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Angola: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

November 3, 2009

LETTER OF INTENT

November 3, 2009

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
700 19th Street N.W.
Washington DC 20431 USA

Dear Mr. Strauss-Kahn:

The Angolan economy has been buffeted by the sudden drop in the prices of its main export commodities. Growth has stalled and the sharp decline in oil exports has put pressure on Angola's external and fiscal positions, as well as on the National Bank of Angola's (BNA) international reserves.

To address these challenges, the Angola government has adopted a robust package of economic policies designed to rebuild international reserves, increase confidence in the kwanza and restore a sustainable macroeconomic position. We are cognizant of the particular burden this needed adjustment will have on the poor and the government is committed to implementing the necessary measures of social support to protect those Angolan citizens that are most vulnerable.

The attached Memorandum of Economic and Financial Policies (MEFP) sets out the policy package that the Angolan government has adopted for the period of 2009–11. The government stands ready to take all necessary policy measures to ensure the attainment of its economic and social objectives. In support of this effort, the government hereby requests a Stand-By Arrangement (SBA) with the Fund for a period of 27 months, in the amount of SDR 858.9 million (equivalent to 300 percent of quota). The first review under the SBA is scheduled for March 2010. The government is also working with other development partners to galvanize their financial support. Beyond the SBA, the government will continue to work toward a medium term agenda to deepen structural reforms on which long-term growth will ultimately depend.

Under the SBA, the government will regularly update the IMF on economic and policy developments and will provide the data needed for adequate monitoring of the program. During the period of the SBA, the government of Angola will maintain close policy dialogue with the IMF and is prepared to take any further measures as appropriate and will consult with the Fund in advance of revisions to measures already contained in the attached MEFP. In addition, in line with good communication to the public and markets, we authorize the IMF to publish this letter of intent, the attached MEFP and the related staff report.

Sincerely yours,

/s/	/s/
Manuel Nunes	Eduardo Leopoldo Severim de Morais
Minister of Economy	Minister of Finance

Attachments:
- Memorandum of Economic and Financial Policies
- Technical Memorandum of Understanding

ATTACHMENT I

MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES FOR 2010 UNDER THE FIRST YEAR PROGRAM OF THE STAND-BY ARRANGEMENT

I. INTRODUCTION AND BACKGROUND

1. Angola is facing significant economic stress, stemming from the sharp decline in the prices of our main exports (oil and diamond). Despite some recovery in international oil prices in recent months, the plunge in oil exports has put pressure on Angola's external and fiscal positions, resulting in significant loss of international reserves. Without decisive policy actions, Angola faces severe balance of payment pressures that could potentially erode the hard-won gains the country has made on macroeconomic stabilization in recent years.

2. **The objective of the government's policy adjustments is to restore a sustainable macroeconomic position while limiting the impact of the economic slowdown on the poor and vulnerable members of the Angolan society.** Our program is underpinned by three pillars: strengthening the underlying fiscal position, returning the foreign exchange market to normal market conditions, and safeguarding financial sector stability. Beyond the immediate goal of stabilizing the macroeconomic environment, the policy package also outlines structural reform areas we would like to pursue over the medium term and on which long-term non-oil sector growth will ultimately depend.

II. THE CURRENT ECONOMIC SETTING AND NEAR-TERM OUTLOOK

3. The Angolan economy is facing a challenging year in 2009.

- **Growth and inflation:** After recording a double-digit growth rate since 2004, real GDP growth has slowed sharply in 2009, largely because oil exports have declined Despite the economic slowdown, inflation increased to 13.8 percent in August (12-month basis) from 13 percent at end-2008 mainly due to higher food prices, exchange rate depreciation, and supply bottlenecks.

- **Fiscal and external position:** The plunge in oil revenues in the first half of 2009 has shifted both the fiscal and current account surpluses in 2008 to substantial deficits in 2009. Through June 2009, usable reserves fell by US$6 billion to US$10 billion (2¾ months of imports), partly reflecting the National Bank of Angola's (BNA) efforts to stabilize the exchange rate and the government's drawdown of its foreign currency deposits at the BNA as budget financing became difficult.

4. **In response to the global economic crisis, the government has taken forceful measures which have helped to stabilize the international reserves.** The BNA raised the rediscount rate and banks' reserve requirements and allowed a modest exchange rate depreciation, while limiting the auction of foreign exchange to the market. Fiscal policy has

also been tightened considerably through the 2009 supplementary budget, which envisages a substantial spending cut.

5. **We anticipate that an economic recovery will begin in the first half of 2010.** Real GDP growth will likely be broadly flat in 2009 but should grow in the range of 8–10 percent in 2010 and 2011, mainly owing to the recovery in oil production, but also due to stronger non-oil GDP growth mainly in agriculture, commerce and construction. This growth outlook is however subject to large margins of error given the fragile nature of the global economic recovery and the likely delayed response of Angola's non-oil sector to the external environment.

6. **The government believes that inflation will slow gradually during the program period.** Inflation is expected at about 13 percent in 2010 (end of period), and to fall further as confidence improves and the external position is strengthened. While the government's ambitious fiscal program and tight monetary policy will contribute towards reducing inflation, once we are able to rebuild our reserves to comfortable levels, exchange rate policy will likely have to play a role towards further reducing inflation.

7. **Despite a more favorable outlook compared to a year ago, we continue to face enormous challenges on macroeconomic management.** While reserve losses have been stemmed since July 2009, underlying pressures remain strong and market confidence has deteriorated significantly; strong dollar demand yielded a widening of the spread between the official and parallel market exchange rates to about 25 percent (from a normal spread of 5 percent) by end-September. Moreover, although the fiscal deficit has been contained, financing it domestically remains a challenge given the low demand for treasury paper. Consequently, through September 2009, the government accumulated US$2.5 billion of domestic arrears (3.6 percent of GDP). The program for which we are seeking IMF support seeks to overcome these challenges on macroeconomic management.

III. Macroeconomic Objectives and Policies for 2010

Macroeconomic Objectives: The government's economic program aims to rebuild reserves, increase confidence in the kwanza and restore a sustainable macroeconomic position during 2009–11. Below we describe the specific policies we have put in place to achieve these broad objectives. The specific quantitative targets and structural policies underlying our adjustment program are summarized in Tables 1 and 2.

Fiscal policy and addressing underlying weaknesses in public finances

8. **While we recognize that all policy instruments should play a role in the policy mix, there is consensus within the government that fiscal policy would need to continue to bear the brunt of the needed adjustment**. Therefore, our fiscal program for 2010 envisages a return to a small fiscal surplus for the year (1.5 percent of GDP), based on some recovery in oil revenues and a sizeable decline of the non-oil primary fiscal balance by about

6 percentage points of non-oil GDP in 2010 on the back of lower public spending. The government will aim to reduce the non-oil primary fiscal balance by another 6 percentage points of GDP in 2011 which will bring the non-oil primary deficit to about 41 percent of non-oil GDP.

9. **The proposed adjustment in our fiscal program for 2010 relies on both revenue growth and expenditure restraint**.

- Oil revenues are projected to increase significantly in both 2010 and 2011 due to increased oil production and more favorable terms of trade conditions. Non-oil revenues are expected to increase as well, but given that they account for less than 20 percent of total revenues, their impact on the overall fiscal stance will be limited.

- On the expenditure side, the 2010 budget will aim for a reduction of 6 percentage points of GDP. This reduction will include limiting the increase in the civil service wage bill to only 4 percent (in real terms) which will allow for a nominal adjustment of the civil service wages in line with inflation and an increase in government employment mainly in social sectors such as education and health. Moreover, the budget will include reducing subsidies to state-owned enterprises, and cutting spending on goods and services. Capital spending is also planned to remain at its 2009 level (in real terms), to allow for post-conflict-related infrastructure projects. Additionally, we will aim to maintain social spending at about 30 percent of total public spending, in line with recent years' average. The government will reduce its domestic arrears in the next few months and some space is provided in the 2010 budget for arrears reduction.

10. **Strengthening our debt management capacity is a high priority**. To keep our debt burden moderate, the government is committed to reducing the external nonconcessional credit as the concessional credit become available which is needed for the continuation of several post-conflict infrastructure projects, particularly in the areas of transportation, water and energy. We will limit our external non-concessional borrowing to US$2 billion under the program (Table 1). However, we are of the view that this borrowing ceiling could be reviewed in the context of SBA program reviews in the event that concessional loans to Angola fall short of our expectations to avoid jeopardizing our vital infrastructure reconstruction process. As concessional resources increase, the level of non-concessional borrowing decreases in the same amount. The government is also working with the World Bank and the Africa Development Bank to reduce implementation costs of infrastructure projects by strengthening the project appraisal framework and improving the procurement system. The government will enhance its monitoring of the debt of state-owned enterprises as part of its strategy to reform these enterprises.

11. The government is committed to addressing medium term fiscal challenges. Our reliance on oil revenues remains high, and the government recognizes the need to further develop an institutional framework which would help to minimize the impact of international oil price fluctuations on public finance and consequently the broader economy.

- To facilitate the convergence toward a sustainable fiscal position, we plan to establish an institutional framework that de-links the fiscal stance from unpredictable oil revenues and ensures that a larger proportion of windfall oil revenues is saved. In this context, after extensive discussions within the government and political leadership, we will submit to the cabinet the approval documents of the Angola Sovereign Wealth Fund, which will manage the oil surpluses of both Sonangol Concessionary and the Central Government, and is consistent with our medium-term fiscal framework as well as the sustainable development of Angola (Table 2). Thus, we would welcome technical assistance from the IMF on the setting up the Sovereign Wealth Fund which will be both a stabilization and a savings fund.

- To complement this framework, over the medium term, we will also consider putting in place a Fiscal Responsibility Law which will further help to guard against procyclical fiscal policy. Our intention is to institute, with advice from the IMF and World Bank, a stronger budgetary framework that will guarantee sound fiscal management and oblige the government to adhere to a prudent fiscal rule.

- The government is committed to reform the tax system, whose efficiency needs to be improved and efforts will be geared toward simplifying the tax system and reducing the already large informal sector and tax evasion. To launch these reforms, the Ministry of Finance has prepared a draft white paper on tax reform strategy which we have shared with the IMF and the government will welcome suggestions by the IMF staff to strengthen our tax reform agenda. Subsequently, the white paper will be discussed by the cabinet. Effective October 2009, the government will put in place a moratorium on issuing new tax incentives pending finalizing our new framework which will aim at rationalizing tax incentives.

12. **We are also committed to building on the progress we have made in reforming our public finance management (PFM) system.** We have recently decentralized budget execution to local governments, expanded the budget execution system (SIGFE) and produced for the first time the General Accounts of the state. We are committed to augment these measures with greater reinforcement of internal controls, stronger coordination between the current and capital budgets, and improvement of line ministries' budgeting capacity, consistent with the recommendations of the 2006 IMF fiscal ROSC. To this end, the government is being assisted by the United States Treasury to strengthen our capacity in this area.

13. **We will take further steps to improve fiscal transparency, including in regard to the activities of the state-owned enterprises (SOEs).** The large size of Angola's SOEs warrants greater fiscal transparency and better oversight of their activities to help monitor fiscal risks.

- We will ensure a timely reporting of quarterly budget execution of the central government and take measures to reduce the time lag on fiscal data reporting in general. To this end, Sonangol, the state-owned oil company, will also report its quarterly quasi-fiscal operations as well as provide its sources of financing and investment operations to the government (Table 2).

- The government plans to adopt a mechanism for a regular review of operational cash flows of major SOEs, including Sonangol. Given its important role in the allocation of oil revenues and quasi-fiscal activities, the audit of the accounts of Sonangol for 2008, including its quasi-fiscal operations, will be fully completed by an audit firm of international reputation by November, 2009 (Table 2). The government is committed to gradually phasing out the quasi-fiscal activities of Sonangol and overtime some of these quasi-fiscal activities will be directly undertaken by the central government. The government will also publish Sonangol's audited financial statements for 2007 and 2008 and adopt this as part of normal standard practice for the future. More generally, the government will examine its compliance with the IMF's principles of Resource Revenue Transparency and identify potential reform agenda.

Normalizing the foreign exchange market backed by prudent monetary management

14. **The government acknowledges the urgent need for renewing the auction system to facilitate the return to the normal functioning of the foreign exchange market.** On October 2, we renewed the auction system, which would help to facilitate the return of the foreign exchange market to normal market conditions and reduce the wedge between the official and parallel markets. This is being supported by a tight monetary policy, which should contain the demand for foreign currency consistent with the program's NIR targets. Going forward, once the foreign exchange market normalizes and a more comfortable external position is achieved, with the help of IMF technical assistance, the BNA will adopt concrete steps to streamline its foreign exchange intervention strategy. We are committed to continue with the market-based auction system over the program period.

15. **The BNA's monetary policy needs to support the program's objective of rebuilding reserves and an orderly return to normalcy of the foreign exchange market.**

- The recent monetary tightening by the BNA has led to a substantial deceleration in the growth of broad money (M2) to below 30 percent by end-August. The BNA will continue to maintain a tight monetary policy stance under the principle of sterilizing the dollar revenues coming from the oil sector that are going to be used for budget expenditure in kwanzas. To support exchange rate policy, the BNA will increase its policy rate to allow market interest rates to rise to a level that would achieve the program path for monetary aggregates (reserve money and broad money). However, as recommended by the best practices on fiscal policy, the costs of monetary policy should not lead to unsustainable growth of the public deficit service.

- The government will also use prudent domestic debt management to limit the drawdown of its deposit at the BNA and thereby support BNA's international reserves. More broadly, as part of monetary and fiscal coordination, the treasury will issue securities for its domestic financing of the government deficit and, in case of a shortfall in market financing, will drawdown its deposits at the BNA. To facilitate the market absorption of government debt, the Treasury will price its securities according to market based interest rate and gradually extend their maturity to long term as market confidence improves. The BNA would sterilize liquidity injection due to the government reduction of its deposits at the BNA by issuing BNA securities at the short-end of the yield curve. Over time we will need to further develop our liquidity management framework including ensuring that the liquidity management instruments are appropriately geared towards our overall monetary objectives. The authorities will aim to rebuild the BNA's reserves to about 3.2 months of import cover in 2010, and about 3.8 months in 2011.

16. **During the program period we will not intensify any existing exchange restrictions or introduce any new restrictions or multiple currency practices that are not consistent with our obligations under Article VIII section 2(a) and 3**. While during the course of 2009 we have enforced the existing exchange restrictions on current account transactions to prevent rapid loss of reserves, we are committed to phase these existing restrictions out by end-June 2010.

Strengthening the financial sector

17. **Maintaining confidence in the financial system is a key priority.** Thus we will put in place a comprehensive strategy to strengthen the financial sector and remain vigilant about the risks. While the financial soundness indicators appear to be at comfortable levels, banks' capital could be quickly eroded by a worsening of credit quality due to both the economic slowdown and credit risks stemming from high level of foreign currency lending. Thus, the BNA will reinforce its guidance to banks on maintaining adequate levels of capital and provisioning to cover such credit risk. We have already taken steps in this direction by requiring banks to classify loans and make provisions for expected losses and we will ensure that the banks are fully compliant with this requirement.

18. **The BNA will also review its regulatory and supervisory framework.** Prudential regulations have already been strengthened in line with the Basel Core Principles for Effective Supervision, including a Basel I capital adequacy framework, and a revised loan classification and provisioning standard. The BNA is committed to strengthening its oversight of the financial sector, including its risk-based bank supervision, with the enactment of prudential rules that appropriately reflect the balance sheet risks of foreign currency lending. We will also expand our on-site and off-site supervision activities, regularly discuss balance sheet developments and contingency plans with bank managers, including the impact of exchange rate changes that has already taken place on banks books,

and review the implementation of our banking resolution framework. To help us to implement these reforms, we would welcome a streamlined and focused Financial Sector Assessment Program (FSAP) mission in the first half of 2010 to assess developments in the financial sector and review our supervisory and regulatory framework.

Safeguards assessment

19. **The BNA welcomes the IMF's safeguards assessment and we believe it will help the BNA to strengthen its internal control systems.** The BNA's financial statements are externally audited by an independent external audit firm. We look forward to the findings and recommendations of the safeguards report and BNA will work with the IMF staff in the coming months to ensure the smooth completion of the safeguards assessment by the time of the first review of the Stand-By Arrangement (March 2010).

Risks and contingency plans

20. **While there are some signs that the global economy is on its way to recovery, the pace of the recovery remains fragile and uncertain, bringing economic and financial risks to the program.** The economic recovery could prove to be slower-than-expected in Angola's major trading partners, which would slow Angola's export growth through its impact on the demand for oil. If such a scenario materializes, the government stands ready to adjust policies, in close consultation with IMF staff, to ensure the achievement of a sustainable external position by the end of the program period. Finally, in the event of potentially disruptive conditions in the foreign exchange market, the authorities will consult with Fund staff on the appropriate policy response.

Program monitoring

21. **We understand that our SBA-supported program will generally be subject to quarterly reviews with quarterly performance criteria set out in the technical memorandum of understanding (TMU)**. Completion of the first two reviews scheduled for March and June 2010 will require observation of the quantitative PCs for end-December 2009 and end-March 2010, respectively, as specified in Table 1.

IV. MEDIUM-TERM STRUCTURAL AGENDA AND POVERTY REDUCTION

22. **The government of Angola recognizes that, in order to lay a robust foundation for non-oil sector growth over the medium term, deeper structural reforms are needed as a means of enhancing competitiveness and invigorating private sector development.** To this end, we plan to take measures to improve tax policy, strengthen tax administration, undertake public expenditure reviews and implement a rigorous civil service reform to enhance the public finances of our central government. For the broader public sector, we will initiate a coherent privatization strategy to address loss-making and non-viable state-owned enterprises (SOEs) which will also help to limit fiscal risks. In addition, we plan to introduce

in the near future a modern regulatory framework for water utilities and the energy sector. We will also initiate trade reforms with the accession to the World Trade Organization (WTO) as the long-term goal. The government recognizes that making effective progress in some of these areas would require extensive technical assistance from both the IMF and our other development partners which will help to build and strengthen our institutions. Thus this medium-term structural reform agenda will take some time to implement fully. We are also working on our poverty reduction strategy. In particular, we will aim to institute a reliable targeting mechanism for the poor. In this context, the government intends, in cooperation with the African Development Bank and the World Bank, to undertake a study on a viable social protection system to direct more resources to the poorest of Angola's citizens.

Table 1. Angola: Quantitative Performance Criteria (PC) and Indicative Targets (IT)

December 2009–December 2010

	December 2009 PC	March 2010 PC	June 2010 PC	September 2010 PC	December 2010 PC
Performance criteria 1/					
Usable net international reserves, floor (millions of US$) /2	9076	9567	10058	10549	11040
Net domestic credit of the BNA, ceiling (billions of kwanzas) 3/	-311	-308	-304	-300	-296
Net credit to the government by the banking system, Ceiling (billions of kwanzas) 4/	268	268	268	268	268
Non-accumulation of domestic arrears, cumulative effective January 1 5/	0	0	0	0	0
Non-accumulation of external arrears, cumulative effective January 1 6/	0	0	0	0	0
Non-concessional borrowing, cumulative effective January 1, ceiling (billions of US$)	2	2	2	2	2
Indicative target					
Floor on social spending, cumulative effective January 1 (billion of kwanza)	786	205	411	616	821
Nonoil fiscal deficit (on accrual basis), cumulative effective January 1, ceiling (billions of kwanzas)	1800	483	967	1450	1934

[1] Evaluated at the programmed exchange rate.

[2] The floor on NIR will be adjusted upward (downward) by the excess (shortfall) of oil revenues received by the Treasury and by the shortfall (excess) of the central government's external debt service relative to program assumptions. The adjustors will be applied only to the extent that the floor on the stock of NIR remains at or above US$6 billion.

[3] The ceiling for NDC will be adjusted upward (downard) by the shortfall (excess) in oil revenues received by the Treasury and by the excess (shortfall) of the central government's external debt service relative to program assumptions.

[4] The ceiling for NCG will be adjusted upward (downward) by the shortfall (excess) in oil revenues received by the Treasury and by the excess (shortfall) of the central government's external debt service relative to program assumptions .

[5] For December 2009 test date, cumulative from November 23.

[6] Continuous performance criterion.

Table 2. Angola: Proposed Structural Measures in the Program

Objectives	Actions	Timing
Prior actions		
Limit fiscal risks	Cabinet approval of the 2010 budget	Done - end October
Structural benchmarks		
Reduce financial sector vulnerability	Amend provisioning regulation to reflect the credit risk of foreign currency loans	March 2010
Reduce financial sector vulnerability	Development of an off-site supervisory tools to monitor banks' credit exposures by currency and maturities	March 2010
Limit fiscal risks	Cabinet approval of the tax reform strategy	June 2010
Improve public finance management	i) Publication of quarterly budget execution reports by the central government; ii) Reporting on a quarterly basis by major SOEs to the government of their quasi-fiscal operations and investment activities and publishing the reports	June 2010
Strengthen fiscal transparency	Completion of the 2008 audit of the accounts of Sonangol, including its quasifiscal operations, by an audit firm of international reputation	November 2009
Improve public finance management	Submission to the cabinet of the approval documents of the Angola Sovereign Wealth Fund (future SBA reviews will set benchmarks on implementation)	June 2010

ATTACHMENT II

TECHNICAL MEMORANDUM OF UNDERSTANDING (TMU)

This memorandum sets out the understandings between the Angolan authorities and the IMF staff regarding the definition of performance criteria and indicative targets, their adjustors, and data reporting requirements for the duration of the Stand-By-Arrangement. Where these criteria and targets are numeric, their unadjusted number values are stated in Table 1 of the Letter of Intent and Memorandum of Economic and Financial Policies. The values against which program compliance will be assessed will be adjusted up or down according to the adjustors specified in this Memorandum.

A. Ceiling on the Overall Non-Oil Primary Deficit on Accrual Basis of the Central Government

Definition

1. The Central Government will observe a ceiling on its Overall Non-Oil Primary Deficit on an Accrual Basis. The observance of this floor is an indicative target. **Overall Non-Oil Primary Deficit on Accrual Basis of the Central Government** is defined as the cumulative balance since the start of the calendar year of the its revenues, except oil-related, and expenditures of the Central Government, except interest payments. It is measured on an accrual basis and therefore it does not include accumulation or clearance of arrears.

Adjustors

- The ceiling will be adjusted downward by
    - The donor-financed expenditures in excess of the program assumptions.
- The ceiling will be adjusted upward by
    - The shortfall in donor-financed expenditures relative to program assumptions.

Data Reporting Requirements

2. Data on the implementation of the budget compiled by the Treasury will be provided on a quarterly basis, to be submitted no later than six weeks after the end of each reporting period.

3. The data to be reported are:

- Flows of (i) government revenue by category (including oil revenues received by the treasury); (ii) government expenditure, including primary current expenditure, domestic and external interest payments, and capital expenditure, of all donor-financed expenditures and resulting from agreements with the Paris Club; (iii) the gross clearance and gross accumulation of domestic and external arrears; (iv) external loan receipts and principal payments; (v) bank and nonbank financing, discriminating the domestic assets from liabilities; (vi) debt cancellation and debt swap operations; (vii) any other revenue, expenditure, or financing not included above.

- Stocks of public domestic debt and external debt.
- The monthly debt service projected the for the next 12-months and annual debt service for the outer years.

B. Ceiling on the Net Domestic Credit by the Central Bank

Definition

4. There will be a ceiling on the Net Domestic Credit by the Central Bank. The observance of this ceiling is a performance criterion. **Net Domestic Credit (NDC) by the Central Bank** are defined as the cumulative change, from the beginning of calendar-year, of the stocks of reserve money minus net foreign assets and other assets (net), evaluated at end-of-period exchange rates. Reserve money comprises bank reserves, cash in circulation, and deposits of the monetary institutions as well as BNA securities outstanding.

Adjustors

- The ceiling for NDC will be adjusted upward by
    - The shortfall in oil revenues received by the Treasury relative to program assumptions.
    - The external debt service by the central government in excess of program assumptions.
    - The shortfall of nonproject medium and long-term central government external borrowing relative to program assumptions.

- The ceiling for NDC will be adjusted downward by
    - the oil revenues received by the Treasury in excess of the program assumptions.
    - the shortfall in external debt service by the central government relative to program assumptions.
    - The nonproject medium and long-term central government external borrowing in excess of program assumptions.

For purposes of calculating the adjustors, these flows will be valued at current exchange rates.

Data reporting requirement

5. The monthly balance sheets of the central bank and the consolidated commercial banks will be transmitted on a monthly basis, with a maximum delay of three weeks.

C. Ceiling on Net Credit to the Central Government by the Banking System (NCG)

6. There will be a ceiling on the Net Credit to the Central Government by the Banking System. The observance of this ceiling is a performance criterion. **Net credit to the central government from the banking system** is defined as the overall position of the main central government institutions vis-à-vis the banking system—that is, the stock of all outstanding claims on the central government (loans, advances and arrears), and all other government debt instruments, such as long-term government securities, held by the BNA and commercial banks less all deposits held by the central government with the BNA and with commercial banks.

Adjustors

- The ceiling for NCG will be adjusted upward by
  - The shortfall in oil revenues received by the Treasury relative to program assumptions.
  - The external debt service by the central government in excess of program assumptions.
  - The shortfall of nonproject medium and long-term central government external borrowing relative to program assumptions.
- The ceiling for NCG will be adjusted downward by
  - The oil revenues received by the Treasury in excess of the program assumptions.
  - The shortfall in external debt service by the central government relative to program assumptions.
  - The nonproject medium and long-term central government external borrowing in excess of program assumptions.

For purposes of calculating the adjustors, these flows will be valued at current exchange rates.

Data reporting requirement

7. Data on the implementation of the budget compiled by the Ministry of Finance and Public Administration will be provided on a quarterly basis, to be submitted no later than five weeks after the end of each quarter, including (i) government domestic revenue by category; (ii) external budget support grants; (iii) government expenditure, including primary current expenditure, domestic and external interest payments, and capital expenditure, including domestically and budget support financed capital expenditure and estimates of externally project financed capital expenditure; (iv) the gross payment and gross accumulation of domestic accounts payable; (v) the gross payment and gross accumulation of domestic payments arrears; (vi) external loan receipts and principal payments; (vii) external arrears payments and accumulation; (viii) bank and nonbank financing; (ix) privatization and land sale receipts; and (x) any other revenue, expenditure, or financing not included above.

8. For the purposes of this memorandum, privatization and land proceeds will be understood to mean all monies received by the government from the sale or concessioning of a public company, organization, or facility to a private company or companies, organization(s), or individual(s), as well as any proceeds generated from the sale of government land and the liquidation of a public company, less restructuring costs.

D. Floor on the Usable Net International Reserves of the Central Bank

Definition

9. There will be a floor on the Usable Net International Reserves of the Central Bank. The observance of this floor is a performance criterion. **The Usable Net International Reserves (NIR) of the Central Bank** are gross international reserves of the Central Bank net of its international reserve liabilities and unconfirmed asset balances, calculated at the current exchange rates. Gross international reserves are those claims on nonresidents that are readily available for international payments (i.e., liquid and marketable and free of any pledges or encumbrances), controlled by the central bank and held for the purposes of meeting balance of payments needs and intervening in foreign exchange markets. It includes also government deposits abroad kept by the central bank. They include gold, holdings of SDRs, the reserve position at the IMF, holdings of foreign exchange and traveler's checks, demand and short-term deposits at foreign banks abroad, fixed-term deposits abroad that can be liquidated without penalty, and holdings of liquid investment-grade securities. For program purposes, unconfirmed balances are defined by the BNA as balances that appear on its books but have not been confirmed to the BNA by its correspondent banks and fund managers abroad, and estimated as of September 30, 2009 and subsequent test-dates. International reserve liabilities of the central bank comprise liabilities to nonresidents contracted by the central bank with remaining maturity of less than a year, any net off-balance-sheet position of the central bank (futures, forwards, swaps, or options) with either resident and nonresidents, any central bank arrears on principal and interest to external creditors and suppliers, and all purchases from the

IMF including purchases with original maturity of more than one year. The unconfirmed balances will be reported to staff by counterparty and account number.

Adjustors

- The floor on NIR will be adjusted upward by
    - The oil revenues received by the Treasury in excess of the program assumptions.
    - The shortfall in external debt service by the central government relative to program assumptions.
    - The lower-than-programmed unconfirmed asset balances at each test date.
    - The nonproject medium and long-term central government external borrowing in excess of program assumptions.
- The floor on NIR will be adjusted downward by
    - The shortfall in oil revenues by the Treasury relative to program assumptions.
    - The external debt service by the central government in excess of program assumptions.
    - The shortfall of nonproject medium and long-term central government external borrowing relative to program assumptions.
- The adjustors will be applied only to the extent that the floor on the stock of NIR remains at or above US$6 billion.

Data reporting requirement

10. A table prepared by the central bank will be transmitted weekly, with a maximum delay of one week, with the daily values of the stock of NIR and the decomposition of the daily variation of the NIR stock into foreign exchange sales to, and purchases from, the government, banks, nonbanks, and SDR purchases from the IMF, interest accrual, and valuation changes. The table will also indicate any off-balance sheet position denominated or payable in foreign currency by the central bank. The data on unconfirmed balances will be reported to Fund staff on a monthly basis within 4 weeks of the end of the reporting period. This will include a breakdown of unconfirmed balances by counterparty and account number, with sufficient detail to identify balances that were previously reported as unconfirmed but become confirmed at the reporting date.

11. Data on exports and imports, including volume and prices and compiled by the Customs and central bank will be transmitted on a quarterly basis within six weeks after the end of each quarter. A preliminary quarterly balance of payments (including nonproject medium and long-term central government external borrowing), compiled by the central bank, will be forwarded within six weeks after the end of each quarter.

E. Ceiling on Nonconcessional External Debt Contracted or Guaranteed by the Central Government

Definition

12. There will be a ceiling on Nonconcessional External Debt Contracted or Guaranteed by the Central Government for the program horizon starting effective from the date of Board approval of the arrangement.[1] Sonangol and other SOEs will not contract nonconcessional debt on behalf of the central government. The observance of this ceiling is a performance criterion. Under the program, observance of continuous ceilings on short-, medium- and long-term nonconcessional external debt constitute performance criteria. Nonconcessional external debt is defined as debt contracted or guaranteed by the central government with a grant element of less than 35 percent, calculated using currency-specific commercial interest reference rates (CIRRs) published by the Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD). Debt rescheduling and debt reorganization are excluded from the limits on nonconcessional external debt. The limits on new nonconcessional external debt contracted or guaranteed by the central government excludes borrowing from the Fund and are specified in Table 1 of the Memorandum of Economic and Financial Policies. The definition of short-term nonconcessional external debt excludes normal short-term (less than one year) import-related financing. The performance criterion on medium- and long-term nonconcessional external debt applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), 8/24/00) but also to commitments contracted or guaranteed for which disbursements have not been received. With respect to the assessment criterion on short-term nonconcessional external debt, the term "debt" has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), 8/24/00).

Data reporting requirements

13. The government will consult with Fund staff before assuming any liabilities in circumstances where they are uncertain whether the instrument in question falls under the assessment criterion. Details of all new external debt (including government guarantees), indicating terms of debt and creditors (concessional or nonconcessional), will be provided on a quarterly basis within six weeks of the end of each quarter.

[1] Given that Sonangol is independent from the government and operates as a commercial entity and due to the fact that it borrows without a government's guarantee, it is excluded from the ceiling on the non-concessional borrowing. Other SOEs are also excluded due to their low weight in the public sector and the fact that they do not pose substantial fiscal risks.

G. Nonaccumulation of Domestic Payments Arrears

Definition

14. The central Government may not accumulate additional domestic payments arrears. This obligation is a performance criterion. A domestic payment obligation is deemed to be in **arrears** if it has not been paid within the due date either specified by the budget law or contractually agreed with the creditor. After rescheduling by agreement with the creditor, the obligation rescheduled is not considered in arrears anymore.

Data reporting requirement

15. The Treasury will submit on a quarterly basis a detailed table of the stock of domestic payments arrears, including the accumulation, clearance, rescheduling and write-off of domestic payments arrears during the quarter. The data are to be provided within six weeks after the end of the quarter.

H. Nonaccumulation of External Payments Arrears

Definition

16. The central Government may not accumulate external payments arrears. This obligation is a performance criterion. **External arrears** are defined as total external debt-service obligations of the government and the central bank that have not been paid by the time they are due, except where agreements between the government and creditors explicitly provide for a grace period after such obligations falling due, in which case the obligation will be in arrears if not paid within the grace period. Obligations in negotiation with creditors are considered arrears until an agreement is legally in effect.

Data reporting requirements

17. Data on external arrears accumulation, clearance, and rescheduling will be transmitted weekly by the BNA at most one week after the fact.

I. Floor on the Central Government Social Expenditures

Definition

18. There will be a floor on the Central Government Social Expenditures. The observance of this floor is an indicative target. Social Spending comprises spending on the following sectors: education, health, rural development, and social affairs, both spending for the current year and arrears repayment related to these sectors.

Data reporting requirements

19. Data on Social Spending will be compiled by the Treasury and will be provided on a quarterly basis, to be submitted no later than six weeks after the end of each reporting period.