and high cost of electricity, including the development of cheaper energy sources. Finally, given that Sao Tome and Principe is a fragile state, we underscore the importance of continued provision of capacity development and urge staff to prioritize TA in the areas of domestic revenue mobilization, public financial management and financial sector regulation and supervision.