EXECUTIVE BOARD MEETING

EBS/20/162
Supplement 2

November 10, 2020

To: Members of the Executive Board

From: The Secretary

Subject: **Republic of South Sudan—Request for Disbursement Under the Rapid Credit Facility—Supplementary Information, Revised Proposed Decision, and Revised Letter of Intent**

Board Action:	Executive Directors' **consideration** (Formal)
Tentative Board Date:	**Wednesday, November 11, 2020**
Proposed Decision:	Page 2
Publication:	Yes*
Questions:	Ms. Lahreche, AFR (ext. 36643) Mr. Hobdari, AFR (ext. 36276) Ms. Jack, AFR (ext. 36293)
Document Transmittal in the Absence of an Objection and in accordance with Board policy:	After Board Consideration—African Development Bank, Arab Monetary Fund, Common Market for Eastern and Southern Africa, Islamic Development Bank, World Trade Organization

***The authorities have indicated that they consent to the Fund's publication of this paper.**

INTERNATIONAL MONETARY FUND

REPUBLIC OF SOUTH SUDAN

November 9, 2020

REQUEST FOR DISBURSEMENT UNDER THE RAPID CREDIT FACILITY—SUPPLEMENTARY INFORMATION, REVISED PROPOSED DECISION AND REVISED LETTER OF INTENT

Approved By

David Owen (AFR) and Gavin Gray (SPR)

Prepared by the African Department in consultation with the Legal Department and the Strategy, Policy, and Review Department

1. This supplement is to inform the Executive Directors that Mr. Dier Tong Ngor was appointed as Governor of the Bank of South Sudan on November 2, 2020, replacing Mr. Gamal Abdallah Wani.

2. Staff has held discussions with Mr. Ngor since his appointment. Mr. Ngor has expressed full commitment to the policies outlined in the Letter of Intent (LOI) and has signed the LOI (see attached). A revised proposed decision with the new date of the LOI is also attached to this supplement.

Revised Proposed Decision

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

1. Republic of South Sudan has requested a loan disbursement in an amount equivalent to SDR 36.9 million (15 percent quota) under the Rapid Credit Facility of the Poverty Reduction and Growth Trust.

2. The Fund notes the intentions of Republic of South Sudan as set forth in the letter from the Minister of Finance and Planning and the Governor of the Bank of South Sudan, dated November 9, 2020, and approves the disbursement in accordance with the request.

Revised Letter of Intent

Juba, November 9, 2020

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Ms. Georgieva,

1. A revitalized peace agreement reached in 2018 has ended a five-year conflict and paved the way to the formation of the transitional unity government in February 2020 and later to an agreement on the number of states and the appointment of state governors. We have also agreed on the power-sharing arrangements at the state level. Following a protracted economic downturn, economic growth turned positive in FY18/19 and inflation was brought down in FY19/20. However, the oil dependence of our economy makes it vulnerable to external shocks.

2. The COVID-19 pandemic and associated decline in oil prices continue to severely affect economic and social conditions in South Sudan. Due to its limited capacity, our health system has not been prepared to respond to the pandemic. As of mid-October, we recorded 2,847 positive cases and 55 deaths. We have implemented measures to contain the virus spread, including international flight suspension, land border restrictions, passenger bus prohibitions, evening curfews, and a mandatory 14-day quarantine period for travelers arriving from high-infection countries. We have allocated additional resources to the health sector and spent about US$8 million to purchase necessary medical equipment, repatriate South Sudanese students from abroad and provide food support to the most vulnerable in the population. To mitigate the economic implications of the pandemic, the Bank of South Sudan (BSS) has introduced some temporary measures. It eased monetary policy (cutting the central bank rate from 15 to 10 percent and the reserve requirement ratio from 20 to 10 percent) and suspended an earlier announced regulation of higher minimum paid-up capital for commercial banks. The BSS also encouraged commercial banks to allow loan moratoria and debt restructuring for distressed customers, by extending maturities and reducing monthly payments.

3. The continued economic recovery in FY19/20 was essential for mitigating the effects of the dual (health and economic) shocks, which severely afflicted—South Sudan at the end of the fiscal year. The economy has continued to weaken in FY20/21, affected by the pandemic-related restrictions and the decline in oil production and exports. We now project an economic contraction of 3.6 percent in FY20/21, compared with a pre-pandemic growth projection of 6.6 percent and estimated GDP growth of 13.2 percent in FY19/20. Inflation is expected to remain in double digits, due to a shortfall in domestic food production and exchange rate pressures. We expect government

revenues to decline by more than 30 percent relative to FY19/20, following the decline in oil prices and oil production, creating a sizable fiscal financing gap.

4. We are requesting emergency funding from the IMF under the Rapid Credit Facility (RCF) to finance our urgent balance of payment and fiscal needs, which are primarily driven by the collapse in oil prices. We are requesting IMF support in the amount of SDR 36.9 million, or 15 percent of quota (about US$52.2 million or 1.2 percent of GDP). While we expect these funds to be disbursed to the BSS, considering the sizable fiscal gap of SSP 36 billion (about 4 percent of GDP), we ask for this support to be made available to the budget by having it on-lent by the BSS to the government on the same terms as obtained from the IMF, and we will open a dedicated account at the BSS for the RCF disbursement.

5. We are committed to transparency in the use of these resources to support essential pandemic-related spending. We will ensure that all such transactions are recorded in the Integrated Financial Management Information System (IFMIS). We will publish all pandemic-related procurement contracts and other related documentation, along with the names of awarded companies and their beneficial ownership information within three months after contract signing, and publish the ex-post validation of delivery of the contracts within one year after the contract signing. We will publish reports on pandemic-related spending on a monthly basis. In addition, the Auditor General will conduct and publish an audit of all spending from this account on a quarterly basis. All the information listed will be published on the website of the Ministry of Finance and Planning as soon as they are completed.

6. We have already prepared, in consultation with Fund staff, a memorandum of understanding (MOU) between the Ministry of Finance and Planning and the BSS, stipulating *responsibilities for servicing financial obligations to the IMF. We have published* our most recent audited financial statements, and we will publish the subsequent statements on completion of the audits; further, we will take steps to improve the timeliness of the financial statements' publication going forward. The BSS will provide IMF staff with access to BSS's most recently completed audit reports and authorization to hold discussion with BSS' external auditors who were contracted by the National Audit Chamber.

7. In support of our request for an RCF, we have prepared a set of policies which would mitigate the effects of the pandemic and ensure orderly economic adjustment to the oil price shock. We are committed to implement fiscal consolidation, while working on restoring economic growth, reducing poverty, and supporting the peace process. We are committed to contain the fiscal deficit in FY20/21 at 2.5 percent of GDP. We are planning to close the FY20/21 balance of payments gap through a combination of IMF support and additional external financing, including donor support. We stand ready to undertake further fiscal adjustment, if expected financing does not materialize or revenue shortfalls occur, which we would achieve by delaying non-essential public sector investment. We have reinvigorated public financial management (PFM) reforms to strengthen expenditure controls and to improve the quality of public spending. These steps will be instrumental to develop our budgeting processes and will support our goal of maintaining a credible and sustainable fiscal path for FY21/22 and the medium term.

8. While rationalizing expenditures, we will protect expenditure on salaries, peace- and nation-building. An automatic decline in oil-related transfers—Transitional Financial Arrangement (TFA) payment and the transfers to oil producing states are indexed to oil prices—will not be sufficient to close the initial pandemic-driven fiscal gap (before expenditure adjustments) of more than 6 percent of GDP. To narrow the fiscal gap to 4 percent of GDP, we will take measures to contain non-essential spending and will reduce operational expenses from 10.6 percent of GDP in FY19/20 to 8 percent of GDP for FY20/21, and investment expenditures from 3.2 percent of GDP in FY19/20 to 2 percent of GDP for FY20/21.

9. We have addressed the issue of debt distress. The agreement with the Qatar National Bank (QNB) signed in July 2020 resolved our arrears on the short-term trade facility provided by the QNB in 2015. According to the IMF assessment, our public debt is now sustainable on a forward-looking basis. We recognize that the assessment critically hinges on our commitments to discontinue the use of expensive and non-transparent oil advances and continue to refrain from highly non-concessional borrowing. We have almost entirely paid back the residual oil advances and have not relied on them since May 2020. In light of the commitments above, we see some limited space for non-concessional borrowing this year for high-return projects. In the medium term, this commitment, combined with our PFM progress, would help us improve public investment and rely more on grants and concessional borrowing, which are important for us to maintain a sustainable debt situation and reduce the risk of debt distress.

10. To alleviate exchange rate pressures and bring down inflation, we will contain government borrowing from the BSS. Following a sharp decline in oil prices at the end of FY19/20, the Ministry of Finance and Planning used its overdraft facility with the BSS to offset revenue losses. We have partly repaid the overdraft facility. Given the scarcity of government financing, the Ministry of Finance and Planning will have to resort to limited borrowing from the BSS (0.6 percent of GDP) in FY20/21, in addition to the RCF disbursement on lent from the central bank. However, the practice of monetary financing of the fiscal deficit will be completely discontinued, starting at the end of FY20/21.

11. Monetary policy aims at stabilizing the exchange rate and bringing inflation down. In August 2020, the BSS discontinued the special accounts scheme, introduced in July 2017 in part to help build foreign exchange reserves. This mechanism proved ineffective in mobilizing FX. This is a first step towards unifying the exchange rate market, an objective that we plan on achieving with support from the Fund's technical assistance. Through appropriate prudential policies, the BSS is also planning to strengthen financial sector resilience.

12. We will accelerate our PFM reforms to strengthen institutions, even while acknowledging that we have made significant strides in improving the governance framework. The continued support of the leadership of the PFM Oversight Committee, established in April 2020, will be critical for keeping the momentum of the reforms. We agreed during the recently concluded capacity development mission to strengthen the macro-fiscal framework as well as the budget process and budget credibility. To advance this work, we will finalize a concept note for the PFM reform strategy, strengthen the financial management system (IFMIS), ensure adequate implementation of the Treasury Single Account, improve cash management practices, and seek technical assistance to

accurately identify and measure domestic arrears. Additionally, we will strengthen our debt management unit, with assistance from the IMF and the World Bank. We also commit to undergo a safeguards assessment by the Fund before Executive Board approval of any subsequent arrangement and to provide staff with access to the central bank's most recently completed audit reports and authorize our external auditors to hold discussions with staff. We will also enhance AML/CFT framework as well as our Anti-Corruption framework, and the capacity of the relevant authorities in South Sudan with the assistance of our international partners. We will enhance the information on oil production and oil-related contracts through the PFM Oversight Committee.

13. We believe that the measures and policies outlined in this letter are adequate for addressing the immediate economic and social challenges—not only our urgent balance-of-payments needs but also our poverty-reducing and growth-enhancing objectives, primarily through efforts to bolster macroeconomic stability. We are committed to transparency and accountability in the use of resources. The audits of all pandemic-related spending will validate the effectiveness of the spending and the systems we put in place, and provide lessons for further strengthening our institutions, processes and systems.

14. We will not introduce measures or policies that would worsen the balance-of-payments position and will not impose new or intensify existing trade restrictions. We will also not introduce or intensify existing restrictions on payments and transfers for current international transactions or multiple currency practices; or enter into bilateral payments agreements which are inconsistent with Article VIII of the IMF's Articles of Agreement. We will consult with the IMF staff on any additional measures that might be required to close the BOP and the fiscal gaps. We will also provide Fund staff with all information needed for monitoring our economic adjustment. We will continue a close policy dialogue with Fund staff and look forward to engaging in a Staff Monitored Program (SMP) after the RCF.

15. We consent to the publication of the IMF staff report, including this letter, and the debt sustainability analysis (DSA) prepared by the IMF and World Bank staffs.

Very truly yours,

/s/

H. E. Mr. Athian Ding Athian
Minister of Finance and Planning

/s/

Mr. Dier Tong Ngor
Governor,
Bank of South Sudan