INTERNATIONAL MONETARY FUND

IMF Country Report No. 12/340

LIBERIA

2012 ARTICLE IV CONSULTATION

November 2012

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2012 Article IV consultation with Liberia, the following documents have been released and are included in this package:

- **Staff Report** for the 2012 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on September 21, 2012, with the officials of Liberia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on November 2, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- **Background Notes** prepared by the IMF.
- **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- **Public Information Notice** (PIN) summarizing the views of the Executive Board as expressed during its November 19, 2012 discussion of the staff report that concluded the Article IV consultation.
- **Statement by the Executive Director** for Liberia.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Liberia*
Memorandum of Economic and Financial Policies by the authorities of Liberia*
Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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International Monetary Fund
Washington, D.C.

LIBERIA

November 2, 2012

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION AND REQUEST FOR THREE-YEAR ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY

KEY ISSUES

Background: Liberia recorded strong macroeconomic performance under a three-year Extended Credit Facility (ECF) Arrangement—successfully completed in May 2012—but poverty remains pervasive, further reforms are warranted to promote broad based growth, and UN forces are still required to underpin social stability.

Article IV consultation and program: The last Article IV consultation was concluded on December 8, 2010. The Executive Board completed the 8th and last review under the Extended Credit Facility on May 9, 2012.

Outlook and risks: The short- to medium-term outlook remains favorable, although subject to considerable risks. Following resumption of iron ore exports in 2011, real GDP growth is estimated at close to 9 percent in 2012, supported by strong growth in the mining sector and expansionary fiscal policy to accommodate a scaling up of infrastructure investment. Adverse movements in the terms of trade and inflationary pressures from international food and oil prices pose risks in the short term. The authorities are requesting an Extended Credit Facility to buttress economic stability while supporting their new poverty reduction and growth strategy.

Staff views: Staff recommends the conclusion of the 2012 Article IV consultation and approval of the three-year arrangement under the Extended Credit Facility. The authorities have consented to publication of this report following the completion of the review.

Approved By

Michel Lazare (AFR) and Chris Lane (SPR)

Discussions were held in Monrovia July 10–24 and September 14–21, 2012. The mission comprised Ms. McAuliffe (head), Messrs. Ismail and Rosales (AFR), and Ms. Sharma (SPR). Mr. Sobolev, resident representative, assisted the mission. The mission met with Minister of Finance Konneh; Governor Jones of the Central Bank of Liberia; Deputy Governors Bettie and Sirleaf of the Central Bank of Liberia; other senior officials, and representatives of the private sector, civil society, and development partners. Mr. Saidy (OED) also joined the discussions and Mr. Graham (World Bank) participated in the concluding discussions. The mission briefed President Johnson Sirleaf on its main findings.

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THE CONTEXT

1. **Liberia made strong macroeconomic gains under a just-completed Extended Credit Facility (ECF) Arrangement, but macroeconomic stability has been hard won, development challenges are daunting, and poverty remains pervasive**. Following an initial post-conflict boost, economic growth has averaged 7 percent a year since 2009 (mostly from non-mining activities before the resumption of iron ore exports in late 2011), while inflation has been largely contained at or near single digits (Figure 1).[1] Tax revenue has steadily increased as a share of GDP, the economy has rapidly monetized, and external debt has been reduced significantly, thanks to substantial debt relief. Nonetheless, Liberia remains a poor country, with massive infrastructure gaps and large development needs. Poverty is pervasive (at 84 percent of the population),[2] and Liberia ranks near the bottom of the UN's Human Development Index (HDI)[3] and is unlikely to meet many of its Millennium Development Goals (MDG) (Table 1 and Figure 2). Job creation is slow, and the economy is unable to absorb the large number of youth and ex-combatants. Private sector development is further constrained by limited access to financial services and a weak credit environment. The economy also remains heavily dollarized (85 percent of commercial bank deposits), and monetary policy plays a limited role in economic management.[4]

2. **Liberia remains a fragile state, with weak institutions**. The sociopolitical situation is gradually improving in the wake of the second national elections in November 2011, but the country remains dependent on UN troops and police (UNMIL) to underpin security. The re-election of President Johnson Sirleaf has been endorsed by international elections observers as transparent and fair, and the UN recently approved a gradual drawdown of its peacekeeping operations (excluding UN police) from the current level of 8,000 troops to about 4,000 by 2015. But building domestic security capacity to undertake some critical security functions transferred from UNMIL is an ongoing challenge. Governance remains a serious concern, and Liberia still ranks high (91 out of 164 countries) in Transparency International's (TI's) latest global corruption barometer of the most corrupt nations.[5]

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[1] Staff revised the entire GDP series for Liberia significantly upward on account of newly available data from the national authorities and the World Bank on activity in the services and iron ore sectors (Appendix I).

[2] Purchasing Power Parity (PPP) basis using a poverty line of US$1.25 per day.

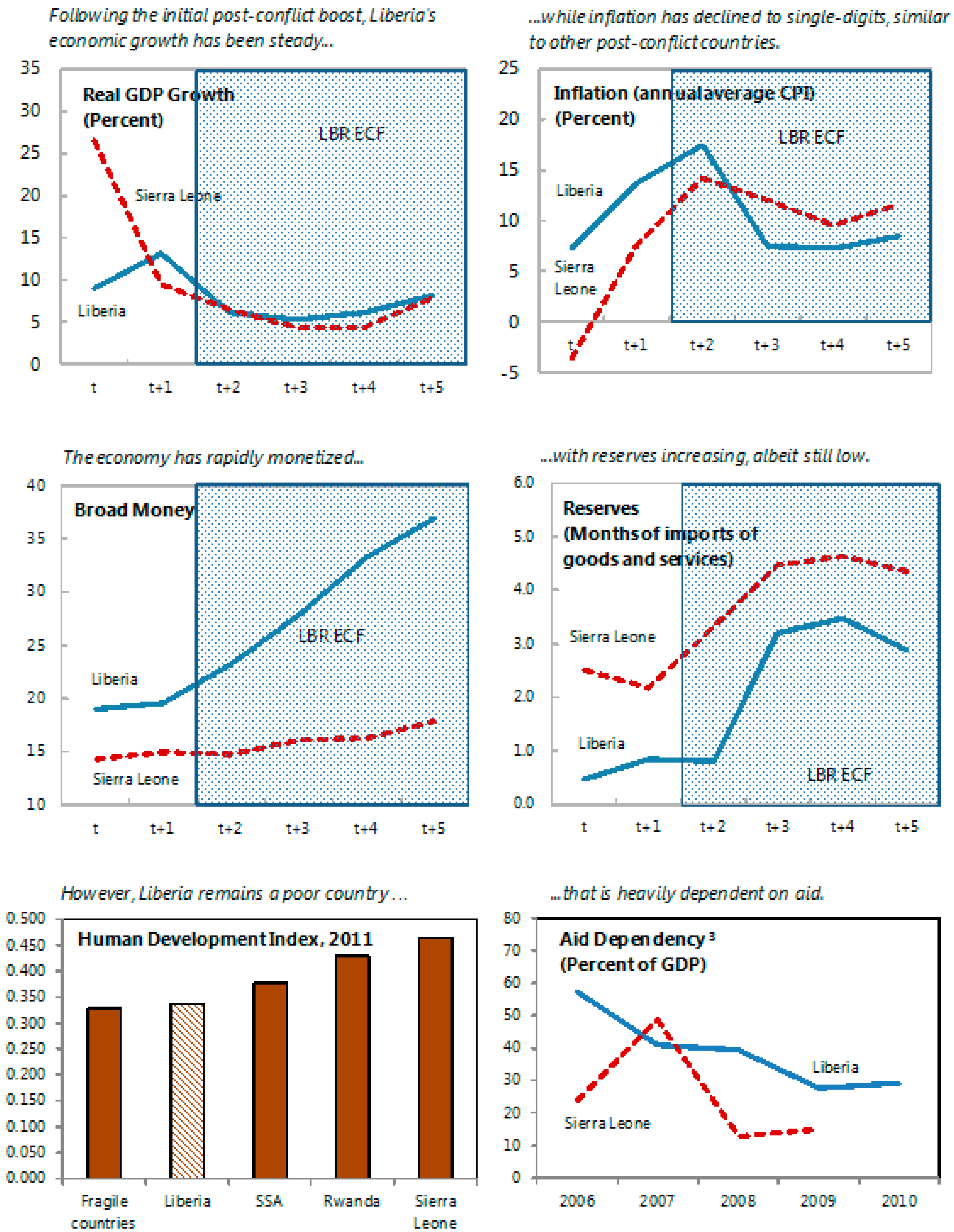
[3] Liberia is ranked 182 out of 187 countries in the 2011 HDI.

[4] Liberia has been heavily dollarized since its founding in 1847. Both the LD and the U.S. dollar are legal tender in Liberia. The de jure exchange rate policy is a managed float.

[5] Transparency International's 2011 Corruption Perceptions Index (CPI).

Figure 1. Liberia: A Post-Conflict Comparison[1] [2]

(Percent of GDP, unless indicated otherwise)



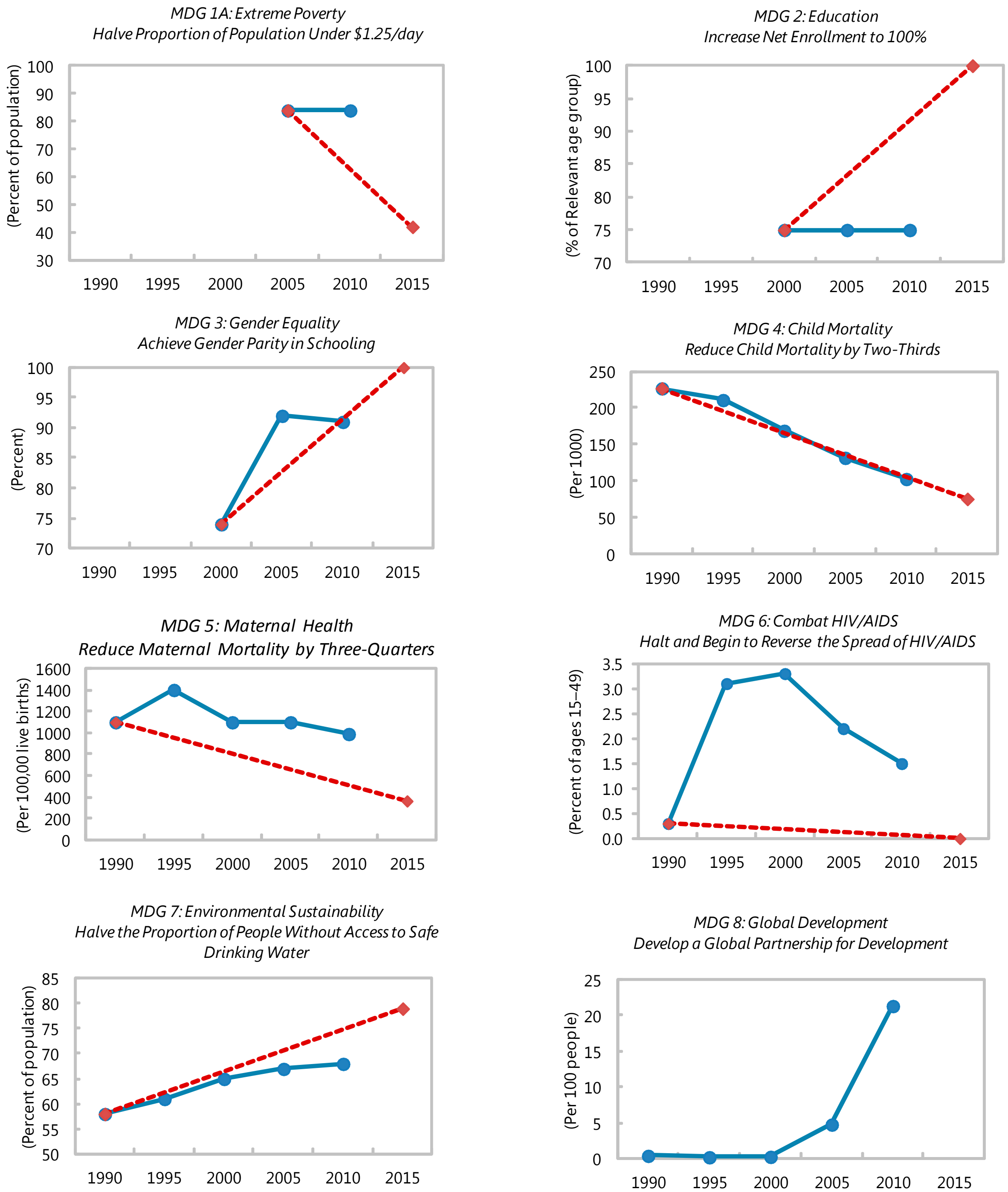
Sources: OECD; IMF, 2012 Spring World Economic Outlook; and LBR country database.

[1] t refers to resumption of elected government. For Liberia, t=2006; Sierra Leone, t=2002.

[2] The shaded area is the period of Liberia ECF which started in 2008.

[3] Aid dependency is defined as official transfers/GDP. For Liberia, UNMIL related transfers are excluded.

Figure 2. Liberia: MDG Progress Report, 1990–2015



Source: World Bank, Millennium Development Goals database.
Note: Solid line indicates observed performance, while dotted line indicates required achievement.

3. **Much more needs to be done to address Liberia's significant post-conflict development needs**. The government has set an ambitious agenda to transform Liberia into a middle-income country by 2030, the underlying theme of their second Poverty Reduction and Growth Strategy (PRS2)—the Agenda for Transformation—and has requested a successor ECF arrangement to support its program (Box 1).[6] The strategy focuses on achieving accelerated broad-based growth through scaling up investment in infrastructure and human capital, raising agricultural productivity, and fostering food security, employment creation, and deepening financial markets—areas where progress fell short under the first poverty reduction strategy (PRS1).

MEFP ¶ 8

4. **Staff sees merit in a successor ECF arrangement**. A successor program would help safeguard macroeconomic stability while bolstering donor support for public investment and social programs. The authorities' have strengthened their policies, aligning them with advice from the last Article IV consultation and subsequent discussions under the previous ECF arrangement (Box 2). At the same time, there are several key administrative reforms on the government's reform agenda that would benefit from continued close IMF engagement. There is also a medium-term need to build up reserve coverage to cope with global market uncertainties, but policy space is limited given the need to direct resources toward infrastructure and priority social spending.

[6] The PRS2 covers 2012–17. It is planned to be formally launched in late 2012.

Box 1. Liberia: The Agenda for Transformation (2012–17)

The Agenda for Transformation is a five-year development plan that underpins Vision 2030 to achieve middle-income status by 2030. The plan focuses on investments in five strategic pillars—at an estimated cost of $3.3 billion over the five-year period—to increase productivity, boost economic growth, and improve social inclusion, particularly among youth. The pillars are

- *Economic transformation,* particularly rehabilitating the hydropower plant, roads, and ports, and updating information and communications technology;
- *Human development* especially education and health;
- *Peace, security, and the rule of law*;
- *Governance and public institutions* to modernize the public sector and enhance transparency and accountability; and
- *Cross-cutting issues* focussed on youth skills, child protection, gender equality, and human rights.

Financing the investment program

- The government plans to cover 12–15 percent of investments with its own resources and is planning a pledging donors' conference in late 2012 to secure loans and grants.

Liberia: Agenda for Transformation Costing Summary (US$, millions)

	FY 12/13	FY 13/14	FY 14/15	FY 15/16	FY 16/17	Five Year
Pillar 1. Economic transformation	594.1	532.4	439.4	354.9	267.8	2,188.6
Pillar 2. Human development	87.2	100.9	120.8	121.1	128.9	558.9
Pillar 3. Peace, security, and rule of law	73.1	90.3	92.1	77.1	73.0	405.6
Pillar 4. Governance and public institutions	40.3	16.5	14.5	14.1	10.0	95.5
Pillar 5. Cross-cutting issues	19.5	28.7	22.5	22.1	19.2	111.9
Total	814.2	768.9	689.3	589.2	498.9	3,360.5

Source: Ministry of Finance, Agenda for Transformation (as of August 30, 2012).

Box 2. Liberia: Performance Under the Previous ECF Arrangement and Lessons Learned

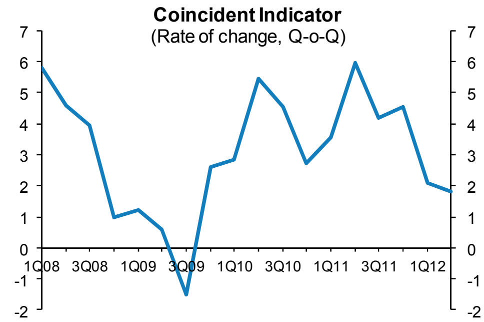
Performance under the first ECF arrangement (2008–12) was strong. All quantitative targets were met since the second review, and most of the structural reform agenda was implemented. Improved policies underlie this performance, aligned with advice from the 2010 Article IV Consultation and the program discussions. Prudent fiscal policy and strengthened public financial management contributed to a near doubling of government revenue, resumption of direct budget support, and initiation of significant infrastructure development projects without accumulation of expenditure arrears. Monetary policy focused on accumulating reserves, which sizably outperformed expectations during the program. Financial policies focused on strengthening the banking system and promoting intermediation.

Despite the progress, weaknesses remain in program implementation. These include significant delays in budget passage and implementation; slow pace of execution of donor-financed infrastructure projects; persistent weaknesses in the banking sector, including access to credit; and little or no progress in reforming state-owned enterprises (SOEs) or tackling poor governance.

Key lessons from the first ECF arrangement have been incorporated in the successor ECF arrangement. These include linking the Medium-Term Expenditure Framework (MTEF) to priorities in infrastructure development, security, and service delivery, in line with the PRS2, and aligning the MTEF with donor support; linking resource revenue to priority investment spending; focusing public investment initially on a few macro critical projects pending improved implementation capacity; customizing technical assistance to support policy design and program implementation; and implementing a more flexible debt management framework to support multiyear investment programs.

CONTINUED ROBUST ECONOMIC GROWTH

5. **Overall economic activity has remained robust in 2012, with inflation declining (Table 2 and Figure 3)**. Growth has been driven mainly by the iron ore sector—which resumed exports in 2011 for the first time since the end of the civil war—and rising activity in construction and services. Growth in the mining sector, however, has not spilled over to the non-mining economy. Short-term indicators point to a slowdown in non-mining activity in the first half of 2012 owing to declining rubber exports and the impact of elevated food and fuel prices on consumption. Following spikes in food and oil prices in 2011 and early 2012, U.S. dollar-denominated inflation declined to under 4 percent by end-June and is expected to remain in single digits through end-2012.



Note: This indicator of activity combines seven monthly series (exports, rice imports, cement production, government expenditure, broad money, private credit, and the exchange rate).

6. **Trade has expanded, but the overall external position remains stable (Table 3)**.[7] The trade deficit has widened in 2012 because of higher concession-financed capital imports and rising food and fuel import prices, offsetting the rise in iron ore exports. Reserve coverage has remained relatively stable at about 2½ months of imports. The Liberian dollar (LD), which was volatile in the first half of 2012, mirroring uncertainty on terms of trade and foreign inflows, has stabilized since June.

7. **The overall fiscal deficit including grants for FY 2011/12 (July–June), at 3.2 percent of GDP, was larger than expected (Table 4)**. MEFP ¶ 7

This reflects delays in collecting large one-off payments from iron ore concessions—which more than offset strong performance in trade taxes—and overruns in current and capital spending (including higher-than-budgeted spending on wages and salaries for new teachers).[8] Capital expenditure was higher than previously estimated, reflecting the execution of unbudgeted projects including the dredging of a port and road rehabilitation. Expenditure overruns were financed domestically through drawing down government deposits and direct borrowing from the central bank.

8. **The expansion in the financial system is decelerating because credit to the private sector has tightened on account of increasing bank fragilities**. Broad money growth has nearly halved on account of a slowdown in bank credit (Table 5 and Figure 4). The financial sector has further weakened owing to high credit risk, increasingly high non-performing loans, and still-weak bank profitability.[9]

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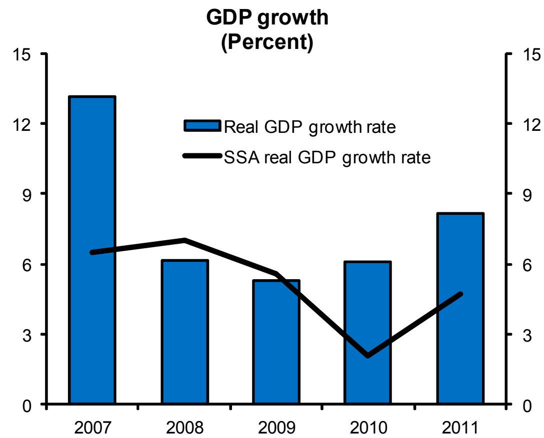
[7] Foreign inflow breakdown was revised significantly on account of re-classification of some financing to the iron ore sector from foreign direct investment to borrowing consistent with concession agreements.

[8] An anticipated decline in trade taxes resulting from adoption of GATT valuation and the first step of adopting the regional common external tariff did not materialize.

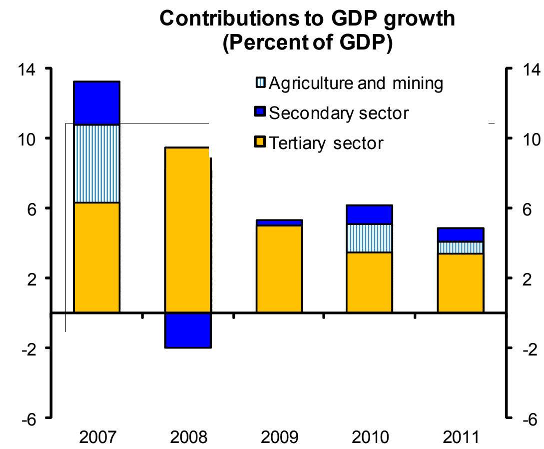
[9] EBS/11/164.

Figure 3. Liberia: Recent Economic Developments

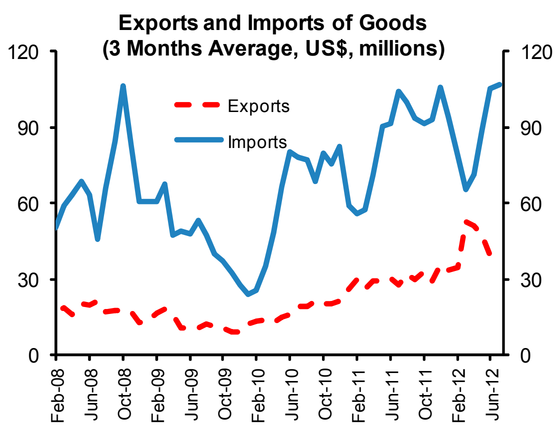
Economic activity has been strong since the resumption of political stability...



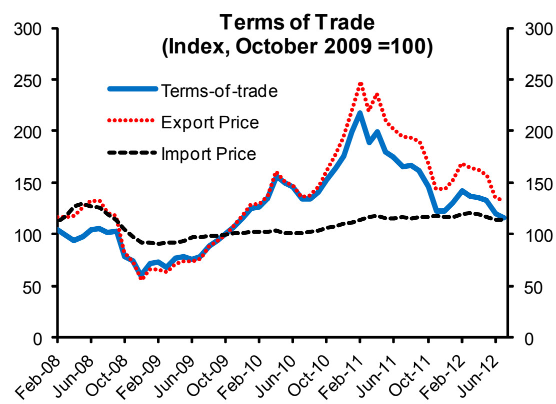
...driven by growth in services and construction.



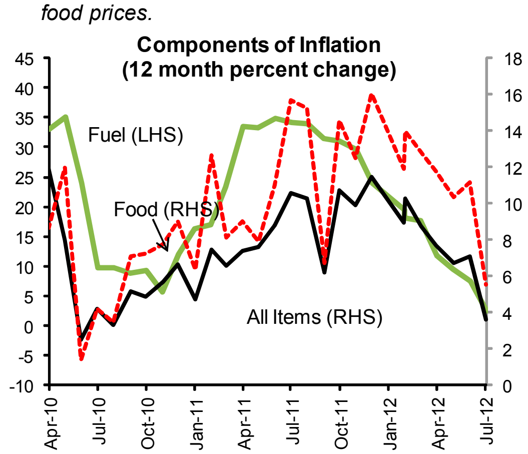
Exports have picked up sharply since late 2011,...



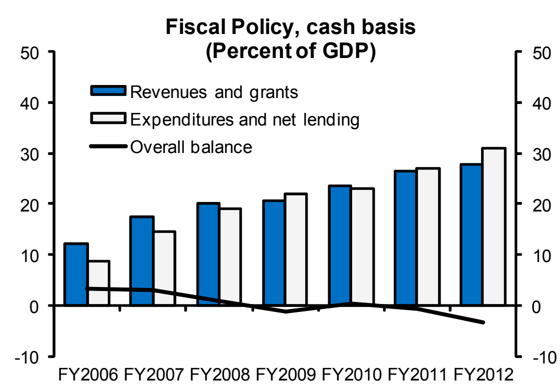
...reflecting improved terms of trade.



Inflation has been broadly stable owing to moderating food prices.



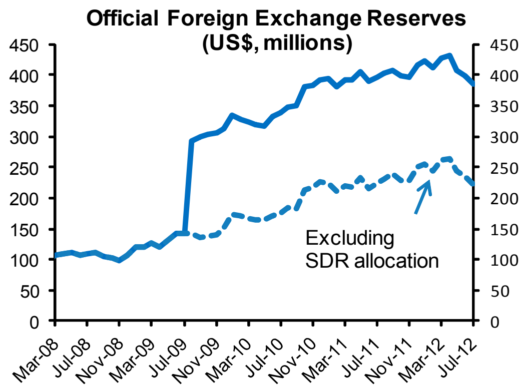
The fiscal position, which had been broadly stable, deteriorated in FY2012 because of current and capital spending overruns.



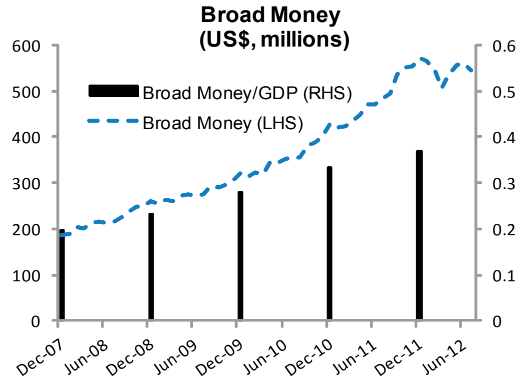
Sources: Liberian authorities and IMF staff estimates and projections.

Figure 4. Liberia: Monetary and Financial Developments

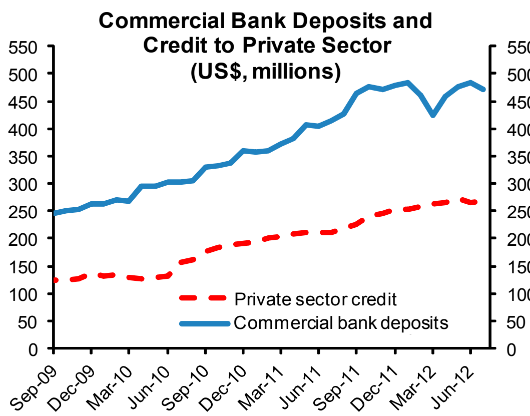
Reserves have declined slightly owing to one-off factors,...



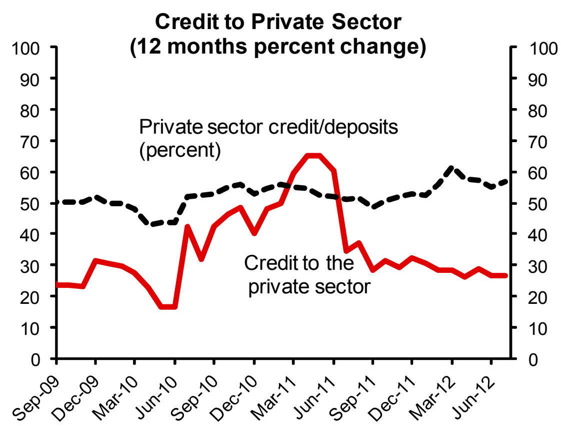
...and broad money growth is slowing from a high base.



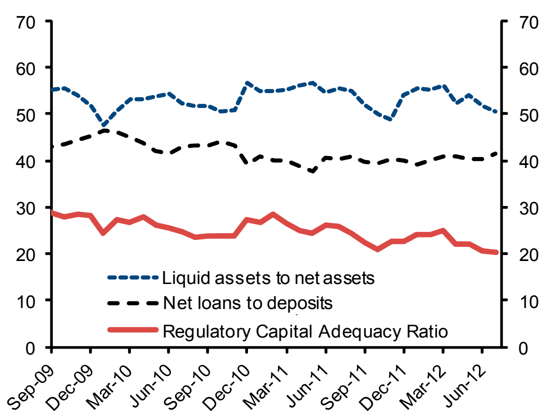
Growth of commercial bank deposits has also slowed,...



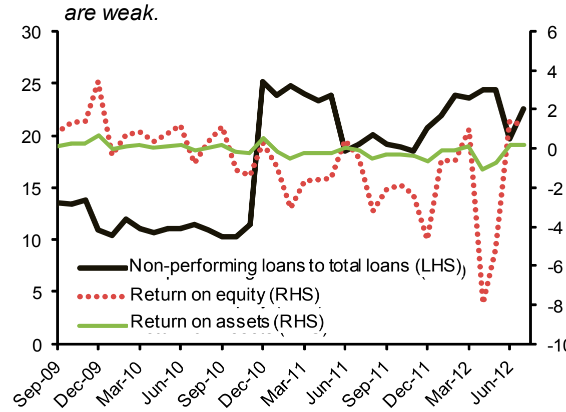
...while private sector credit growth is moderating.



Banks remain well capitalized and highly liquid,...



...although NPLs are elevated and bank returns are weak.



Sources: Liberian authorities and IMF staff estimates and projections.

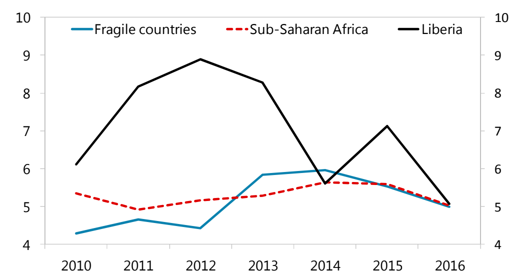
MEETING THE CHALLENGES OF MAINTAINING MACROECONOMIC STABILITY WHILE SCALING UP PUBLIC INVESTMENT

9. **The Article IV consultation discussions focused on policies to consolidate macroeconomic stabilization and lay the basis for accelerated and diversified growth**. The authorities and staff agreed that achieving high, broad-based growth and job creation in the next decade or so will require a significant increase in infrastructure and social investments, aligned with the PRS2. The authorities need to (i) build policy buffers to mitigate vulnerabilities; (ii) catalyze expected strong natural resource revenue to support the development agenda; and (iii) create a favorable business climate to support broad-based growth and job creation.

A. Favorable Outlook with Risks

10. **The economic outlook is favorable but not without risks**. Real GDP growth is projected at between 8 and 9 percent in 2012–13, above the average for Sub-Saharan Africa (SSA) and other fragile countries (Table 6 and Figure 5).[10] Increasing commodity exports, strong foreign direct investment (FDI), and large infrastructure investment are expected to underpin medium-term economic activity. Mining activity will peak in 2012, reflecting the pickup of iron ore exports, and then will surge again in 2015 as production capacity in the only currently operating iron ore mine reaches full capacity. However, the weak outlook for iron ore prices may limit the macroeconomic impact of higher mining production, especially on revenue and export receipts. Following the one-off slow down in 2012, non-mining activity is projected to normalize and increase steadily over the medium term driven primarily by construction and services. Inflation is expected to moderate to 6–7 percent by end-2012. The external current account deficit is expected to widen further in 2012–14 owing to investment-related imports, and then narrow over the medium term as these imports unwind and exports rise. Reserve coverage would remain stable—albeit low—at about 2½ months of imports (Box 3).[11]

Real GDP Growth
(Percent)



Sources: WEO and country database.

[10] Sub-Saharan Africa Fragile States as defined in the IMF *Regional Economic Outlook: Sub-Saharan Africa*: *Maintaining Growth in an Uncertain World*, October 2012. The countries include Burundi, Central African Republic, Comoros, the Democratic Republic of the Congo, Côte d'Ivoire, Eritrea, Guinea, Guinea-Bissau, Liberia, São Tomé & Príncipe, Togo, and Zimbabwe. In 2015 and 2016, Guinea and São Tomé & Príncipe are non-iron ore and non-oil GDP.

[11] Excluding IMF disbursements.

Liberia: Medium-term Outlook, 2009–15

	2009	2010 Prel.	2011 Prel.	2012 Proj.	2013 Proj.	2014 Proj.	2015 Proj.
	(Annual percentage change)						
GDP at constant prices	5.3	6.1	8.2	8.9	8.3	5.6	7.1
Real GDP excluding mining sector	5.3	5.8	5.8	3.8	6.1	6.8	7.3
Consumer prices (average)	7.4	7.3	8.5	6.6	5.6	5.0	5.0
Consumer prices (US dollar denominated, year-on-year)	2.4	1.3	10.2	3.2	1.3	1.8	1.6
	(Percent of GDP, unless otherwise indicated)						
Central government budget [1]							
Total revenue and grants	20.7	23.5	26.4	27.8	27.3	28.8	27.6
Of which: total revenue	18.6	22.5	23.6	26.1	24.9	26.5	25.8
Total expenditure and net lending	21.9	23.1	27.0	31.0	33.3	35.4	33.8
Overall fiscal balance (including grants)	-1.2	0.5	-0.6	-3.2	-6.0	-6.6	-6.2
Current account balance (including official grants)	-28.8	-32.8	-34.1	-52.4	-62.4	-65.8	-39.3
Gross official reserves (months of imports) [2]	3.2	3.8	3.0	2.6	2.7	2.8	3.0

Sources: Liberian authorities and IMF staff estimates and projections.

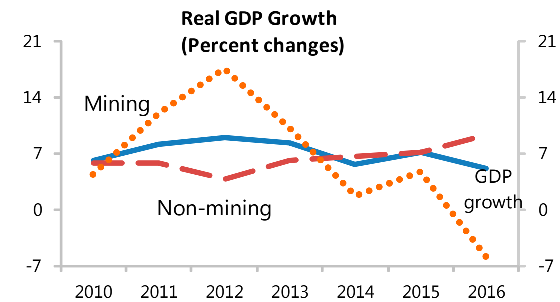
[1] Budget data expressed as fiscal year ending in June on a cash basis, i.e., 2011 = FY2010/11.

[2] Excludes UNMIL service and iron ore concessions related imports, but includes IMF disbursements under the requested ECF.

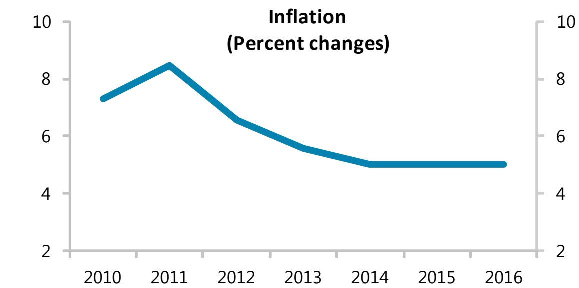
Figure 5. Liberia: Medium-Term Outlook, 2010–16

(Percent of GDP, unless indicated otherwise)

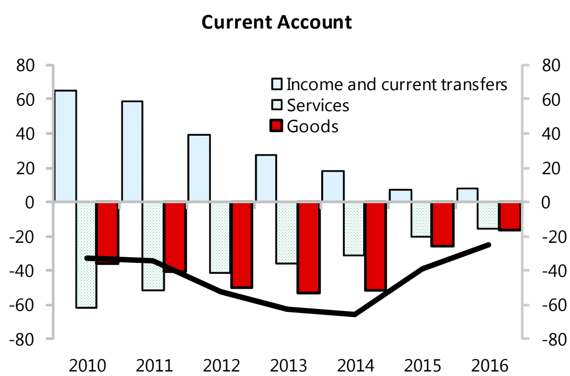
The outlook over the medium term is positive, helped by the expansion of the mining sector,...



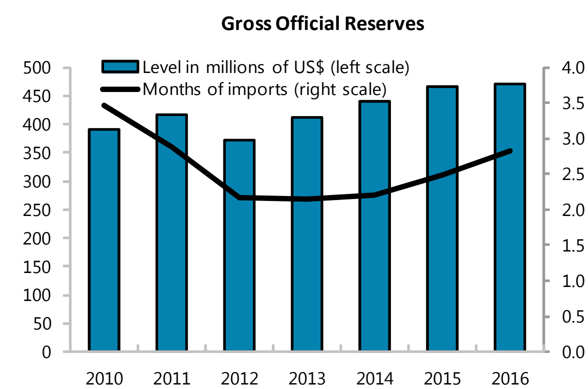
... while inflation continues to moderate.



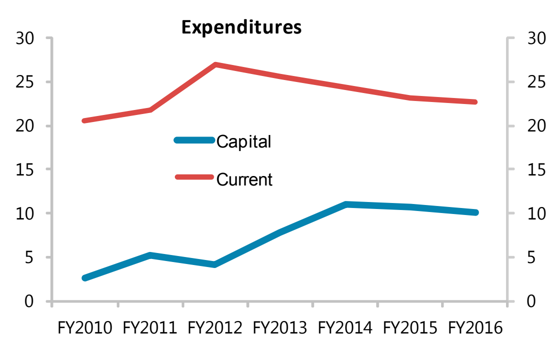
Strong export performance will contribute to narrow the trade and current account deficits,...



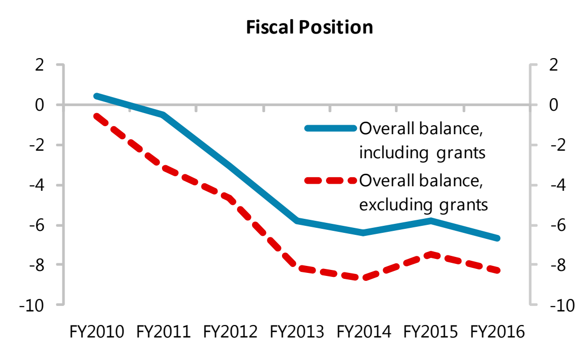
... increasing reserves to three months of imports.



Current spending is expected to moderate, creating some fiscal space for capital spending...



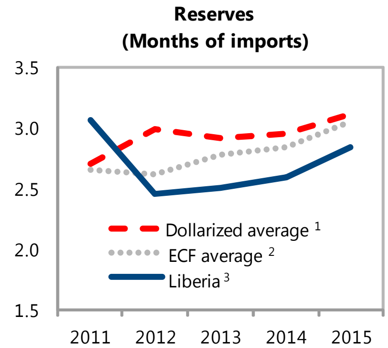
while the fiscal deficit widens, reflecting the ambitious public sector investment program.



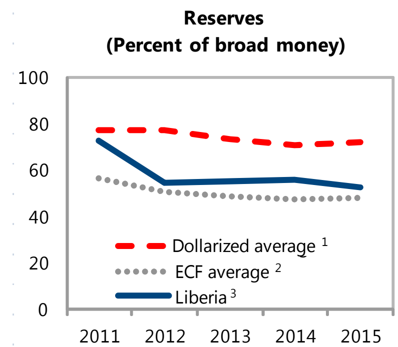
Sources: Liberian authorities and IMF staff estimates and projections.

Box 3. Liberia: Reserve Adequacy

International reserves are an important source of self-insurance against external shocks. Liberia is vulnerable to a variety of exogenous shocks stemming from sharp swings in terms of trade, weakly diversified exports, and reliance on international trade to import large quantities of essential goods. In addition, as a largely dollarized economy, reserves may also be needed to provide liquidity to the banking sector in the event of capital flight.

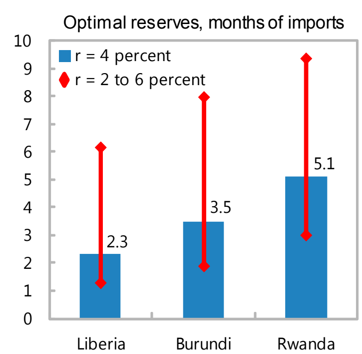


Commonly used metrics that focus on import cover, broad money, and model-based estimates provide some limited guidance on reserve adequacy. Theoretical and empirical analysis on determining the optimal or desired level of precautionary reserves is limited, particularly for dollarized economies. In Liberia, reserves remain below the traditional rule of three months of imports, even when UNMIL services and iron ore-related imports are taken into account. They are also low compared to other low-income dollarized countries, and other ECF arrangement countries in the region. Broad money is a less firmly based indicator in the literature, but can capture the risk of outflows by domestic residents and the potential need for bank support in or after a crisis. However, this vulnerability may be limited in Liberia because of the foreign ownership of banks and the non-systemic nature of the banking system. Using this measure, reserve coverage of broad money in Liberia is close to peer countries and above the 20 percent of broad money rule of thumb.



[1] Dollarized countries: Cambodia, Sao Tomé and Príncipe.
[2] ECF countries: Burundi, Mali, and Sierra Leone.
[3] Liberia estimates do not include ECF disbursements.

Model estimates that maximize the welfare benefits, subject to the cost of holding reserves, suggest optimal reserve holdings in Liberia in the range of one to six months of imports.[1] The benefit is measured by a decline in the probability and cost of a crisis, given country-specific fundamentals and shocks. However, the methodology is particularly sensitive to the assumption on the opportunity cost of holding reserves, which can range between two and six percent. Given the large investment needs in Liberia, the opportunity cost of holding reserves is assumed to be on the higher end of the estimates. On balance, this suggests that three months of imports is adequate reserve coverage in the medium term and would align Liberia with peer countries.



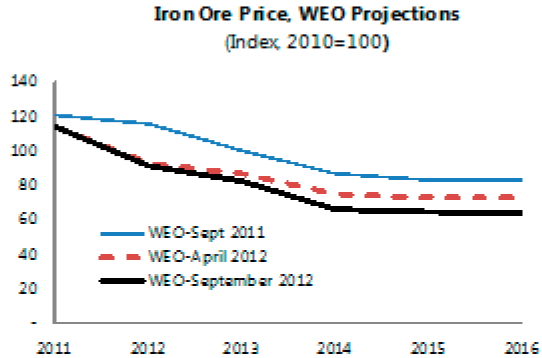
Source: IMF staff estimates.

[1] Based on the metric proposed in the recent Board paper on Assessing Reserve Adequacy, 2011.

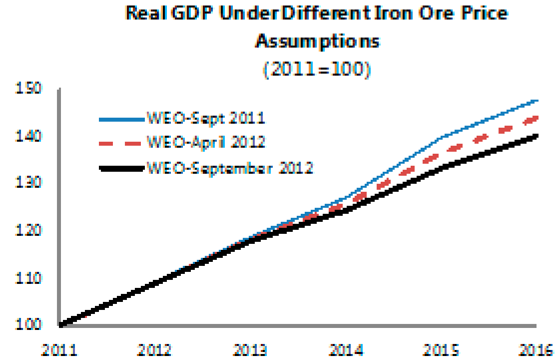
11. **Liberia's main risks are a protracted slow growing global economy and adverse movements in terms of trade (Table 7)**. Sluggish global demand for commodity exports—especially iron ore—poses risks to Liberian exports and may delay FDI, with negative impacts on the economy, the current account, and the fiscal balance (Figure 6). Downside risks come from weak public investment absorptive capacity. While Liberia will continue to fully pass through increases in fuel prices and maintain reduced import tariffs to mitigate high food prices, coping with further adverse external price movements could pose a challenge. In particular, Liberia is vulnerable to further increases in the import price of rice—the staple food in Liberia—although rice prices have so far not moved significantly in world markets. The authorities noted that importers are encouraged to hold six months of rice in the country, although the monitoring system relies on self-reporting by private agents. In an exogenous shock, the authorities would seek additional rice grants from donors. They are also evaluating existing interventions, including the school feeding program, and assessing new options to protect the most vulnerable while minimizing potential fiscal costs. On the upside, a pickup in iron ore and forestry production, positive developments in petroleum exploration, and high-return public investments present significant opportunities.

Figure 6. Liberia: Sensitivity to Iron Ore Prices

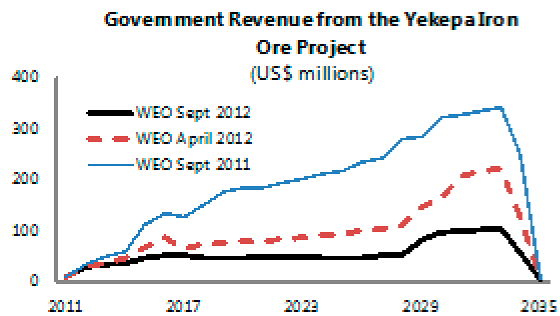
A deterioration in the outlook for iron ore prices, all else constant, transmits to Liberia's economy through...



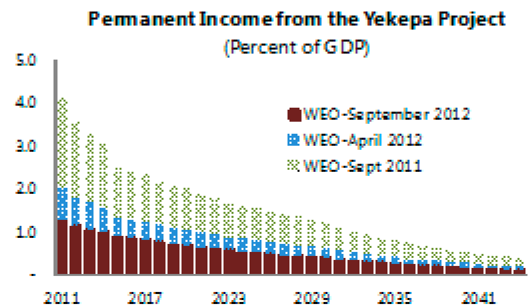
slowing down growth,



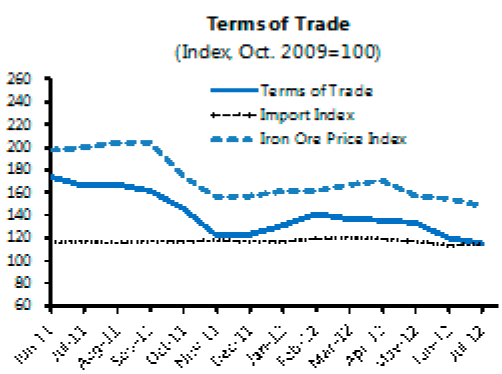
lowering iron ore revenue projections,...



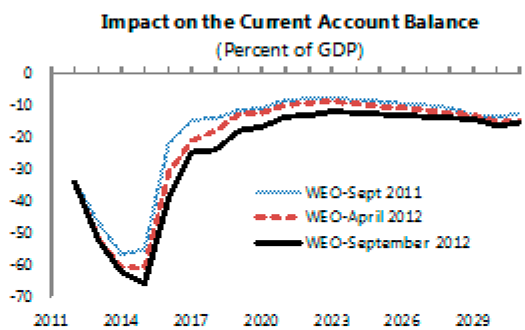
reducing the permanent income from iron ore,...



causing deterioration in terms of trade...



and widening projected current account deficits.



Sources: IMF staff estimates and World Economic Outlook.

12. **The authorities agreed to build reserves to three months of imports**. They agreed with staff's assessment that this level of import coverage strikes a balance between building buffers to contain external risks and limiting the high opportunity cost of accumulating reserves given the high yield on public investment considering the massive infrastructure gaps. This level of reserves also leaves a margin for foreign exchange market intervention to address excess exchange rate volatility. Over the longer term, reserves accumulation beyond three months may be desireable, because the opportunity costs of holding reserves declines once the large investments are completed, and reserves will build confidence in the financial system as the economy continues to monetize.

MEFP ¶ 32

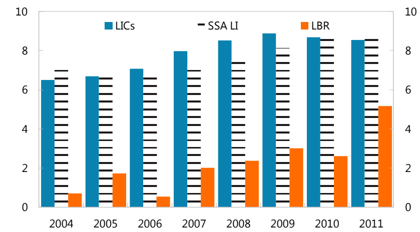
Authorities' views

13. **The authorities broadly agreed with staff's views on the economic outlook, although they are targeting stronger growth over the longer term**. PRS2 calls for growth of about 8½ percent a year over the longer term to achieve middle-income status by 2030. Achieving and maintaining this high growth rate, however, is challenging and will require fully securing the estimated $3 billion in financing needed to implement PRS2—some $2 billion above the baseline projections—including a substantial crowding-in of the private sector. Staff and the authorities discussed policies needed to remove bottlenecks to achieving higher growth, including improvements in competitiveness, diversification of the economy, especially agriculture, and execution of public investment projects.[12] Staff analysis found improved efficiency of public investments can have a significant impact on growth (Box 4).

[12] Legal, institutional and managerial bottlenecks hamper selection and implementation of public investment projects. These bottlenecks include weaknesses in prioritizing high-return projects, conducting feasibility and pre-feasibility studies, monitoring the project investment cycle, and coordinating efforts of the Ministry of Finance (MoF) and implementing ministries. Project execution could also benefit from broadening the list of construction companies to include non-resident firms and pre-qualifying them; limiting the number of projects allocated to a single contractor; and pooling similar small projects.

Box 4. Liberia: Macroeconomic Impact of Scaling Up Public Investment

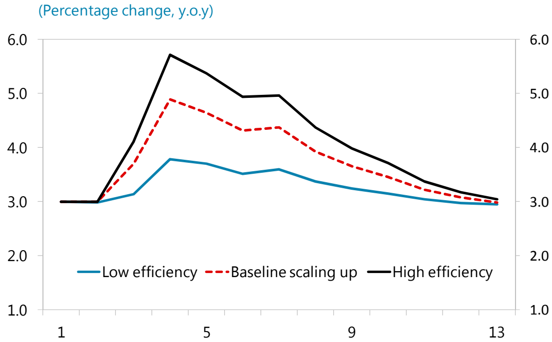
Public Investment Across Countries
(Percent of GDP)



Source: WEO database and IMF staff calculations.

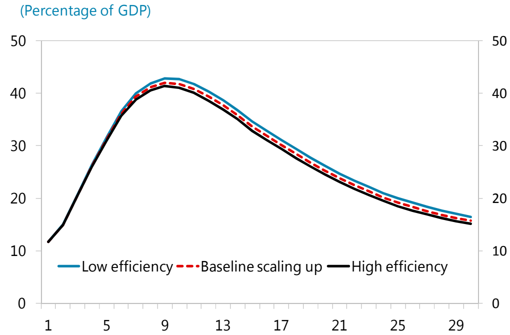
Liberia can achieve significant growth dividends from scaling up public investment and improving efficiency of capital spending. Public investment has been low in Liberia—about 3 percent of GDP on average in recent years—and below that of other low-income countries. Liberia also has a weak track record of project implementation—historically around 50 to 60 percent of budgeted capital expenditure is executed. A dynamic economic model, calibrated to Liberia specifics, was used to estimate the economic return from higher public investment relative to steady-state trend growth, as well as the impact of improving project efficiency.[1] Starting from Liberia's low base, an average increase of 5 percentage points of GDP a year in investment in seven years contributes to an approximately 1 percentage point increase in the annual growth rate of real per capita income on average over ten years. The growth effect peaks 3 to 4 years after the initial investment and then gradually declines over time returning to trend growth of 3 percent in per capita terms. The estimate assumes an efficiency rate of public investment of around 60 percent.[2] Assuming an improvement in the efficiency rate to 80 percent, consistent with improved project selection and strengthened execution capacity, real per capita income growth could potentially increase by an additional half percentage point over the medium term. On the other hand, the same amount of investment with a lower efficiency rate of 20 percent would result in lower growth over the longer term. Getting to higher growth faster, in turn, improves Liberia's debt dynamics. This shows the critical need for stepped-up efforts to tackle bottlenecks to project implementation. The exercise, however, has some caveats, and the estimates should be seen as an approximation rather than as a forecast.

Liberia: Real Per Capita Income Growth
(Percentage change, y.o.y)



Source: IMF staff calculations.

Liberia: Public Debt Under Different Growth Scenarios
(Percentage of GDP)



Source: IMF staff calculations.

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[1] EBS/12/139, Supplement 1.

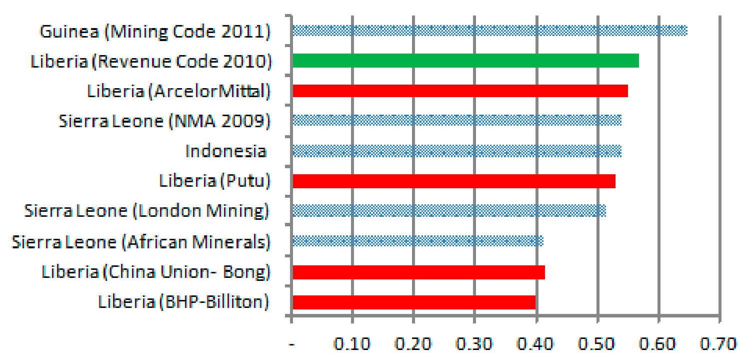
[2] The average for low-income countries. The efficiency rate measures the rate at which executed public investment translates into productive capital. For more details see Buffie, E. , A. Berg, C. Patillo, R. Portillo, and L. Zanna, 2012, "Public Investment, Growth, and Debt Sustainability: Putting Together the Pieces." IMF Working Paper No. 12/144.

B. Challenges: Managing Liberia's Natural Resource Wealth

14. **Over the longer term, proper management of revenue from natural resources will be important to support the development agenda**.[13] While iron ore-related revenue—estimated at around 1.1 percent of GDP or 4 percent of government revenue in 2012—is not expected to have a significant fiscal or macroeconomic impact in the near term, it is projected to rise over the medium term as more concessions begin production.[14] There is also potential for one-off windfalls related to petroleum exploration. Considering the potential for strong mining revenue, staff encouraged the authorities to step up efforts to establish a fiscal framework for managing this windfall, including measures to (i) build buffers to cope with export price volatility; (ii) smooth spending and avoid boom-bust cycles; and (iii) channel resources toward high-return public investment and other priority spending aligned with the PRS2.

15. **Liberia has an adequate tax code for taxing the mining sector, but concession agreements have ad hoc terms**. Staff estimates of the impact of comparative fiscal terms on the only currently producing iron ore mine show that the revised Liberia Revenue Code (LRC) yields returns comparable to international standards, but tax breaks in existing iron ore concessions have limited potential fiscal returns. If these concessions come up for renegotiation, the authorities should aim to harmonize the terms with the LRC and avoid tax breaks. Moreover, the authorities need to improve monitoring of production and financial statements of concessions to ensure that income tax payments fully reflect operations.

Effective Tax Return Under Comparative Fiscal Terms (Average effective tax return)[1]



[1] Different fiscal regimes and iron ore concession agreements applied to the Liberian Yekepa iron ore project operated by ArcelorMittal. Discount rate = 0 ; iron ore $DMT FOB price converges to $46 constant 2012 dollars.
Source: IMF staff estimates.

16. **Concession agreements are transparent, but further actions are needed to improve governance**. Liberia complies with the Extractive Industries Transparency Initiative (EITI); however, transparency and governance can still be improved in the petroleum sector. The

[13] EBS/12/139, Supplement 1.

[14] Three major iron ore concessions are yet to commence production. By 2015, iron ore is projected to account for around 15 percent of GDP, exceeding all other commodity exports (rubber, palm oil, timber, other metals) combined. Outside of iron ore, palm oil and forestry have significant potential to boost exports, revenue, and growth although land disputes and capacity constraints are slowing implementation.

authorities need to put in place governance structures that would delineate the responsibilities of regulation, oversight, and profit sharing in the petroleum sector, which are all currently held by the National Oil Company of Liberia (NOCAL). The authorities agreed with the staff's assessment and are planning to revise the Petroleum Act by mid-2013 to improve governance in the sector. They will also update the fiscal regime to international best practices and have requested IMF technical assistance.

17. **Some key concessions sectors have limited interaction with the non-concession economy owing to the scarcity of skilled domestic labor**. Rubber is the only concession sector so far employing domestic labor on a significant scale. Improving education and training and setting up local supply chains to serve the concessions may help make mineral sector growth more broad based and inclusive. Activity in the palm oil sector has been bogged down by sociopolitical challenges stemming from land disputes in the concession areas, but the sector carries high potential for job creation because of labor-intensive production.

C. Boosting Competitiveness and Growth

18. **Continued strong reforms are needed to improve Liberia's competitiveness and the business environment**. Given the high dollarization of the Liberian economy, the authorities broadly agreed that public investment and structural reforms are needed to improve cost competitiveness. The business climate remains constrained by continued high operating costs, particularly related to energy and transportation, as well as weak administrative capacity, a complicated and costly regulatory environment, uncertain property rights, and limited access to domestic finance (Box 5 and Figure 7). Ongoing regional integration within the Economic Community of West African States (ECOWAS)[15] and World Trade Organization (WTO) accession[16] will help to reduce barriers to trade and improve competitiveness.

[15] Benin, Burkina Faso, Cape Verde, Cote d'Ivoire, The Gambia, Ghana, Guinea (suspended), Guinea-Bissau, Liberia, Mali, Niger (suspended), Nigeria, Senegal, Sierra Leone, and Togo. Liberia's adoption of the regional Common External Tariff (CET) remains stalled because of concerns from regional partners on compensatory measures to cushion potential revenue losses.

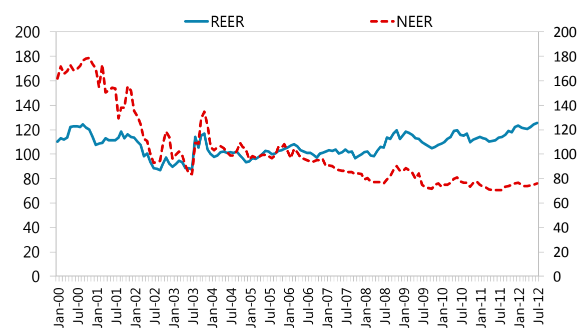
[16] Liberia requested membership in the WTO in 2007 and attended the first Working Party on WTO Accession in July 2012. The authorities are seeking to achieve membership in five years and are pressing ahead on reforms, particularly to reduce non-tariff barriers.

Box 5. Assessing External Stability and Competitiveness in Liberia

Liberia's external sector remains stable, with current account developments dominated by the activities in the concessions sector and aid flows. While the current account deficit is expected to widen significantly over the next three years from capital imports related to the iron ore sector, the expected acceleration of iron ore production and exports from 2015 will contribute to a narrowing in the current account deficit over the longer term. Iron ore production will also support a diversification of exports. (By 2015, iron ore exports are expected to rise to more than 60 percent of total exports, replacing rubber as the main export). Although this may help to offset idiosyncratic shocks in the rubber sector, commodity prices tend to move together such that the export sector is still vulnerable to falls in commodity prices. Moreover, if discovered, there is a potential for commercially viable oil which could have a significant impact on exports. Nonetheless, the current account deficit remains high as a share of GDP over the long term, especially given Liberia's heavy dependence on imports to cover basic goods; and there is need for ongoing adjustment, especially to boost and diversify exports.

The real effective exchange rate has appreciated close to 25 percent since mid-2008 reflecting higher domestic inflation, particularly food and fuel prices.[1] Given the high degree of dollarization in the economy, the authorities broadly agreed with the assessment that sustained policy measures are needed to improve cost competitiveness.

Liberia: Nominal and Real Effective Exchange Rates
(Index, 2002 =100 percent)

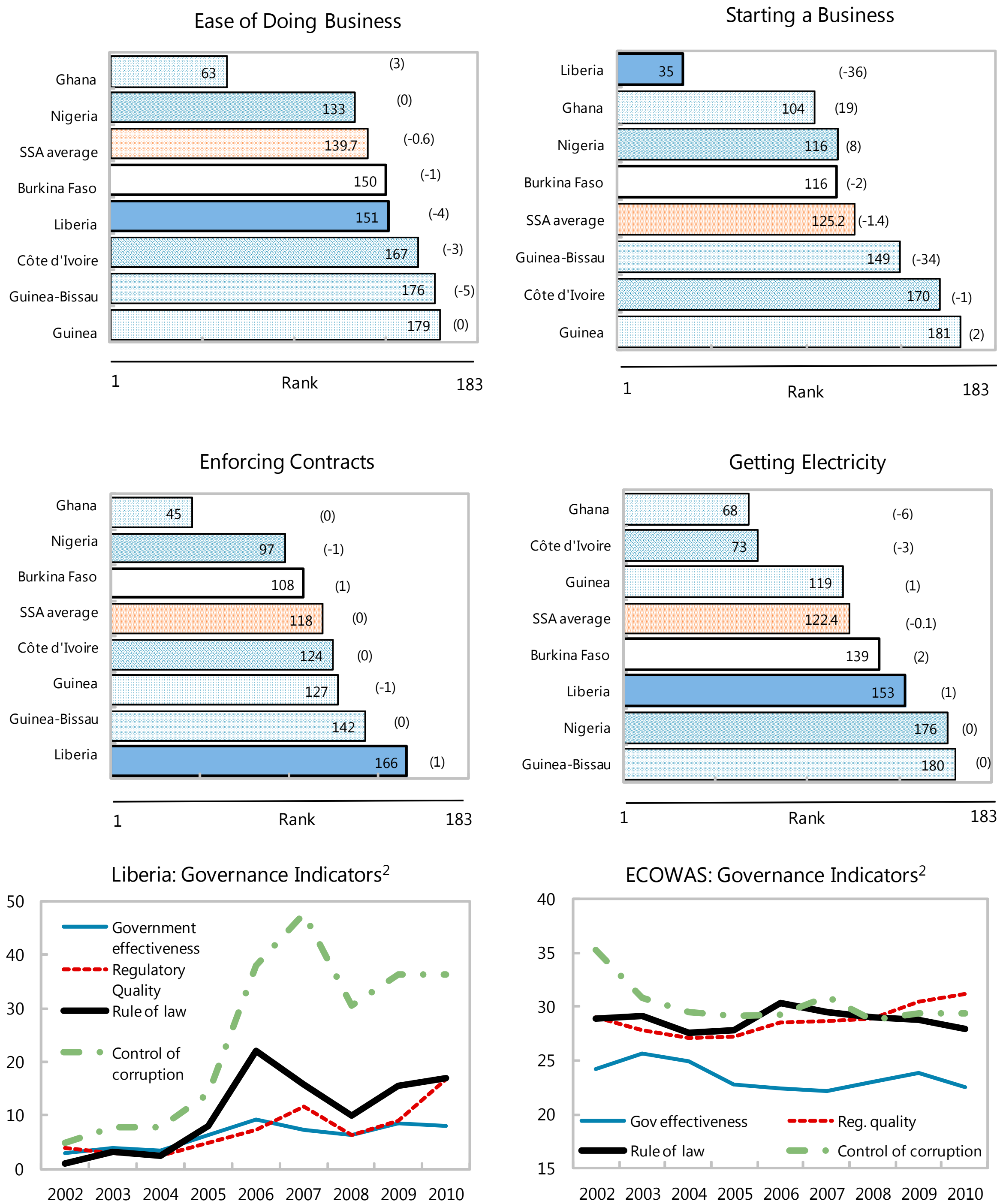


Sources: Central Bank of Liberia and IMF staff calculations.

Structural bottlenecks are a key element holding back Liberia's competitiveness. Liberia's overall rank in the World Bank's Doing Business Indicators improved four places in 2012, but growth remains constrained by continued high operating costs of energy and transportation. Electricity costs are the highest in sub-Saharan Africa because of reliance on batteries and generators, while access to electricity is one of the lowest in the world at close to zero compared with an average of 28.5 percent for sub-Saharan Africa. Sustained measures are also needed to streamline the complicated and costly regulatory environment, harmonize government business inspections, streamline payment of taxes, improve enforcement of contracts, and improve access to finance.

[1] Real exchange rate assessment in Liberia is limited by serious data limitations. Further, given the high degree of dollarization, any real exchange rate overvaluation would need to be addressed by increasing productivity and reducing domestic costs.

Figure 7. Liberia: 2012 Business Climate—A Cross Country Comparison [1]



Sources: World Bank, *Doing Business* database and *Governance Indicators* database.

[1] The numbers in parentheses show the change between the 2012 and 2011 rankings.

[2] An increase signals an improvement.

THE PILLARS OF AN ECF-SUPPORTED PROGRAM

A. Three Key Pillars

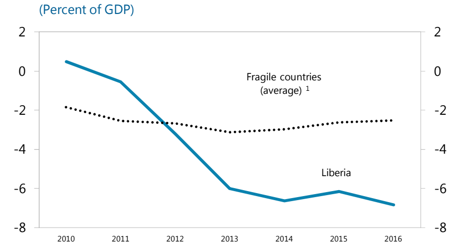
19. **The proposed ECF arrangement would support the authorities' program to accelerate broad-based growth and poverty reduction, aligned with their PRS2, while maintaining macroeconomic stability**. Consistent with these objectives, discussions centered on three key pillars

- Creating fiscal space for higher capital spending by containing personnel costs and other current transfers;
- Strengthening the financial sector through reducing vulnerabilities and improving access to credit; and
- Underpinning growth with structural reforms to further improve public financial management, governance, and the business environment.

B. Creating Fiscal Space for Scaling Up Investment

20. **The government's medium-term fiscal policy plans (i) a widening of the fiscal deficit (including grants) to about 6 percent of GDP—larger than the average for fragile countries—to accommodate higher capital spending aligned with the PRS2; (ii) reallocating spending toward priority sectors; and (iii) improving public financial management and execution of public investment projects**. The fiscal deficit increases by nearly 3 percent of GDP in 2012/13 to accommodate a 4 percent of GDP increase in capital spending—a near doubling from FY 2011/12 (Figure 8).[17] Current spending is projected to decline 1 percent of GDP, mainly from lower personnel costs, cuts goods and services, and reductions in transfers to state-owned enterprises (SOEs) (including election-related transfers). Tax revenue as a share of GDP—which is already high compared to the region—is expected to remain broadly unchanged. Planned measures to broaden the tax base for services (notably for inbound telephone calls) and actions to strengthen the large taxpayers unit are expected to help make up for recent one-off tax payments—including windfall withholding taxes in FY 2011/12. Fiscal policy continues to be anchored by debt management, which allows for an increase in

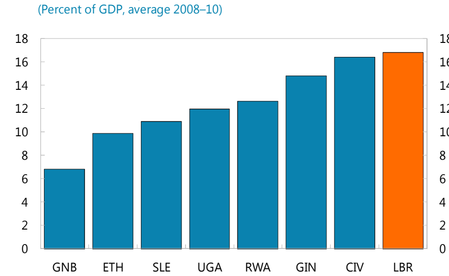
Liberia: Overall Fiscal Balance Including Grants, 2010–16
(Percent of GDP)



Source: WEO, country database.

1 Fragile countries include Burundi, Comoros, Côte d'Ivoire, Guinea, Liberia, Sierra Leone, The Gambia, Togo, Zimbabwe,.

Cross-Country Public Tax Revenue Comparisson
(Percent of GDP, average 2008–10)



Sources: World Economic Outlook and IMF staff calculations.

[17] The FY 2012/13 budget law was signed into law in August 2012 and is consistent with the ECF-supported fiscal program.

external borrowing to accommodate higher capital spending while maintaining debt sustainability and avoiding domestic arrears.[18]

Liberia: Central Government's Medium-Term Fiscal Framework, FY 2011–15
(Percent of GDP)

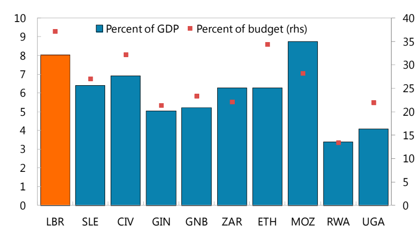
	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
	Prel.	Prel.	Proj.	Proj.	Proj.
Total revenue and grants	26.4	27.8	27.3	28.8	27.6
Total revenue	23.6	26.1	24.9	26.5	25.8
Tax revenue	18.98	21.6	19.7	19.2	19.2
Non-tax revenue	4.6	4.6	5.2	7.3	6.6
Grants	2.8	1.7	2.4	2.3	1.8
Total expenditure	27.0	31.0	33.3	35.4	33.8
Current	21.8	27.0	25.6	24.4	23.1
Of which: one-off PSIP current spending	….	….	2.9	1.9	1.4
Salaries and wages	9.8	11.3	11.0	10.8	10.2
Capital	5.2	4.1	7.8	11.0	10.7
Overall balance (including grants)	-0.6	-3.2	-6.0	-6.6	-6.2
Overall balance (excluding grants)	-3.4	-4.9	-8.4	-9.0	-8.0
Net financing	0.6	3.2	6.0	6.6	6.2
Foreign	0.3	0.9	5.5	6.7	6.4
Domestic	0.3	2.3	0.5	0.0	-0.2

Sources: Ministry of Finance and IMF staff estimates.

21. **The authorities agreed on the importance of streamlining current spending—particularly the wage bill—and reallocating savings toward capital outlays**. Liberia's wage bill, which is among the highest in the region both as a percentage of GDP and of total spending, is expected to decline by about 1 percent of GDP over the medium term. The FY 2012/13 wage policy thus has no salary increases and minimal net new hires. The authorities are working to clean up the payroll by eliminating ghost workers and duplicates—with an estimated savings of 1.5 percent of GDP. Staff urged the authorities to use such savings and any other unspent current allocations to pay for capital spending, particularly given uncertainties surrounding the timing of external financing. However, given political constraints, the authorities indicated that, if realized, the savings will be allocated to increase salaries for all public servants. The authorities also introduced fiscal rules—starting in the FY 2012/13 budget—that limit the share of the budget allocated to personnel costs (to no more than 34 percent of the budget) and limit transfers of unspent investment allocations to recurrent spending. Staff recommended more ambitious rules, in particular, by bringing personnel costs to around 31 percent of the budget and reducing transfers from capital to current spending to zero. The authorities plan to assess savings during the first half of the 2012/13 fiscal year to tighten the rules in subsequent budgets. Staff indicated that additional savings could also be achieved during the current fiscal year by reducing discretionary spending on food, travel, transportation, communications, and other special allowances.

MEFP ¶s 12-13

Cross-country Public Sector Wage Bill Comparisson
(Percent of GDP and percent of total spending, average 2008-10)



Sources: World Economic Outlook and IMF staff calculations.

[18] There are no new domestic arrears beyond those settled in 2008.

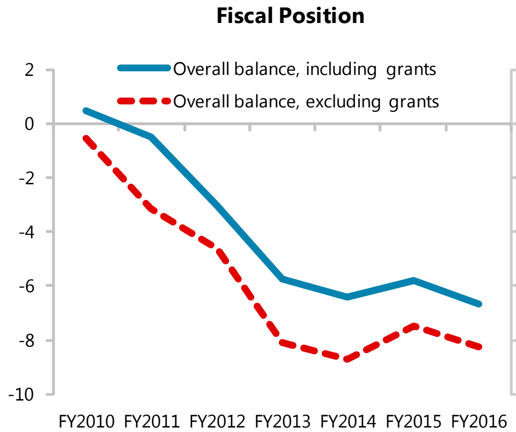
MEFP ¶18

22. **The medium-term fiscal deficit is expected to be financed mainly from foreign loans, but includes some limited domestic financing in FY 2012/13**. The authorities pushed for flexibility to use central bank reserves as bridge financing for their large strategic investments, in advance of loan disbursements that are under negotiation. The mission emphasized the need to maintain reserves at comfortable levels to mitigate external vulnerabilities and the authorities agreed to advance the planned issuance of LD treasury bills—now set for end-2012—to help to cover their financing needs from the highly liquid domestic market, and abstain from direct financing from the central bank.

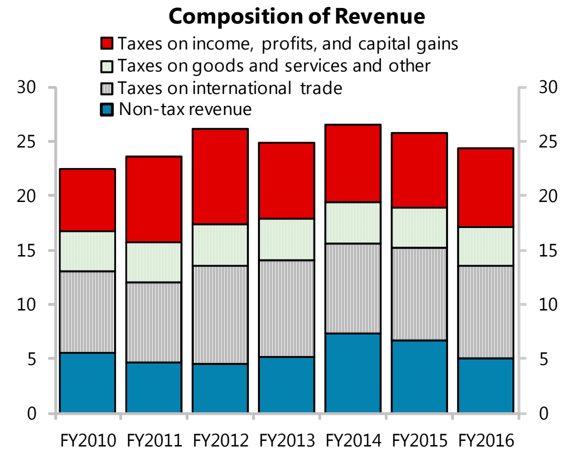
Figure 8. Liberia: Fiscal Medium-Term Outlook, FY2010–16

(Percent of GDP)

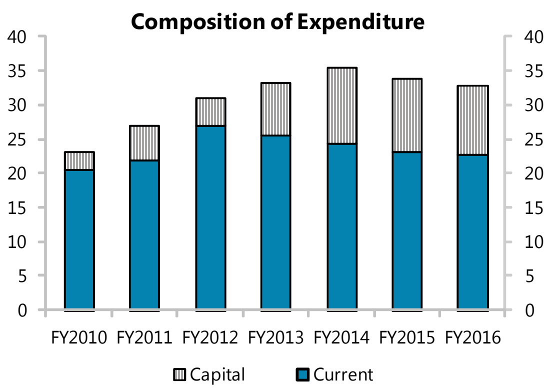
The fiscal balance is expected to widen, reflecting the scaling up of capital spending...



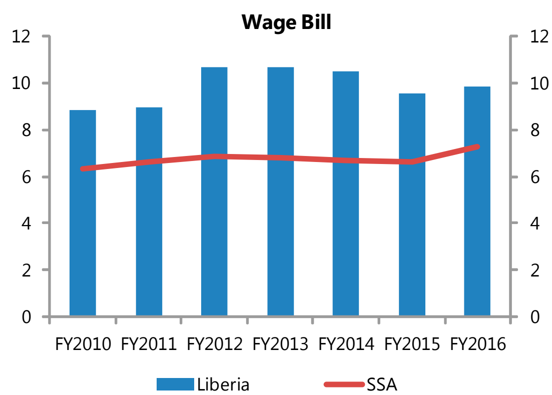
...while revenue remains stable over the medium term.



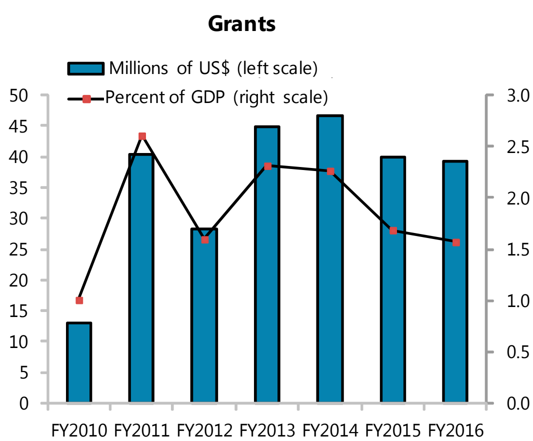
Current spending is expected to moderate to create fiscal space for capital spending...



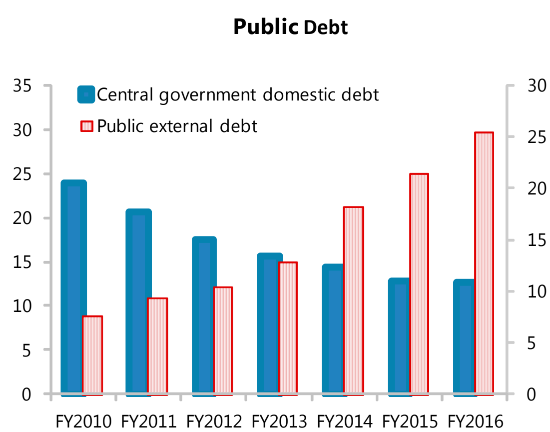
...while the wage bill declines, albeit still high by regional standards.



Budget support grants remain at stable levels.



Public external debt will remain manageable.



Sources: Liberian authorities and IMF staff estimates and projections.

C. Improving Monetary Policy and Deepening the Financial Sector

23. **In the dollarized economy, monetary policy will continue to play a limited role focused on containing Liberian dollar-denominated inflation through the exchange rate**. Liberian dollars remain important to the vulnerable poor, and any sudden depreciation can have a severe impact on their purchasing power and welfare. Thus, monetary policy will continue to aim at containing excessive volatility in the exchange rate while aiming for a modest increase in the foreign exchange position.

MEFP ¶31

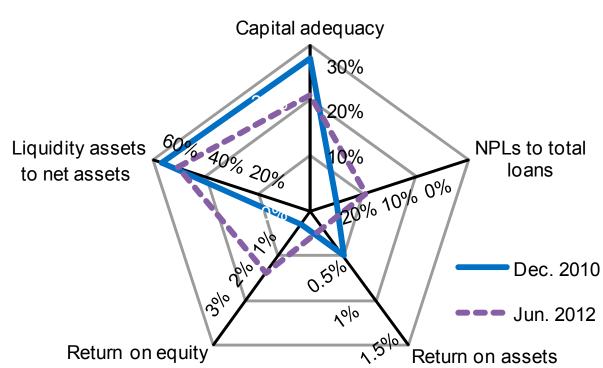
24. **The absence of an anchor for monetary policy, however, remains a challenge**. There is no target or band for exchange rate policy or monetary interventions to anchor market expectations on Liberian dollar inflation. At the same time, given the already high reserve requirement (22 percent), the CBL's monetary tool to mop up excess liquidity is limited to the weekly foreign exchange auctions, but the use of this instrument is limited by reserve accumulation objectives. While the planned launch of the local currency treasury bill market will add a new liquidity management instrument, the authorities did not concur that an announced monetary target would anchor expectations given the volatility in the shallow foreign exchange market. They also see a need to maintain policy flexibility in addressing liquidity demands and external shocks. The CBL will continue to improve its liquidity forecasting to strengthen policy effectiveness though capacity constraints remain an obstacle. Staff reiterated the need for improved collaboration and information sharing between the CBL and the Ministry of Finance (MoF).

25. **The authorities expressed commitment to de-dollarization and plan to take steps to strengthen demand for the LD**. These include improving the quality and increasing the denomination of LD notes and de-dollarizing civil servant wages and tax payments. The issuance of LD denominated treasury bills should also help absorb excess Liberian dollar liquidity while increasing incentives for banks to hold Liberian dollar deposits. Staff emphasized that strengthening the monetary framework including through establishing a transparent anchor will help support confidence in the LD and potentially de-dollarization. The authorities agreed that policies to strengthen the demand for the Liberian dollar should be market based and serve to enhance the credibility of economic policy and develop the financial market.

MEFP ¶32

26. **Overall, the banking system remains capitalized and liquid, but risks are elevated stemming from high non-performing loans and low profitability**. System-wide capitalization remains high though it has been eroded by the stock of bad loans with a few banks falling below capital requirements. The CBL is working with the affected banks on their recapitalization plans to ensure full

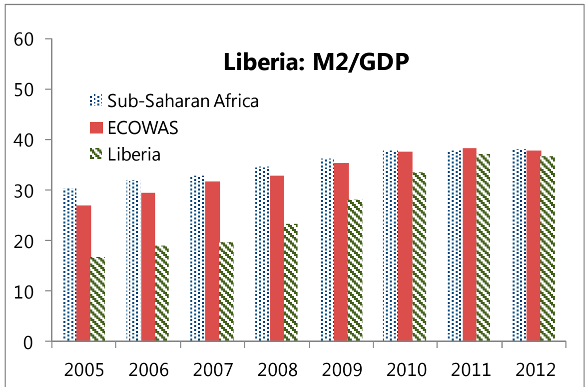
Liberia: Barometer of Financial Soundness



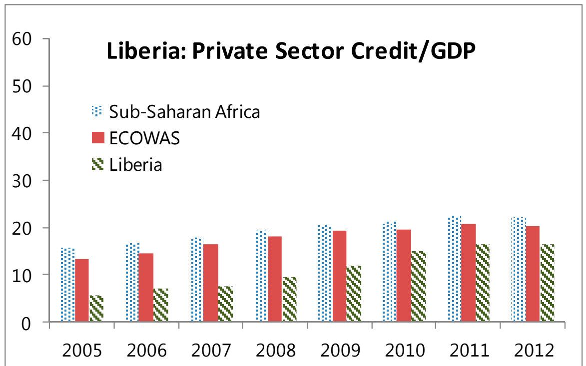
Source: Central Bank of Liberia.

compliance with regulatory requirements by end-2012. The authorities introduced a commercial court in 2012 to improve asset recovery from defaulting borrowers, but loans predating the court are outside of the court's purview; and it is not a court of final appeals, which limits its effectiveness. Moreover, the CBL's roll out of risk-based supervision—which is now in its second round of bank inspections—is progressing and plans to allow greater adaptability to the multitude of risks and vulnerabilities in the system.

27. **Deepening the financial sector remains a high priority**. Despite rapid monetization and growth in private sector credit, access to credit remains weak and limited to a few borrowers. Small- and medium-size enterprises (SMEs)—and rural borrowers in particular—have difficulties accessing credit. Banks are reluctant to extend credit to the sector given weaknesses in the legal and judicial framework, weak property rights, limited collateral and credit reference systems, and weak capacity of commercial banks to appraise SMEs and rural farmers. Moreover, interest rate rigidity and the short maturities of bank liabilities and credit impede lending to productive sectors (Box 6). To improve access to credit, especially for small borrowers, the CBL is strengthening the commercial court, expanding the credit reference system, and establishing a collateral registry.



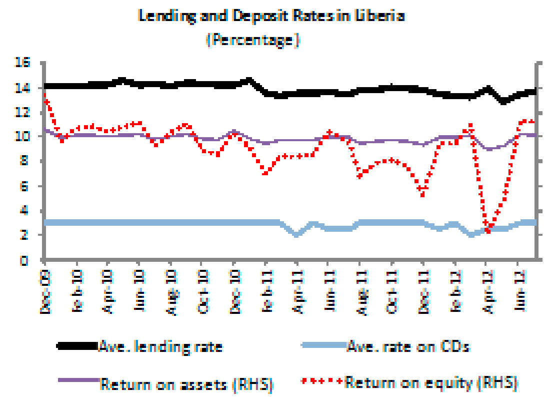
Source: IMF staff estimates.



Source: IMF staff estimates.

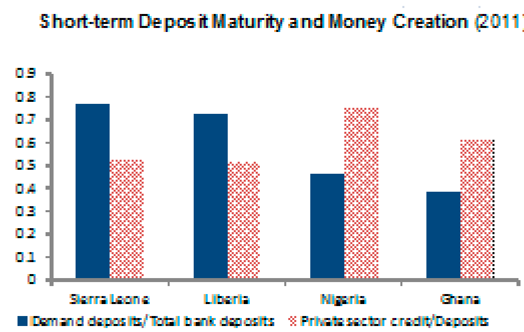
Box 6. Liberia: Interest Rate Rigidities and Short-Maturity of Deposits and Credit

Despite poor bank returns, lending and deposit rates have remained rigid. CBL moral suasion, absence of a money market, and banks' capacity constraints in analyzing market liquidity and credit demand all serve to contain lending rates.[1] The low net interest margins by regional comparison lead banks to rely on non-interest income, which accounts for nearly 60 percent of revenue.



Source: Central Bank of Liberia.

Long-term financing sources are scarce. The supply of time and savings deposits to meet the high demand for long-term financing from sectors such as agriculture, construction, and manufacturing is limited in the current term structure. Most commercial bank deposits are demand deposits, and most of the loans are short-term or overdrafts.



Sources: IMF staff and national authorities.

The authorities are using ad hoc methods to boost credit to small borrowers. The CBL has undertaken a few initiatives to stimulate long-term lending to SMEs and agriculture by placing long-term U.S. dollar deposits at commercial banks. This approach carries potential reputational risks to the CBL while exposing their balance sheet to possible credit risk should they be pressured to share losses.

[1] EBS/12/59, Appendix II; and EBS/12/139, Supplement 1.

D. Attaching Priority to Improving Governance and Transparency

MEFP ¶20-30

28. **Improving governance and transparency also remains a high priority**. The authorities will draw on a recently completed Public Expenditure and Financial Assessment (PEFA) to further improve public financial management (PFM) (Box 7). Staff urged the authorities to step up efforts to strengthen financial oversight and reporting of SOEs—an outstanding issue from the last ECF arrangement—and further roll out the Integrated Financial Management Information System (IFMIS) especially to include the civil service payroll; strengthen government cash management; streamline procurement procedures and improve project execution; and establish a natural resource

revenue unit in the MoF to improve monitoring of concessions. The authorities are also advancing reforms to strengthen debt and aid management capacity, especially proper recording and monitoring of all public debt, including off-budget financing. The authorities' anti-corruption strategy is also advancing through enforcement of a recently introduced Code of Conduct for public sector employees.

29. **Financial structural reforms to alleviate risks and streamline regulation and payments are also important**. The CBL plans to submit to the legislature a revised Insurance Act to streamline regulations in the sector and establish the central bank as the sole regulator. A national payments law—recently submitted to the legislature—and capacity building at the CBL should help improve bank settlements and reduce overhead for transactions.

Box 7. Liberia: Public Financial Management—Achievements and Challenges

The 2012 Public Expenditure and Financial Accountability (PEFA) assessment showed improvements in public financial management (PFM) but important challenges remain (21 out of 30 PEFA indicators were rated C or lower). The main challenges are

- Comprehensiveness and transparency of budget documents has improved slightly; but financial reporting remains below standard, and timely publication is lacking. State-owned enterprise (SOE) reporting is incomplete and reports on externally financed projects are not available.
- Policy-based budgeting has improved and is aligned with the 2009 PFM Act. Nonetheless, the budget is not approved on time which limits cash planning, procurement, and budget execution.
- Predictability and controls in the budget execution have improved; but payroll controls and cash planning remain weak.
- Budget credibility remains to be fully established. Although arrears have been controlled and fiscal stability maintained, credibility in revenue and expenditure estimates is weak.
- External audit remains weak. Despite the significant efforts to strengthen the General Audit Commission, none of its audits has lead to remedial actions.
- Bringing donor support on-budget has not advanced.

E. Maintaining Debt Sustainability and Strengthening Management Capacity

MEFP ¶36-41

30. **Liberia continues to have a low risk of debt distress—as confirmed by the debt sustainability analysis (DSA)** (EBS/12/139, Supplement 3). Staff and the authorities agreed to raise the foreign currency borrowing ceiling (including concessional and nonconcessional borrowing) to 4 percent of GDP in net present value (NPV) terms on average in 2012–15, monitored by an indicative target.[19] The larger borrowing amount (equivalent to about $300–400 million depending on the level of concessionality) averaged over three years would provide increased flexibility to accommodate higher capital expenditure over the period—taking account of capacity constraints and "lumpy" investments—while maintaining low debt vulnerabilities. In the event that sufficient concessional financing cannot be secured, the government has expressed interest in commercial borrowing for some of their strategic high-yielding infrastructure projects, assessed by a credible third party. Staff urged the authorities to carefully assess their financing options and take advantage of

[19] The debt ceilings would include SOEs.

available grants and highly concessional financing to the maximum amount possible, but indicated that limited nonconcessional financing could be considered, if requested, tied to specific projects.

31. **HIPC Initiative debt restructuring negotiations are nearing completion, and discussions are advancing with development partners on new financing commitments**. Debt restructuring negotiations with the Saudi Fund and the Arab Development Bank have concluded; however discussions with Taiwan, Province of China, have not advanced, despite the authorities' efforts. To finance part of the rehabilitation of the hydroelectric plant, the authorities are discussing concessional loans with bilateral and multilateral partners.

MEFP ¶38

F. Improving the Quality of Statistics for Economic Management

32. **Improving national account statistics remains a priority**. National account data is very weak with real GDP being benchmarked to 1992 owing to shortcomings in data for later years. The authorities recently conducted an establishment survey (covering all registered business enterprises) to help compile new national accounts. A household income and expenditure survey (HIES) is being planned for 2013, but is yet to secure sufficient financing. Staff urged the authorities to mobilize resources for the HIES and to seek donor financing. Better national account estimates may help in the compilation of balance of payments statistics, which also need improvement.

MEFP ¶45

ACCESS, PROGRAM MONITORING, AND RISKS

33. **Access is proposed at 40 percent of quota (SDR 51.68 million) phased in seven equal disbursements (Table 8)**. This level of access would allow reserves to increase to three months of import coverage over the course of the program. Although the proposed access is lower than the norm for second-time ECF users (access varies widely between 40–120 percent of quota), it is aligned with comparable countries such as Sierra Leone (30 percent of quota), Mali (32 percent), and Burundi (39 percent). The arrangement could be augmented at a later date, if needed, to address external shocks.

34. **The program would monitor six quantitative performance criteria (PC), streamlined from the previous ECF arrangement (MEFP Table 1)**. Proposed structural benchmarks for the first year of the ECF arrangement—which include the measures pending from the last ECF arrangement—are geared toward further enhancing budget control and monitoring, improving execution of capital spending, controlling payroll growth, and further developing the financial sector (MEFP Table 2).

35. **Liberia's capacity to repay the IMF is strong (Table 9)**. Projected debt financing to the Fund is low as a share of GDP, exports, and government revenue. Public external debt will remain well below thresholds of debt distress over the medium term. Liberia's IMF credit outstanding

will peak at 68 percent of quota, far below the norm for ECF countries. The ECF arrangement is expected to be fully financed (Table 10). The mission followed up on outstanding recommendations of the 2011 safeguards assessment update, and a draft Memorandum of Understanding (MOU) between the CBL and the MoF on repayment of the IMF's credit will be finalized by end-2012.

36. **Although the authorities are firmly committed to reform, considerable risks exist**. The government faces substantial political pressure to reduce poverty and accelerate public investments—areas where progress was slow in the past. Lack of policy coordination and weaknesses in technical capacity, institutions, and governance, however, will continue to test the government's ability to implement its ambitious development plans. Nonetheless, the government has demonstrated a solid track record of program implementation under the previous ECF arrangement and is benefiting from continued large-scale technical assistance, including from the IMF. Liberia also remains vulnerable to external shocks, particularly volatility in commodity prices, food and fuel price increases, and a prolonged global slowdown in growth.

STAFF APPRAISAL

37. **Liberia recorded strong macroeconomic gains under the recently completed three-year ECF Arrangement, but development challenges remain with large infrastructure gaps and poverty still at very high levels**. Economic activity has picked up, inflation has been contained, institutions have been partially rebuilt, and fiscal accounts have been consolidated, including restoration of debt sustainability. However, much more needs to be done to ensure that the benefits of rapid growth lead to job creation and poverty reduction.

38. **The economic outlook is favorable, but with challenges**. The most immediate challenge is to maintain the hard-won stabilization gains while creating fiscal space to boost spending on infrastructure and human development, promote financial sector deepening and access to credit, and create a favorable business climate to support broad-based growth and job creation.

39. **The budget for FY2012/13 is appropriately aligned to PRS2 and envisages scaling up public investment and investing in people and in institutions**. While execution of capital spending improved in FY 2012, the government's effectiveness in substantially increasing investment is still far from complete. Achieving higher investment levels is challenging and will require addressing capacity constraints including political, institutional, and technical skills. The planned measures to establish a Project Management Office are welcome.

40. **Scaling up infrastructure investment without jeopardizing hard-won macroeconomic stability requires efforts to expand revenue collection and contain current spending**. The recent measures to contain current spending are welcome, especially cleaning up the wage bill and introducing fiscal rules that limit the share of wages and salaries in total spending and the share of capital spending that could be transferred to current spending.

However, a stronger commitment is required to tighten the fiscal rules and ensure that savings in current spending are reallocated to capital expenditure. The authorities' plan to strengthen revenue collections by a combination of tax policy and administrative measures is welcome, but more needs to be done to increase revenue over the longer term. Strengthening administrative reforms is warranted to support growth and investment, and the recently completed PEFA is a clear road map to strengthen public financial management.

41. **The monetary framework remains very basic**. Significant scope remains to improve monetary policy implementation by anchoring the framework to a transparent target and introducing treasury bills to improve liquidity management.

42. **Over the longer term, proper management of revenue from natural resources will be crucial to support the development agenda and maintain macroeconomic stability**. While current natural resource revenue accounts for less than 10 percent of government revenue, it is expected to rise over the medium term as iron ore production picks up and the potential windfalls related to petroleum exploration materialize.

43. **Liberia has a low risk of debt distress, which, together with improved debt management skills, supports a higher external borrowing ceiling to accommodate the scaling up of public investment**. The DSA suggests there is room to accommodate higher borrowing—on concessional and possibly nonconcessional terms—without worsening the risk of debt distress. Any request for limited nonconcessional borrowing could be considered in future program discussions as long as it remains within the overall borrowing ceiling and is tied to specific projects that have been independently evaluated for high economic and social returns.

44. **The external payments position remains stable, but Liberia could benefit from building reserves to cover three months of imports**. Although the authorities' view is that reserves accumulation carries a high opportunity cost given the country's development financing needs, building reserves will support CBL's foreign exchange market intervention to address excess exchange rate volatility, and will be a buffer against domestic and external shocks. The authorities should avoid direct borrowing from the CBL—with the exception of short-term bridge delays in disbursement from external creditors—and rely on treasury bills to cover any domestic financing needs, as well as to develop the domestic financial market.

45. **Financial sector reform is advancing, but promotion of financial sector deepening and access to credit is needed to improve private sector development and boost economic growth**. The CBL is commended for introducing risk-based supervision. Given the high levels of non-performing loans and the low bank profitability, expanding access to financial services will require enhancing the collection and dissemination of credit information while strengthening supervision, including improving the credit reference system, establishing a collateral registry, and strengthening the asset recovery framework.

46. **Staff supports the authorities' request for a successor arrangement under the ECF**. The ECF arrangement will allow Liberia to maintain an adequate level of international reserves to cope with global market uncertainties, while bolstering donor support for public investment and social programs. Liberia remains a fragile state and risks remain to program implementation from ongoing capacity weaknesses. Nevertheless, the authorities' commitment to strong fiscal management and administrative reforms mitigate these risks.

47. **It is proposed that during the ECF arrangement Liberia stay on a 24-month Article IV cycle in accordance with the decision on consultation cycles**.[20]

[20] Decision No. 14747-(10/96) (9/28/2010).

Table 1. Liberia: Millennium Development Goals

	1990	1995	2000	2005	2010	SSA 2010	Goals 2015
Goal 1: Eradicate extreme poverty and hunger							
Employment to population ratio, 15+, total (%)	*57*	57	57	58	59	64	
Employment to population ratio, ages 15-24, total (%)	*34*	34	33	33	33	46	
Income share held by lowest 20%	..	..	..	*6*	..	..	
Malnutrition prevalence, weight for age (% of children under 5)	..	..	23	*20*	..	22	11.5
Poverty gap at $1.25 a day (PPP) (%)	..	..	..	*41*	..	21	
Poverty headcount ratio at $1.25 a day (PPP) (% of population)	..	..	..	*84*	..	48	
Vulnerable employment, total (% of total employment)	..	..	..	*80*	79	..	
Goal 2: Achieve universal primary education							
Literacy rate, youth female (% of females ages 15-24)	..	*54*	..	*73*	*81*	*69*	100
Literacy rate, youth male (% of males ages 15-24)	..	*66*	..	*69*	*70*	*77*	100
Primary completion rate, total (% of relevant age group)	..	..	..	*69*	*62*	*70*	100
Total enrollment, primary (% net)	..	..	*46*	..	..	*76*	100
Goal 3: Promote gender equality and empower women							
Ratio of female to male primary enrollment (%)	..	..	74	*92*	*91*	*93*	100
Ratio of female to male secondary enrollment (%)	..	..	73	..	..	*82*	100
Ratio of female to male tertiary enrollment (%)	..	..	55	..	..	*63*	100
Goal 4: Reduce child mortality by two-thirds							
Immunization, measles (% of children ages 12-23 months)	..	..	63	63	64	75	
Mortality rate, infant (per 1,000 live births)	161	146	112	83	61	71	107
Mortality rate, under-5 (per 1,000 live births)	241	219	164	117	83	113	161
Goal 5: Improve maternal health by three-fourths							
Adolescent fertility rate (births per 1,000 women ages 15-19)	..	*152*	149	144	131	108	
Births attended by skilled health staff (% of total)	..	..	51	*46*	..	46	
Contraceptive prevalence (% of women ages 15-49)	..	..	10	*11*	..	22	
Maternal mortality ratio (modeled estimate, per 100,000 live births)	1,200	1,900	1,300	1,100	770	500	900
Pregnant women receiving prenatal care (%)	..	..	84	*79*	..	73	
Goal 6: Combat HIV/AIDS, malaria, and other diseases by half							
Incidence of tuberculosis (per 100,000 people)	199	219	242	266	293	271	100
Prevalence of HIV, female (% ages 15-24)	..	..	..	..	*0.7*	4	0
Prevalence of HIV, male (% ages 15-24)	..	..	..	..	*0.3*	2	0
Prevalence of HIV, total (% of population ages 15-49)	0.3	3.1	3.3	2.2	*1.5*	6	0
Tuberculosis case detection rate (%, all forms)	*46*	30	22	40	56	60	23
Goal 7: Ensure environmental sustainability							
Forest area (% of land area)	51.2	..	48.1	46.5	44.9	28.0	
Improved sanitation facilities (% of population with access)	..	11	12	15	18	31.0	100
Improved water source (% of population with access)	..	58	61	67	73	61.0	100
Goal 8: Develop a global partnership for development							
Internet users (per 100 people)	0	*0*	0	*0*	2.3	10.0	
Mobile cellular subscriptions (per 100 people)	0	0	0	5	39	45	
Fertility rate, total (births per woman)	7	6	6	6	5	5	
Memorandum items:							
GNI per capita, Atlas method (current US$)	*280*	*120*	190	120	210	1,178	
GNI, Atlas method (current US$) (billions)	*0.6*	*0.3*	0.5	0.4	0.8	1,006	
Life expectancy at birth, total (years)	42	42	46	52	56	54	
Literacy rate, adult total (% of people ages 15 and above)	..	*43*	..	*54*	*59*	63	

Source: World Development Indicators.

Table 2. Liberia: Selected Economic and Financial Indicators, 2009–15

	2009	2010	2011	2012		2013	2014	2015
		Prel.	Prel.	8th Rev[1]	Proj.	Proj.	Proj.	Proj.
	(Annual percentage change, unless otherwise indicated)							
National account and prices								
GDP at constant prices	5.3	6.1	8.2	8.8	8.9	8.3	5.6	7.1
Real GDP excluding mining sector	5.3	5.8	5.8	3.1	3.8	6.1	6.8	7.3
GDP deflator (US dollars)	-1.7	5.4	10.6	2.9	5.0	1.1	1.0	7.2
Nominal GDP (millions of US dollars)	1,155.1	1,291.9	1,545.4	1,699.2	1,767.5	1,934.4	2,062.7	2,368.9
Consumer prices (average)	7.4	7.3	8.5	5.2	6.6	5.6	5.0	5.0
Consumer prices (end of period)	9.7	6.6	11.4	3.3	5.5	4.7	4.0	4.0
Consumer prices (US dollar denominated, year-on-year)	2.4	1.3	10.2	1.9	3.2	1.3	1.8	1.6
External sector								
Exports, f.o.b.	-39.7	40.4	77.0	25.9	23.8	14.3	8.5	65.5
Imports, f.o.b	-19.0	17.4	49.9	24.4	33.3	16.1	5.6	-5.0
Terms of trade (deterioration -)	-9.2	76.8	16.1	-7.9	-24.1	-2.5	-0.8	-10.3
Average exchange rate (local currency per U.S. dollar)	68.3	71.4	72.2	…	…	…	…	…
Average nominal effective exchange rate change (depreciation -)	-1.7	-3.7	-4.8	…	…	…	…	…
Average real effective exchange rate (depreciation -)	8.5	2.3	-1.1	…	…	…	…	…
Gross official reserves (months of imports) [2]	3.2	3.8	3.0	2.9	2.6	2.7	2.8	3.0
Gross official reserves (millions of U.S. dollars)	312.2	391.4	415.8	373.7	372.1	411.7	440.2	466.0
Money and credit								
Net foreign assets	1.4	149.8	11.9	-15.2	-20.2	0.0	-3.6	-3.8
Net domestic assets	5.7	-89.9	101.4	60.2	74.6	17.1	14.6	23.4
Net claims on central government	-0.2	-84.4	25.5	-19.3	-11.6	-5.7	-0.3	-0.5
Claims on nongovernment	42.2	27.0	30.6	56.2	60.9	15.9	11.7	19.3
Other items (net)	1.9	-10.0	-2.2	2.2	2.2	0.0	0.0	0.0
Broad money (M2)	24.1	33.5	32.7	11.4	13.2	9.3	7.0	13.2
Reserve money	2.1	32.0	47.7	9.7	9.7	8.9	8.1	16.4
Velocity (GDP-to-M2)	3.6	3.0	2.7	1.9	2.7	2.7	2.7	2.8
Money multiplier (M2/M0)	4.8	5.4	5.4	5.5	5.6	5.7	5.6	6.0
	(Percent of GDP)							
External sector								
Current account balance								
(including official grants)	-28.8	-32.8	-34.1	-48.1	-52.4	-62.4	-65.8	-39.3
(excluding official grants)	-108.4	-108.5	-97.2	-97.5	-99.9	-106.4	-100.3	-65.9
Trade balance	-36.4	-35.5	-40.7	-44.4	-49.5	-53.0	-51.8	-25.5
Exports, f.o.b.	13.3	16.7	24.6	27.5	26.7	27.9	28.3	40.8
Imports, f.o.b	-49.7	-52.2	-65.4	-71.9	-76.2	-80.9	-80.1	-66.3
Central government budget [3]								
Total revenue and grants	20.7	23.5	26.4	29.3	27.8	27.3	28.8	27.6
Of which: total revenue	18.6	22.5	23.6	27.2	26.1	24.9	26.5	25.8
Total expenditure and net lending	21.9	23.1	27.0	29.4	31.0	33.3	35.4	33.8
Of which: current expenditure	18.9	20.5	21.8	26.0	27.0	25.6	24.4	23.1
capital expenditure	3.0	2.6	5.2	3.4	4.1	7.8	11.0	10.7
Overall fiscal balance (including grants)	-1.2	0.5	-0.6	-0.1	-3.2	-6.0	-6.6	-6.2
Overall fiscal balance (excluding grants)	-3.3	-0.6	-3.4	-2.2	-4.9	-8.4	-9.0	-8.0
Public external debt	145.4	8.8	10.7	9.1	12.1	14.8	21.1	24.9
Central government domestic debt	26.1	24.0	20.6	18.1	17.6	15.7	14.4	12.8

Sources: Liberian authorities and IMF staff estimates and projections.

[1] EBS/12/59. Data as percent of GDP re-calculated using rebased GDP.

[2] Excludes UNMIL service and iron ore concessions–related imports.

[3] Budget data expressed as fiscal year ending in June on a cash basis, i.e., 2011 = FY2010/11.

Table 3. Liberia: Balance of Payments, 2010–15

(Millions of U.S. dollars, unless otherwise indicated)

	2010	2011	2012		2013	2014	2015
	Prel.	Prel.	8^{th} Rev[1]	Proj.	Proj.	Proj.	Proj.
Trade balance	-459	-630	-754	-876	-1,026	-1,068	-603
Exports, f.o.b.	215	381	467	472	539	584	967
Of which: rubber	156	250	232	185	186	200	187
Of which: Iron	0	26	133	138	147	162	538
Imports, f.o.b	-674	-1,010	-1,221	-1,347	-1,565	-1,652	-1,570
Services (net)	-805	-798	-824	-732	-705	-657	-494
Of which: UNMIL services [2]	-455	-418	-342	-342	-266	-190	-76
Income (net)	-200	-161	-166	-262	-330	-399	-463
Of which: public interest payments due [3]	-109	-1	-1	-1	-3	-4	-5
Of which: IMF	-1	-1	0	0	0	0	-1
Current transfers	1,041	1,062	926	943	803	647	479
Donor transfers (net)	978	976	838	839	695	534	365
Of which: UNMIL transfers	600	550	450	450	350	250	100
Private transfers (net)	63	86	88	89	92	96	97
Current account balance	-424	-526	-818	-926	-1,257	-1,477	-1,081
Current account balance, excluding grants	-1,402	-1,503	-1,656	-1,765	-2,059	-2,068	-1,560
Capital and financial account (net)	1,286	513	769	865	1,224	1,366	940
Capital account (HIPC debt relief) [4]	1,586	0	0	0	0	0	0
Financial account	-300	513	769	865	1,224	1,366	940
Foreign direct investment (net)	286	295	724	279	328	344	270
Portfolio investment (net)	0	0	0	0	0	0	0
Other investment (net)	-586	218	46	587	896	1,023	669
Official financing: Medium and long term (net)	-819	2	22	11	98	126	131
SDR allocation	0	0	0	0	0	0	0
Disbursements	0	6	28	17	104	135	143
Amortization	-819	-4	-6	-6	-6	-9	-12
Private financing (net) [4]	234	216	24	575	798	897	538
Errors and omissions	15	0	0	0	0	0	0
Overall balance	820	-14	-49	-61	67	129	159
Financing	-820	-11	49	61	-67	-129	-159
Change in gross official reserves (increase -) [5]	-78	-24	42	43	-40	-29	-26
Net use of Fund credit and loans	-849	14	7	18	22	19	17
Disbursements	14	14	7	18	22	22	22
Of which: ECF financing	14	14	7	18	22	22	22
Repayments	-863	0	0	0	0	-3	-6
Donor financing	0	0	0	0	50	120	150
Exceptional financing	108	0	0	0	0	0	0
Debt forgiveness	1,586	0	0	0	0	0	0
Change in arrears [6]	-1,586	0	0	0	0	0	0
Debt rescheduling plus HIPC interim debt relief [7]	108	0	0	0	0	0	0
Memorandum items:							
Current account balance (percent of GDP)							
Including grants	-32.8	-34.1	-48.14	-52.4	-65.0	-71.6	-45.6
Excluding grants	-108.5	-97.2	-97.5	-99.9	-106.4	-44.8	-39.4
Trade balance (percent of GDP)	-35.5	-40.7	-44.4	-49.5	-53.0	-51.8	-25.5
Donor transfers (net, percent of GDP)	75.7	63.2	49.3	47.5	38.5	31.7	21.7
Public sector external debt (medium and long term)							
Debt outstanding, including arrears	114	166	154	214	287	435	589
(percent of GDP)	8.8	10.7	9.1	12.1	14.8	21.1	24.9
Debt service charges (after relief)	2.2	5.8	7.3	7.3	8.6	12.9	16.3
(percent of GDP)	0.2	0.4	0.4	0.4	0.4	0.6	0.7
Terms of trade (2000=100)	212	246	228	187	182	180.8	162.2
Gross official reserves	391	416	374	372	412	440	466
Gross official reserves (months of imports) [8]	3.8	3.0	2.9	2.6	2.7	2.8	3.0

Sources: Liberian authorities and IMF staff estimates and projections.

[1] EBS/12/59. Data as percent of GDP re-calculated using rebased GDP.
[2] Net of estimated value of goods and services purchased by UNMIL (and its staff) in Liberia.
[3] From 2007, interest charged on debt stock after application of traditional debt relief mechanisms.
[4] Includes short-term trade credits and private sector operating balances abroad.
[5] Includes SDR assets and excludes SDR liabilities of US$ 163.2 million.
[6] Includes debt forgiveness from multilateral creditors and Paris Club creditors.
[7] Includes deferred debt service payments in the interim period.
[8] Excludes UNMIL service and iron ore concessions related imports.

Table 4. Liberia: Fiscal Operations of the Central Government, FY2010–15 [1]
(Millions of U.S. dollars)

	FY2010	FY2011	FY2012		FY2013	FY2014	FY2015
		Actual	8th Rev	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	288.0	374.9	470.8	461.0	505.6	575.8	611.4
Revenue	275.0	334.6	437.3	432.7	460.8	529.1	571.4
Tax revenue	207.8	269.2	338.9	357.0	364.2	383.6	424.7
Taxes on income, profits, and capital gains	70.2	111.2	120.0	145.4	131.3	142.3	153.8
Taxes on goods and services	39.2	48.4	72.0	53.7	61.0	64.6	68.7
Taxes on international trade	91.7	105.4	147.0	149.0	162.4	166.4	191.1
Other taxes	6.7	4.3	5.7	8.9	9.5	10.3	11.1
Non-tax	67.3	65.4	98.3	75.8	96.6	145.5	146.7
Grants	13.0	40.3	33.5	28.3	44.8	46.7	40.0
Expenditure and net lending	282.2	382.9	472.9	514.3	616.6	708.4	748.1
Current expenditure	250.5	309.4	418.8	446.6	473.1	487.5	512.0
Wages and salaries	113.9	138.6	186.0	187.3	204.0	216.0	225.6
Goods and services	76.7	86.3	116.1	134.0	141.3	135.0	145.0
Subsides and transfers	55.7	80.5	112.0	120.2	121.3	129.4	133.1
Interest	4.2	4.0	4.7	5.1	6.6	7.1	8.3
Capital expenditure	31.7	73.5	54.1	67.8	143.5	220.8	236.2
Foreign loan financed [2]	0.0	9.6	18.0	21.0	104.6	136.6	143.9
Domestically financed	31.7	63.9	36.1	46.8	38.9	84.3	92.3
Unallocated expenditure	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net lending	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance							
Including grants	5.9	-7.9	-2.1	-53.3	-111.0	-132.5	-136.7
Excluding grants	-7.1	-48.2	-35.6	-81.5	-155.8	-179.3	-176.7
Identified financing	-5.9	8.0	2.1	53.3	111.0	132.5	136.7
External financing (net)	-3.3	3.8	12.5	15.1	101.8	133.1	140.9
Loans	0.0	9.6	18.0	21.0	104.6	136.6	143.9
Amortization (-)	-3.3	-5.8	-5.5	-5.9	-2.8	-3.4	-3.0
Domestic financing (net)	-2.6	4.3	-10.4	38.2	9.3	-0.6	-4.2
Central Bank of Liberia	0.2	10.0	-5.2	43.5	0.0	0.0	0.0
Use of deposits	3.8	10.0	-5.2	23.5	0.0	0.0	0.0
Gross borrowing	0.0	0.0	0.0	20.0	0.0	0.0	0.0
Deposit money banks	-0.9	-3.0	-1.5	-1.5	9.3	-0.6	-4.2
Treasury bill purchases (net)	0.0	0.0	0.0	0.0	15.0	0.0	0.0
Other lending to government	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other (including repayment of arrears)	-1.8	-2.7	-3.8	-3.8	0.0	0.0	0.0
Unidentified financing/float	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Memorandum items:							
Iron ore-related revenues	29.9	33.1	44.7	18.2	13.9	31.2	33.9
Total public external debt [3]	1,679.9	113.9	140.6	166.0	286.7	435.1	589.1
Central government domestic debt [4]	293.8	292.0	291.0	290.9	289.7	288.7	284.2
Of which: foreign currency denominated	280.4	278.9	278.3	278.3	277.6	277.0	272.8
Basic balance [5]	37.6	65.5	52.0	14.5	32.4	88.3	99.4
Current balance [6]	24.6	25.2	18.5	-13.8	-12.3	41.6	59.4
Primary balance, including grants	10.1	-4.0	2.7	-48.2	-104.5	-125.4	-128.4
Fiscal year nominal GDP	1,223.5	1,418.7	1,607.9	1,656.4	1,850.9	1,998.5	2,215.8

Sources: Liberian authorities and IMF staff estimates and projections.

[1] Budget is shown on a cash basis (i.e., debt service payments are shown after all debt relief).

[2] Approximately 50 percent of on-budget loan-financed capital expenditure substitutes for hitherto off-budget, grant-financed expenditure.

[3] Includes debt to IMF.

[4] Includes central government debt to the Central Bank of Liberia (which is excluded from domestic debt in the debt sustainability analysis).

[5] Basic balance is defined as (total revenue and grants minus project grants) minus (total expenditure minus foreign and domestically financed investment spending).

[6] Current revenue less current expenditure.

Table 4. Liberia: Fiscal Operations of the Central Government, FY2010–15 (continued) [1]
(Percent of GDP)

	FY2010	FY2011	FY2012		FY2013	FY2014	FY2015
		Actual	8th Rev[7]	Prel.	Proj.	Proj.	Proj.
Total revenue and grants	23.5	26.4	29.3	27.8	27.3	28.8	27.6
Revenue	22.5	23.6	27.2	26.1	24.9	26.5	25.8
Tax revenue	17.0	19.0	21.1	21.6	19.7	19.2	19.2
Taxes on income, profits, and capital gains	5.7	7.8	7.5	8.8	7.1	7.1	6.9
Taxes on goods and services	3.2	3.4	4.5	3.2	3.3	3.2	3.1
Taxes on international trade	7.5	7.4	9.1	9.0	8.8	8.3	8.6
Other taxes	0.5	0.3	0.4	0.5	0.5	0.5	0.5
Non-tax	5.5	4.6	6.1	4.6	5.2	7.3	6.6
Grants	1.1	2.8	2.1	1.7	2.4	2.3	1.8
Expenditure and net lending	23.1	27.0	29.4	31.0	33.3	35.4	33.8
Current expenditure	20.5	21.8	26.0	27.0	25.6	24.4	23.1
Wages and salaries	9.3	9.8	11.6	11.3	11.0	10.8	10.2
Goods and services	6.3	6.1	7.2	8.1	7.6	6.8	6.5
Subsides and transfers	4.5	5.7	7.0	7.3	6.6	6.5	6.0
Interest	0.3	0.3	0.3	0.3	0.4	0.4	0.4
Capital expenditure	2.6	5.2	3.4	4.1	7.8	11.0	10.7
Foreign loans financed [2]	0.0	0.7	1.1	1.3	5.6	6.8	6.5
Domestic and grant financed	2.6	4.5	2.2	2.8	2.1	4.2	4.2
Unallocated expenditure	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance							
Including grants	0.5	-0.6	-0.1	-3.2	-6.0	-6.6	-6.2
Excluding grants	-0.6	-3.4	-2.2	-4.9	-8.4	-9.0	-8.0
Identified financing	-0.5	0.6	0.1	3.2	6.0	6.6	6.2
External financing (net)	-0.3	0.3	0.8	0.9	5.5	6.7	6.4
Loans	0.0	0.7	1.1	1.3	5.6	6.8	6.5
Amortization (-)	-0.3	-0.4	-0.3	-0.4	-0.2	-0.2	-0.1
Domestic financing (net)	-0.2	0.3	-0.6	2.3	0.5	0.0	-0.2
Central Bank of Liberia	0.0	0.7	-0.3	2.6	0.0	0.0	0.0
Use of deposits	0.3	0.7	-0.3	1.4	0.0	0.0	0.0
Gross borrowing	0.0	0.0	0.0	1.2	0.0	0.0	0.0
Deposit money banks	-0.1	-0.2	-0.1	-0.1	0.5	0.0	-0.2
Treasury bill purchases (net)	0.0	0.0	0.0	0.0	0.8	0.0	0.0
Other (including repayment of arrears)	-0.1	-0.2	-0.2	-0.2	0.0	0.0	0.0
Unidentified financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:							
Iron ore-related revenues	2.4	2.3	2.8	1.1	0.7	1.6	1.5
Total public external debt [3]	137.3	8.0	8.7	10.0	15.5	21.8	26.6
Central government domestic debt [4]	24.0	20.6	18.1	17.6	15.7	14.4	12.8
Of which: foreign currency denominated	22.9	19.7	17.3	16.8	15.0	13.9	12.3
Basic balance [5]	3.1	4.6	3.2	1.7	1.8	4.4	4.5
Current balance [6]	2.0	1.8	1.1	-1.7	-0.7	2.1	2.7
Primary balance, including grants	0.8	-0.3	0.2	-5.8	-5.6	-6.3	-5.8
Fiscal year nominal GDP (millions of U.S. dollars) [7]	1,223.5	1,418.7	1,607.9	1,656.4	1,850.9	1,998.5	2,215.8

Sources: Liberian authorities and IMF staff estimates and projections.

[1] Budget is shown on a cash basis (i.e., debt service payments are shown after all debt relief).
[2] Approximately 50 percent of on-budget loan-financed capital expenditure substitutes for hitherto off-budget, grant-financed expenditure.
[3] Includes debt to IMF.
[4] Includes central government debt to the Central Bank of Liberia (which is excluded from domestic debt in the debt sustainability analysis).
[5] Basic balance is defined as (total revenue and grants minus project grants) minus (total expenditure minus foreign and domestically financed investment spending).
[6] Current revenue less current expenditure.
[7] EBS/12/59. Data as percent of GDP re-calculated using rebased GDP.

Table 5. Liberia: Monetary Survey, 2009–14
(Millions of U.S. dollars; unless otherwise indicated)

	2009	2010	2011	2012		2013	2014
				8th Rev	Proj.	Proj.	Proj.
			(Central Bank balance sheet)				
Net foreign assets	-749.1	191.4	236.3	140.5	147.2	151.6	145.6
Of which: IMF credit [1]	-891.2	-44.4	-46.4	-64.9	-74.8	-96.9	-115.9
CBL's gross foreign reserves [2]	372.5	467.0	523.6	494.4	495.4	546.7	584.1
Commercial banks' US$ denominated deposits at CBL	60.2	75.5	107.8	120.7	123.3	135.0	143.9
CBL's gross official foreign reserves [4]	312.2	391.4	415.8	373.7	372.1	411.7	440.2
Government US$ denominated deposits at CBL	45.5	103.7	84.2	77.0	84.2	84.2	84.2
CBL's net foreign exchange position [4 5 6]	226.6	243.1	273.4	238.6	213.1	230.6	240.1
CBL's net foreign exchange position excluding SDR holdings	65.1	77.0	107.7	72.2	50.0	67.6	77.2
Net domestic assets	823.0	-93.8	-92.2	17.6	10.8	20.4	40.4
Net claims on government	1,067.4	170.6	219.0	178.2	194.5	183.9	183.3
Claims on other public sector [5]	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Claims on private sector	1.8	4.9	5.8	6.5	6.7	7.3	3.1
Claims on commercial banks	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other items (net) [5]	-246.1	-269.3	-317.0	-269.3	-269.3	-269.3	-269.3
Base money	73.9	97.6	144.0	158.0	158.0	172.0	186.0
			(Monetary survey)				
Net foreign assets	-664.3	330.5	369.9	313.6	295.0	295.1	284.5
Net domestic assets	986.7	100.1	201.5	322.7	351.9	412.0	472.0
Net domestic credit	1,241.3	380.1	487.8	602.8	632.0	692.1	752.0
Net claims on government	1,074.3	168.0	210.8	170.1	186.3	175.7	175.1
Claims on nongovernment	154.5	199.6	264.5	432.8	300.5	516.4	576.9
Claims on private sector	136.5	191.3	253.2	283.5	289.6	316.9	240.4
Claims on public enterprises	17.9	7.0	9.9	9.7	9.6	9.3	9.0
Claims on nonbank financial institutions	0.0	1.3	1.4	1.4	1.3	1.3	1.3
Other Items (Net)	-254.6	-280.1	-286.3	-280.1	-280.1	-280.1	-280.1
Monetary aggregates							
Monetary base (M0)	67.1	79.9	105.9	115.6	115.0	125.0	135.7
Currency in circulation	59.0	70.0	92.5	100.2	99.2	107.7	117.2
Required reserves	8.1	9.9	13.4	15.5	15.8	17.3	18.4
Commercial bank deposits	263.4	360.5	478.9	536.2	547.7	599.4	639.2
Total demand deposits	201.3	260.1	348.6	360.8	368.6	196.1	209.1
L$ denominated deposits	12.3	16.4	23.6	26.4	26.9	49.1	52.3
US$ denominated deposits	188.9	243.7	325.1	334.4	341.6	147.0	156.7
Time, savings and other deposits	62.1	100.4	130.3	175.4	179.1	403.4	430.1
L$ denominated deposits	19.4	24.5	39.2	43.9	44.8	29.5	31.4
US$ denominated deposits	42.7	76.0	91.1	131.5	134.3	373.9	398.7
Broad money (M2)	322.4	430.6	571.4	636.4	646.9	707.1	756.4
L$ component	90.8	110.9	155.2	170.4	171.0	186.2	201.0
US$ component	231.7	319.6	416.2	465.9	475.9	520.9	555.4
Memorandum items:							
Broad money (annual change)	24.1	33.5	32.7	11.4	13.2	9.3	7.0
L$ component as percent of beginning period broad money	2.4	6.2	10.3	2.7	2.8	2.4	2.1
US$ component as percent of beginning period broad money	21.7	27.3	22.4	8.7	10.5	6.9	4.9
Reserve money (annual change)	2.1	32.0	47.7	9.7	9.7	8.9	8.1
Base money (annual change)	6.0	19.1	32.5	9.2	8.6	8.7	8.5
Credit to government (annual change)	-0.2	-84.4	25.5	-19.3	-11.6	-5.7	-0.3
Credit to private sector (annual change)	31.5	40.1	32.4	12.0	14.4	9.4	6.6
Velocity (GDP-to-M2)	3.6	3.0	2.7	1.9	2.7	2.7	2.7

Sources: Liberian authorities and IMF staff estimates and projections.

[1] Data for 2012 8th Review corrected from US$58.1 to US$64.9 million.
[2] SDR holdings are included from December 2009.
[3] Defined as gross official reserves less government foreign currency deposits at the central bank.
[4] Including public enterprises and the local government.
[5] Including valuation adjustment.
[6] Excluding ECF disbursements.

Table 6. Liberia: Medium-Term Outlook, 2010–16

	2010 Prel.	2011 Prel.	2012 Proj.	2013 Proj.	2014 Proj.	2015 Proj.	2016 Proj.
	(Annual percentage change)						
National income							
Real GDP	6.1	8.2	8.9	8.3	5.6	7.1	5.1
Agriculture & fisheries	2.7	3.9	1.9	3.3	4.4	4.8	5.6
Forestry	6.7	3.4	2.5	1.8	6.0	6.1	6.1
Mining & panning	46.4	166.3	133.0	31.6	-4.6	5.6	-37.0
Manufacturing	3.1	3.1	3.1	3.2	3.5	3.6	3.7
Services	7.7	7.6	5.4	9.2	8.7	9.4	12.5
Real GDP excluding mining sector [1]	5.8	5.8	3.8	6.1	6.8	7.3	9.2
Nominal non-mining per capita GDP (U.S. dollar)	341.2	384.3	392.5	412.6	436.4	458.5	495.1
Prices							
GDP deflator	5.4	10.6	5.0	1.1	1.0	7.2	0.2
Consumer prices (annual average)	7.3	8.5	6.6	5.6	5.0	5.0	5.0
Consumer prices (end of period)	6.6	11.4	5.5	4.0	5.0	5.0	5.0
Population (millions)	3.8	3.9	4.0	4.1	4.2	4.3	4.4
	(Percent share)						
Nominal GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Agriculture & fisheries	36.5	36.2	30.8	28.9	28.7	25.8	25.6
Forestry	8.3	8.1	7.5	7.2	7.3	6.9	7.1
Mining & panning	0.9	4.5	12.5	13.7	12.2	17.5	13.4
Manufacturing	4.1	3.8	3.6	3.4	3.4	3.1	3.1
Services	50.3	47.4	45.6	46.7	48.4	46.7	50.8
	(Percent of GDP, fiscal year)						
Central government operations							
Total revenue and grants	23.5	26.4	27.8	27.3	28.8	27.6	26.0
Total revenue	22.5	23.6	26.1	24.9	26.5	25.8	24.4
Grants	1.1	2.8	1.7	2.4	2.3	1.8	1.6
Total expenditure and net lending	23.1	27.0	31.0	33.3	35.4	33.8	32.8
Current expenditure	20.5	21.8	27.0	25.6	24.4	23.1	22.7
Capital expenditure	2.6	5.2	4.1	7.8	11.0	10.7	10.1
Unallocated expenditure	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance, including grants	0.5	-0.6	-3.2	-6.0	-6.6	-6.2	-6.8
Overall fiscal balance, excluding grants	-0.6	-3.4	-4.9	-8.4	-9.0	-8.0	-8.4
Public external debt	8.8	10.7	12.1	14.8	21.1	24.9	29.5
Central government domestic debt	24.0	20.6	17.6	15.7	14.4	12.8	12.6
	(Percent, unless otherwise indicated)						
M2/GDP	33.3	37.0	36.6	36.6	36.7	36.1	36.3
Private sector credit/GDP	14.8	16.4	16.4	16.4	16.4	16.4	16.4
Velocity (GDP-to-M2)	3.0	2.7	2.7	2.7	2.7	2.8	2.8
Money multiplier (M2/M0)	5.4	5.4	5.6	5.7	5.6	6.0	5.9
	(Percent of GDP, unless otherwise indicated)						
External sector							
Current account balance, including grants	-32.8	-34.1	-52.4	-62.4	-65.8	-39.3	-24.7
Current account balance, excluding grants	-108.5	-97.2	-99.9	-106.4	-100.3	-65.9	-50.2
Trade balance	-35.5	-40.7	-49.5	-53.0	-51.8	-25.5	-15.9
Exports	16.7	24.6	26.7	27.9	28.3	40.8	39.4
Imports	-52.2	-65.4	-76.2	-80.9	-80.1	-66.3	-55.3
Grants (donor transfers, net)	75.7	63.2	47.5	38.5	31.7	21.7	19.1
Gross official reserves (millions of U.S. dollars)	391.4	415.8	372.1	411.7	440.2	466.0	470.8
Months of imports of goods and services [2]	3.8	3.0	2.6	2.7	2.2	3.0	3.0

Sources: Liberian authorities and IMF staff estimates and projections.

[1] Chained weighted sectoral average growth rate.

[2] Excludes UNMIL service and iron ore concessions related imports.

Table 7. Liberia: Risk Assessment Matrix[1]

Source of Risks	Relative Likelihood	Impact if Realized
International food price increases	Medium	Liberia is particularly exposed to increases in the import price of rice—the staple food in Liberia. Higher prices would affect the most vulnerable in society, putting pressure on additional assistance from the government and donors.
Strong intensification of the euro area crisis	Medium	Primary channels of contagion are lower demand for exports and falling commodity prices causing a deterioration in the external position.
A global economic slowdown	Medium	A protracted global slowdown would lead to sharper commodity price declines and reduce prospects for ongoing investment in Liberia's concessions sector. This risks future fiscal revenue and growth prospects.
Sharp slowdown in China	Low	China is a key driver of demand in commodity markets, where Liberia's exports are concentrated, and has investments in the mining sector. A sharp slowdown in China would lower exports and risk the upside return of future mining investments.[2]
Disorderly withdrawal of UNMIL	Low	Social and political instability diverting resources from public investment and additional pressure on donor assistance.
Weak implementation of public investment program or insufficient financing	Medium	Lower growth and ongoing high energy costs.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path discussed in this report (which is the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding this baseline. The RAM reflects staff's views on the source of risks and overall level of concerns as of the time of discussions with the authorities.

[2] Only one iron ore concession is included in the baseline. Investment from China represents an upside risk to the outlook.

Table 8. Liberia: Schedule of Disbursements Under the Proposed ECF Arrangements, 2012–15

Amount (Total: SDR 51.68 million)	**Date of Availability**	**Conditions for Disbursement**[1]
SDR 7.382 million	November 19, 2012	Executive Board approval of the three-year ECF arrangement
SDR 7.382 million	May 15, 2013	Executive Board completion of the first review under the three-year ECF arrangement
SDR 7.382 million	November 15, 2013	Executive Board completion of the second review under the three-year ECF arrangement
SDR 7.382 million	May 15, 2014	Executive Board completion of the third review under the three-year ECF arrangement
SDR 7.382 million	November 15, 2014	Executive Board completion of the fourth review under the three-year ECF arrangement
SDR 7.382 million	May 15, 2015	Executive Board completion of the fifth review under the three-year ECF arrangement
SDR 7.388 million	November 15, 2015	Executive Board completion of the sixth review under the three-year ECF arrangement

Source: IMF staff estimates.

[1] In addition to the conditions that normally apply to an ECF arrangement.

Table 9. Liberia: IMF Credit Position and Projected Payments to the IMF, 2012–24

(Millions of SDRs, unless otherwise indicated)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Prospective drawings													
ECF[2]	11.8	14.8	14.8	14.8	-	-	-	-	-	-	-	-	-
Projected debt service to the IMF [1]	0.0	0.0	2	3.9	5.7	7.9	12.0	11.4	12.7	13.1	10.8	8.2	5.2
Repayments and repurchases	-	-	2.1	3.7	5.5	7.7	11.8	11.2	12.6	13.0	10.8	8.1	5.2
ECF-current	0.0	0.0	2.1	3.7	5.5	7.7	9.6	6.0	4.4	2.7	0.4	0.0	0.0
ECF-projected	0.0	0.0	0.0	0.0	0.0	0.0	2.2	5.2	8.1	10.3	10.3	8.1	5.2
Interests	0.0	0.0	0.2	0.2	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.0	0.0
ECF-current	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
ECF-projected	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0	0.0
In percent of													
GDP	0.0	0.0	0.2	0.2	0.3	0.4	0.6	0.5	0.6	0.5	0.4	0.3	0.2
Gross official reserves	0.0	0.0	0.8	1.3	1.8	2.5	3.9	3.7	4.2	4.5	3.6	2.7	1.7
Exports of goods and services	0.0	0.0	0.4	0.5	0.7	1.0	1.4	1.3	1.3	1.3	1.0	0.8	0.5
Fiscal revenue (excluding grants)	0.0	0.0	0.6	1.0	1.3	1.6	2.2	1.9	2.0	1.9	1.5	1.0	0.6
Fund credit outstanding	49.4	64.2	76.8	87.9	82.4	74.8	62.9	51.7	39.2	26.2	15.4	7.3	2.1
In percent of													
GDP	4.3	5.0	5.6	5.6	5.0	4.3	3.2	2.5	1.7	1.1	0.6	0.3	0.1
Gross official reserves	20.2	23.6	26.4	28.5	26.4	23.7	20.3	16.9	13.1	8.9	5.1	2.4	0.7
Exports of goods and services	9.5	11.5	13.3	10.8	10.0	9.2	7.2	5.7	4.2	2.6	1.5	0.7	0.2
Fiscal revenue (excluding grants)	16.4	17.9	20.2	22.1	18.3	14.8	11.6	8.8	6.2	3.8	2.1	0.9	0.2
Quota	38.2	49.7	59.5	68.0	63.8	57.9	48.7	40.0	30.3	20.3	11.9	5.6	1.6

Sources: Liberia Finance Department and IMF staff estimates.

[1] The IMF Board extended the waiver of interest payments for concessional loans through December 31, 2012. For 2013, the interest rate will be 0 percent for ECF loans. After 2013, projected interest charges are based on 0.25 percent a year for the ECF. The IMF will review the interest rates for all PRGT facilities by end-2013 and every two years thereafter.

[2] 2012 includes ECF augmentation of SDR 4.4 million under the previous arrangement.

Table 10. Liberia: External Financing Requirements and Sources, 2010–15
(US$ millions)

	Est.	Projections				
	2010	2011	2012	2013	2014	2015
I. Total financing requirement	-4,733	-1,531	-1,728	-1,998	-2,053	-1,489
Current account (excluding donor grants)	-1,402	-1,503	-1,765	-1,952	-2,011	-1,446
Debt amortization	-1,669	-4	-6	-6	-9	-12
NFA	-78	-24	43	-40	-32	-31
Of which: gross reserves	-79	-24	43	-40	-29	-26
Reduction in arrears	-1,586	0	0	0	0	0
II. Total available financing	3,026	1,517	1,710	1,976	2,030	1,467
Donor transfers	978	976	839	745	654	515
Debt forgiveness	1,586	0	0	0	0	0
Foreign direct investment	286	295	279	328	344	270
Official medium- and long-term flows	0	6	17	104	135	143
Private financing	177	240	575	798	897	539
III. Exceptional financing	1,707	14	18	22	22	22
IMF	14	14	18	22	22	22
Debt forgiveness	1,586	0	0	0	0	0
Debt rescheduling	108	0	0	0	0	0
	1,707					
IV. Financing gap	0	0	0	0	0	0

Sources: Liberian authorities and IMF staff estimates and projections.

Appendix I. Summary Memo on GDP Revision for Liberia

The GDP for Liberia has been revised by IMF staff (AFR and STA) on account of uncertainty over the previous estimates and evidence of underestimation (high tax revenue to GDP ratio relative to peer countries, significantly higher monetization ratios than in peer countries).

Estimates of nominal contribution of non-services sectors are unchanged. For sectors such as agriculture, mining, forestry and manufacturing, value added at market prices is calculated based on output estimates derived from CBL monthly surveys on production and exports as well as the *Production Estimates of Major Crops and Animals 2008*.[1] Retail price data is not available and so international price data from the IMF's World Economic Outlook (WEO) Global Assumptions are used.

The revisions in the 2008 GDP are in the value added by the services sectors including: construction, education, health, financial services, government services, and trade and hotels and other services. Additionally, the revision includes rough estimates of imputed rents on occupied dwellings (previously not incorporated due to lack of data). The revision took into consideration results from the Supply and Use Tables (SUT) for 2008 and their limitations, as well as the share of these sectors in the GDP of comparator countries such as Sierra Leone and Gambia.

Construction was revised upward based on deflating estimates from the SUT estimates, which used an excessively high value added ratio to gross output. Government services are revised to incorporate the wage bill plus 20 percent of capital expenditure. Financial services were revised to include noncommercial bank activities including the CBL and rough estimates of activity in the insurance sector. Trade, hotels and similar services (restaurants, haircuts, etc.) are revised based on estimates from peer countries (about 30 percent of total services). Other services such as private education and health are revised based on the report *Appraisal of the 2010–20 education sector plan*[2] and SUT outcomes.

The revised GDP estimates results in aggregate monetary indicators for 2008 (broad money to GDP, private sector credit to GDP) comparable to neighboring Sierra Leone for the same year. Revenue to GDP declined by around one-third, but remains somewhat elevated relative to the region, which is mostly on account of higher tax revenue from international trade—on account of heavy reliance on imports—and non-tax revenue related to concessions and the Liberia Maritime Authority.

Table 1 shows a comparison between the break down for the nominal contribution of each sector to 2008 GDP under the old and revised estimates, while Table 2 shows the share of each sector. The revision shows a higher share for the services sector. Table 3 compares between old and revised GDP series at the time of the rebasing following the eighth review under the previous ECF arrangement for Liberia approved in 2008 and expired on May 31, 2012.

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[1] Produced by the Ministry of Agriculture of Liberia, Liberia Institute of Statistics & Geo-information services (LISGIS), United Nations Food and Agriculture Organization (FAO), Catholic Relief Services and Samaritan Purse.

[2] http://www.globalpartnership.org/media/library/Country_Documents/Liberia/ESP_Appraisal_Endorsement_Report.Final-Fe-.27-2010.pdf

Table1. Breakdown of GDP for 2008 by sectors

(US$ Millions)	2008 (Old GDP)	2008 (Revised GDP)
GDP at market prices	**831.6**	**1100.5**
Agriculture & fisheries	460.0	460.0
Rubber	104.7	104.7
Coffee	0.1	0.1
Cocoa	2.7	2.7
Rice	145.1	145.1
Cassava	101.5	101.5
Palm oil	0.0	0.0
Other	105.8	105.8
Forestry	92.6	92.6
Logs & timber	..	..
Charcoal & wood	92.6	92.6
Mining & panning	9.2	9.2
Iron ore	0.0	0.0
Diamonds	5.3	5.3
Other	3.9	3.9
Manufacturing	51.1	51.1
Cement	13.0	13.0
Beverages & beer	31.7	31.7
Other	6.3	6.3
Services	218.6	487.5
Electricity & water	6.0	6.0
Construction	20.3	44.0
Imputed rent (Occupied dwellings)	..	80.0
Trade, hotels, etc	46.2	151.9
Transportation & communication	30.3	30.3
Transport related to iron ore		
Financial institutions	20.2	35.7
Government services	70.2	86.2
Other services	25.5	53.4
Import Duties + Taxes on G&S − Subsidies on G&S	78.7	78.7
GDP at factor costs	752.9	1021.8

Table 2. Sectors as share of GDP for 2008

Share of GDP at market prices (Percentage)	2008 (Old GDP)	2008 (Revised GDP)
GDP at market prices	100.0	100.0
Agriculture & fisheries	55.3	41.8
Rubber	12.6	9.5
Coffee	0.0	0.0
Cocoa	0.3	0.2
Rice	17.5	13.2
Cassava	12.2	9.2
Palm oil	0.0	0.0
Other	12.7	9.6
Forestry	11.1	8.4
Logs & timber	..	..
Charcoal & wood	11.1	8.4
Mining & panning	1.1	0.8
Iron ore	0.0	0.0
Diamonds	0.6	0.5
Other	0.5	0.4
Manufacturing	6.1	4.6
Cement	1.6	1.2
Beverages & beer	3.8	2.9
Other	0.8	0.6
Services	26.3	44.3
Electricity & water	0.7	0.5
Construction	2.4	4.0
Imputed rent (Occupied dwellings)	..	7.3
Trade, hotels, etc	5.6	13.8
Transportation & communication	3.6	2.8
Transport related to iron ore	0.0	0.0
Financial institutions	2.4	3.2
Government services	8.4	7.8
Other services	3.1	4.9

Table 3. Comparison Between Old and Revised GDP Estimates for 2008–2011 at the Eighth Review Under the Previous ECF [1]

(US$ Million)	2008	2009	2010	2011
Revised IMF nominal GDP (at market prices)	**1,100.5**	**1,155.9**	**1,291.9**	**1,545.4**
Old IMF nominal GDP (at market prices)	**831.6**	**844.7**	**941.4**	**1,105.8**
Revised IMF GDP real growth (%)	**8.2**	**6.7**	**6.1**	**8.2**
Old IMF GDP real growth (%)	**4.7**	**2.8**	**5.0**	**6.4**

[1] Previous ECF arrangament for Liberia approved in 2008 and expired on May 31, 2012.

Appendix II. Fiscal Information Under the Government Finance Statistics Manual 2001

Table 1. Liberia: Fiscal Operations of the Budgetary Central Government, FY2010–15 [1]

(Millions of U.S. dollars)

	FY2010	FY2011	FY2012		FY2013	FY2014	FY2015
		Actual	8th Rev	Proj.	Proj.	Proj.	Proj.
Revenue	**288.0**	**374.9**	**470.8**	**461.0**	**505.6**	**575.8**	**611.4**
Taxes	207.8	269.2	338.9	357.0	364.2	383.6	424.7
Social contributions [2]	…	…	…	…	…	…	…
Grants	13.0	40.3	33.5	28.3	44.8	46.7	40.0
Other revenue (non-tax revenue)	67.3	65.4	98.3	75.8	96.6	145.5	146.7
Expense	**250.5**	**309.5**	**418.8**	**446.5**	**473.1**	**487.5**	**514.0**
Compensation of employees (wages & salaries)	113.9	138.6	186.0	187.3	204.0	216.0	225.6
Use of goods and services	76.7	86.3	116.1	134.0	141.3	135.0	145.0
Subsidies and transfers	55.7	80.6	112.0	120.2	121.3	129.4	133.1
Consumption of fixed capital [2]	…	…	…	…	…	…	…
Interest	4.2	4.0	4.7	5.1	6.6	7.1	8.3
Grants	0.0	0.0	0.0	0.0	0.0	0.0	2.0
Social benefit [2]	…	…	…	…	…	…	…
Other expenses	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net acquisition of nonfinancial assets	**31.7**	**73.5**	**54.1**	**67.8**	**143.5**	**220.8**	**236.2**
Foreign loan financed [3]	0.0	9.6	18.0	21.0	104.6	136.6	143.9
Domestically financed	31.7	63.9	36.1	46.8	38.9	84.3	92.3
Gross operating balance	37.6	65.4	52.0	14.5	32.4	88.3	97.4
Net lending (+)/borrowing (-) (overall balance)	**5.9**	**-8.0**	**-2.1**	**-53.3**	**-111.0**	**-132.5**	**-138.7**
Net financial worth, transactions	**5.9**	**-8.0**	**-2.1**	**-53.3**	**-111.0**	**-132.5**	**-136.7**
Net acquisition of financial assets	**-2.9**	**-10.0**	**5.2**	**-43.5**	**-15.0**	**0.0**	**0.0**
By instrument							
Currency and deposits	-3.8	-10.0	5.2	-23.5	0.0	0.0	0.0
Debt securities	0.9	0.0	0.0	0.0	-15.0	0.0	0.0
Loans	0.0	0.0	0.0	-20.0	0.0	0.0	0.0
Net incurrence of liabilities	**-8.8**	**-2.0**	**7.2**	**9.9**	**96.0**	**132.5**	**136.7**
By residency and instrument							
Domestic	**-5.4**	**-5.8**	**-5.3**	**-5.3**	**-5.7**	**-0.6**	**-4.2**
Currency and deposits	0.0	-3.0	-1.5	-21.5	-5.7	-0.6	-4.2
Securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Liberian authorities and IMF staff estimates and projections.

[1] GFS 2001 presentation with budget shown on a cash basis (i.e., debt service payments are shown after all debt relief).

[2] Not available.

[3] Approximately 50 percent of on-budget loan-financed capital expenditure substitutes for hitherto off-budget grant-financed expenditure.

Table 1. Liberia: Fiscal Operations of the Budgetary Central Government, FY2010–15 (continued) [1]

(Percent of GDP)

	FY2010	FY2011		FY2012		FY2013	FY2014	FY2015
		PN	Actual	8th Rev [4]	Proj.	Proj.	Proj.	Proj.
Revenue	**23.5**	**26.4**	**26.4**	**29.3**	**27.8**	**27.3**	**28.8**	**27.6**
Taxes	17.0	19.0	19.0	21.1	21.6	19.7	19.2	19.2
Social contributions [2]	…	…	…	…	…	…	…	…
Grants	1.1	2.8	2.8	2.1	1.7	2.4	2.3	1.8
Other revenue (non-tax revenue)	5.5	4.6	4.6	6.1	4.6	5.2	7.3	6.6
Expense	**20.5**	**21.8**	**21.8**	**26.0**	**27.0**	**25.6**	**24.4**	**23.2**
Compensation of employees (wages & salaries)	9.3	9.8	9.8	11.6	11.3	11.0	10.8	10.2
Use of goods and services	6.3	6.1	6.1	7.2	8.1	7.6	6.8	6.5
Subsidies and transfers	4.5	5.7	5.7	7.0	7.3	6.6	6.5	6.0
Consumption of fixed capital [2]	…	…	…	…	…	…	…	…
Interest	4.2	4.0	4.0	4.7	5.1	6.6	7.1	8.3
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	2.0
Social benefit [2]	…	…	…	…	…	…	…	…
Other expenses	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net acquisition of nonfinancial assets	**2.6**	**5.2**	**5.2**	**3.4**	**4.1**	**7.8**	**11.0**	**10.7**
Foreign loan financed [3]	0.0	0.7	0.7	1.1	1.3	5.6	6.8	6.5
Domestically financed	2.6	4.5	4.5	2.2	2.8	2.1	4.2	4.2
Gross operating balance	3.1	4.6	4.6	3.2	0.9	1.8	4.4	4.4
Net lending (+)/borrowing (-) (overall balance)	**0.5**	**-0.6**	**-0.6**	**-0.1**	**-3.2**	**-6.0**	**-6.6**	**-6.3**
Net financial worth, transactions	**0.5**	**-0.6**	**-0.6**	**-0.1**	**-3.2**	**-6.0**	**-6.6**	**-6.2**
Net acquisition of financial assets	**-0.2**	**-0.7**	**-0.7**	**0.3**	**-2.6**	**-0.8**	**0.0**	**0.0**
By instrument								
Currency and deposits	-0.3	-0.7	-0.7	0.3	-1.4	0.0	0.0	0.0
Debt securities	0.1	0.0	0.0	0.0	0.0	-0.8	0.0	0.0
Loans	0.0	0.0	0.0	0.0	-1.2	0.0	0.0	0.0
Net incurrence of liabilities	-0.7	-0.1	-0.1	0.4	0.6	5.2	6.6	6.2
By residency and instrument								
Domestic	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	0.0	-0.2
Currency and deposits	0.0	-0.2	-0.2	-0.1	-1.3	-0.3	0.0	-0.2
Securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	-0.3	0.0	0.0	0.0	1.2	0.0	0.0	0.0
Other accounts payable	-0.1	-0.2	-0.2	-0.2	-0.2	0.0	0.0	0.0
External	-0.3	0.3	0.3	0.8	0.9	5.5	6.7	6.4
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Loans	-0.3	0.3	0.3	0.8	0.9	5.5	6.7	6.4
Other accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Liberian authorities and IMF staff estimates and projections.

[1] GFS 2001 presentation with budget shown on a cash basis (i.e., debt service payments are shown after all debt relief).

[2] Not available.

[3] Approximately 50 percent of on-budget loan-financed capital expenditure substitutes for hitherto off-budget grant-financed expenditure.

[4] EBS/12/59, GDP data was significantly revised after the 8th review based on improved estimates of the size of the services sector.

Appendix III. Letter of Intent

Monrovia, November 2, 2012

Madame Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Madame Lagarde,

1. The attached Memorandum of Economic and Financial Policies (MEFP) summarizes the economic and financial policies of the government of Liberia for the period July 2012–June 2015. These policies are anchored in the government's Agenda for Transformation—the new Poverty Reduction Strategy (PRS2), which the government intends to formally launch in November 2012.

2. The government requests that the MEFP be supported by the International Monetary Fund (IMF) under a three-year Extended Credit Facility (ECF) and requests the first disbursement under the ECF. We hereby request the approval by the Executive Board of a three- year ECF arrangement in an amount equivalent to SDR 51.68 million (40 percent of Liberia's quota). To monitor progress in implementing our reform agenda, the program includes a set of quantitative performance criteria, indicative targets, and structural benchmarks, outlined in the attached Memorandum of Economic and Financial Policies (MEFP) and the Technical Memorandum of Understanding (TMU).

3. The previous ECF-supported program, approved in 2008, was successfully completed on May 31, 2012. Over the last four years, Liberia made substantial progress: macroeconomic and financial stability was achieved, key institutions were largely rebuilt, external debt profile improved and a mechanism was put in place to ensure a sustainable position going forward, and social conditions were improved. Nonetheless, important challenges remain. This MEFP outlines our recent economic performance and economic and social policies planned for FY 2012/13 (July–June).

4. The outlook for the second half of 2012 and over the medium term remains favorable. We expect the expansion of Government spending to provide additional employment and increase household incomes. The global economic outlook still presents risks, especially with the slowdown in China and continued economic problems in Europe. These factors largely present risks to the continued growth in the export sector.

5. Macroeconomic performance in 2011 and during the first half of 2012 has been strong. Growth is estimated to have reached 8.2 percent in 2011, U.S. dollar-denominated inflation closed at 10.2 percent. Gross official reserves rose to 3 months of imports at end-2011. These positive results have carried over into the first half of 2012. Growth is estimated at close to 9 percent this year due mainly to the resumption of iron ore exports. Inflation has declined to 4 percent year-on-year at end-June 2012.

6. Liberia's new Poverty Reduction Strategy 2 (PRS2)–the Agenda for Transformation–focuses on investment in human development, infrastructure and institutions. The focus of PRS2 will be on laying the foundation for broad-based and inclusive growth; taking the achievements we have made under the first PRS and using those as an opportunity to work on reforms that will promote business activity, rebuilding educational institutions, enhancing governance reforms and borrowing to invest in large capital projects that will open up Liberia to industry. Developing the Liberian private sector is a priority goal of the Government's transformation agenda. The budget for FY 2013 focuses on this agenda, and there has been a large expansion of capital investment to at least 25 percent of the budget. It has been prepared in the context of a Medium Term Expenditure Framework (MTEF) to maintain the Government's focus on critical investments in infrastructure and capacity building. This year's budget introduces a multi-year budgeting framework, and ensures resources are aligned to the policy priorities in the Agenda for Transformation. It focuses on the main fiscal challenges including containing recurrent spending and boosting capital spending.

7. Monetary policy over the medium term will focus on containing inflation by maintaining stability in the exchange rate. The CBL aims to build reserve coverage to about three months of imports over the medium term to buttress the macroeconomic stability, giving due consideration to the high opportunity cost of holding reserves in the face of strong development needs and massive infrastructure gaps. The government also intends to strengthen policies aimed at improving confidence and widespread use of the Liberian dollar.

8. The Government of Liberia and the CBL believe that the economic and financial policies set forth in the attached memorandum provide an adequate basis for achieving the objectives and targets of our program, but we will take any additional measures that may become necessary for this purpose. We will consult closely with the IMF staff on the adoption of such measures, and in advance of any revisions to the policies contained in the MEFP. We will provide the Fund with all information necessary to monitor implementation of the program supported by the ECF in a timely manner as outlined in the Technical Memorandum of Understanding.

9. We remain committed to transparent policy-making and are willing to make the contents of this letter and those of the attached MEFP and Technical Memorandum of Understandings (TMU), as well as the Staff Report for the 2012 Article IV consultation discussions available to the public.

Sincerely yours,

/s/

Amara Konneh
Minister of Finance
Ministry of Finance

/s/

Joseph Mills Jones
Executive Governor
Central Bank of Liberia

Attachments: Memorandum on Economic and Financial Policies

Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

I. INTRODUCTION

1. The Government of Liberia remains committed to achieving poverty reduction through sustained economic growth and inclusive development while maintaining broad macroeconomic stability. The strategies to achieve these goals are set out in the Agenda for Transformation—Poverty Reduction Strategy 2 (PRS2)—and the medium-term priorities set in the long term national vision "Liberia Rising 2030". The Government and the International Monetary Fund (IMF) are cooperating on a second three-year Extended Credit Facility (ECF) to support prudent macroeconomic policies and structural reforms that underlie strategies in the PRS2 and Liberia Rising 2030.

2. This memorandum of economic and financial policies (MEFP) reviews the main achievements since 2008 under the previous ECF arrangement, recent developments during 2012, and describes policies and targets for 2012/13 (July-June) and the medium term (2014/15).

II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE BUTTRESSED UNDER PREVIOUS EXTENDED CREDIT FACILITY (ECF) ARRANGEMENT

3. In 2011, economic growth continued its solid performance with an estimated growth of 8.2 percent. The growth forecast for 2012 is put at 8.7 percent, expected to be largely driven by the restart of the iron ore and higher quantity of timber exports, as well as growth in the construction and services sectors.

4. The Government of Liberia continued on its path of commitment to sound macroeconomic management underpinned by transparency and accountability. Performance buttressed by the previous ECF arrangement was strong and very constructive. The Government implemented an Integrated Financial Management Information System (IFMIS), passed a new PFM law, and set out rules for controlling debt. Also, bank regulation and supervision were strengthened and efforts are in place to regulate and supervise the insurance companies and microfinance institutions. Concrete steps were taken to improve the credit environment with the passing into law of a commercial code and the subsequent establishment of a commercial court, in addition to the credit reference system established at the CBL. These, inter alia, have led to expansion in commercial deposits and credit. Exchange rate broadly stabilized and inflation remained largely contained with strong growth continuing even during the global financial crisis. The Government rebuilt internal audit capacity and strengthened the General Auditing Commission (GAC) ability to conduct audits of all Government Ministries and Agencies. The Automated System for Custom Data (ASYCUDA) system was rolled out at the major entry ports and the Government increased the level of tax revenues coming from domestic sources. During

the course of the last five years the overall budget increased from around US $185 million in 2007/08 to US $516 million in 2011/12. Despite Liberia's progress so far, important challenges remain. The largest of these remains the huge infrastructure deficit (i.e., electricity, roads, and sea and air ports). The Mount Coffee Hydroelectric plant and much of the road system outside of Monrovia are still incomplete, even though much progress has been made in expanding the road and power networks. The Government has demonstrated commitment to improve the power system; this is demonstrated by the US $45.3 million allocated to energy in the FY2013 budget. Liberia has also joined the West African Power Pool scheme (WAPP). Despite the efforts that have already been put in place to control recurrent spending and set a minimum level of capital spending within the budget at 25 percent, the infrastructure funding needs far exceed the available resources requiring external assistance.

5. The Government introduced an interim policy measure, the 150 Day Action Plan with the objective of making short-term, high impact policy interventions aimed at creating temporary jobs at different entities in Government; expanding the service network of the national transit authority, and developing the MTEF and the associated budget.

6. The government is still in the process of reconciling GoL accounts for FY2011/12 using the newly-installed Integrated Financial Management Information System (IFMIS). On the basis of IFMIS data, revenue collection for 2011/12 is estimated at US $475.2 million, including a carry forward (re-appropriation from unspent funds from previous fiscal year) of US $8.6 million from FY2010/11 and US$ 7.5 million in borrowing from the CBL. Excluding these two items,[1] revenue for FY2011/12 amounted to about US $460 million, compared to the ECF 8th Review target of US $470.2 million. According to IFMIS, government expenditures for FY2011/12 amounted to US $488 million (including expenditures made during July–September in line with the 90-day rule to cover commitments from the previous fiscal year).[2] In addition, US $21 million was spent on off-budget projects including road construction and rehabilitation financed by multilaterals. There was also US $12 million spent on dredging the port which was not included in the budget and executed off-budget, financed by direct borrowing from the central bank. These off-budget expenditures are not included in IFMIS. Including the off-budget items, total expenditures amounted to US $514 million, compared to the 8th review ECF target of US $473 million.[3] The full extent of the FY2011/12 budget outturn will be known once the on-going reconciliation of the GoL accounts is finalized.

[1] Carry-forward of re-appropriations and borrowing from CBL are recorded as domestic financing in ECF macroeconomic framework.

[2] Expenditures made during the 90 day period are not included in the ECF macro framework. IFMIS in 2011/12 (US $488) includes US $10 million in amortization and arrears payments that are recorded as financing in the ECF macro framework, and does not include US$ 2 million in interest payments which are included as expenditures in the ECF framework.

[3] The 8th Review included the off-budget items in government expenditures.

III. OBJECTIVES AND ECONOMIC POLICIES FOR THE THREE-YEAR ECF PERIOD

7. Over the next three years, the successor ECF arrangement will help support our new Poverty Reduction Strategy 2, the Agenda for Transformation (AfT), which builds on the gains made from the previous PRS1. Under this AfT, investment will be made in infrastructure; institutions and in people with efforts exerted at directing a significant portion of expenditure towards capital projects, which is expected to double in the 2012/13 budget. The AfT aims to consolidate the gains made at maintaining macroeconomic stability and building a foundation for strong economic growth. The AfT sets out to ensure stable, strong economic growth with the end objective of meeting middle income status by 2030. Our current estimates suggest that this would require around 8 percent real growth annually. In the context of the Agenda for Transformation (PRS2), the strategy for economic growth and poverty reduction is anchored in a six-point strategy:

- Investing in infrastructure, particularly in energy and roads. This is the key to the economic renewal; transforming Liberia into a West African hub and a major trading partner in the region.
- Investing in people. An educated population is the key to innovation, growth, good business, and good governance. There will be an expansion of vocational and technical training, of business apprenticeship and university training.
- Invest in agriculture. Investing in agriculture is the key to generating incomes for the poorest households, stable and low-priced food and to controlling inflation and reducing poverty. With investment in agriculture, we can build a consumer base amongst the poorest, and we can reduce the insecurity that holds back investment.
- Developing the private sector with emphasis on Liberian entrepreneurship. Steps will be taken to remove impediments to private sector growth as well as to provide the necessary investment incentives for small and medium businesses.
- Prioritizing policies that facilitate job creation, especially for the young. This will promote stability and the building of skills. This year the Government has set aside $15 million for training and creating employment opportunities entirely focused on youth.
- Reducing inequality. We must ensure that the proceeds of growth benefit all of society, and that the abundance of natural resources is used wisely to create economic and employment opportunities.

8. The Government, under the AfT, aims to ensure that we target interventions that will promote incomes among the poorest households. The key objectives of AfT as seen below are set out in 4 main pillars and cross-cutting considered as the 5^{th} pillar:

Security and Rule of Law: the Government will invest in the security sector in preparation for the UNMIL drawdown; this will include developing a strategy for the necessary areas of security investment to meet the major areas of UNMIL activity. Together with the Ministry of Justice, we will prepare by October 31, 2012 a proposed budget for FY 2014 which we will discuss with UNMIL by November 30 to finance training needs and start assuming some non-peace keeping and other related activities. Spending on security will be part of the MTEF starting with FY 2014.

Governance and Public Institutions: the Government will work to promote reforms to enhance governance and economic management, including continuing the program-based MTEF budget next year; and reforming the reporting mechanism to ensure that, prior to allotments being disbursed, the Ministry of Finance is aware of performance and shortfalls by Ministries and Agencies. The Government will continue to roll out reforms to our budget process, and our expenditure management, support the work of LACC and the GAC in monitoring government activities and continue to ensure we provide operational support to M&As.

Human Development: education and an expansion of vocational training will be funded and free access to basic education for all children will be enhanced. The easiest way to lift people from poverty is to provide the opportunity for growth; the Government will work on developing work readiness training, and eradicate illiteracy.

Cross Cutting: funding has been put aside in this budget for youth schemes to promote youth empowerment; the Government will support the Ministry of Gender Development in its efforts to ensure workplace fairness. We will fund anti-HIV programs and implement the new Children's Law and establish National Council for Children's' Well-being.

9. The cost of the AfT/PRS2 is estimated at around US $2.2 billion over the period of the IMF program. This will be funded by the Government and donor partners with externally funded donor efforts aligned with the PRS. The MTEF budget sets out the major priorities for funding of the Government. This includes: the rebuilding of the Mount Coffee Hydroelectric plant (which will be co-financed between Government and Donors); the construction of new roads and bridges in line with the Transport Master Plan. Generally, however, the Government priorities are: rebuilding power infrastructure and generation (and connecting to the West African Power Pool), rebuilding roads, controlling recurrent spending and rebuilding educational institutions (and expanding the role of vocational education).

IV. THE POLICY AGENDA FOR 2012/13

A. Fiscal Policy

10. The budget for FY 2013 has been prepared in the context of the recently introduced Medium Term Expenditure Framework (MTEF). This year budget introduces multi-year budgeting framework, and ensures resources are aligned to the policy priorities in the Agenda for

Transformation. It focuses on the main fiscal challenges including containing recurrent spending and boosting capital spending.

11. Over the medium term, we plan to continue to gradually increase capital spending as a share of the budget through further reallocation from current spending. To support this objective, already this fiscal year, we have put in place a current spending savings policy to reduce spending on gasoline, foreign and domestic travel, as well as other non-priority spending. Savings will be allocated to priority spending, particularly capital investment. For FY 2014 plans are being made to collapse public sector employees' basic salary with the current special allowances to better control payroll spending. We will create a Liberia Development Fund in FY 2013 to save the unspent investment appropriation ensuring that unfinished infrastructure projects' funding is not constrained in the upcoming fiscal years.

12. The budget for FY 2013 was built around fiscal rules. These rules included efforts to promote capital spending, reduce transfers between spending lines, and control recurrent expenditures. The key rules (see details in the Budget Framework Paper) are as follows:

a. No more than 34 percent of FY 2013 budget should be allocated to salaries and wages. And we are committed to reducing it further down by FY 2015 as a way to create the necessary fiscal space to increase capital spending.

b. At least 25 percent of the budget must be capital spending, of which at least 10 percent must be on the energy sector.

c. 25 percent of GoL expenditure on goods and services will be spent on Liberian businesses (25 percent of furniture spending must also be on Liberian sourced products).

d. no more than 15 percent of capital spending must be on administrative overheads.

e. transfers from investment to recurrent must be no more than 5 percent of investment appropriations.

13. Revenue collection will be strengthened by a combination of additional tax policies and tax administrative measures. These include the migration from General Sales Tax (GST) to Common External Tariff (CET); taxation on inbound calls; strengthening tax enforcement and compliance by conducting comprehensive audits of the largest 20 taxpayers including commercial banks, logging and insurance companies, as well as by launching a robust anti-smuggling campaign; and strengthening taxpayers services by establishing a one-stop customer care center, with technical assistance from the IMF, which will include a special call center to answer tax questions that would be accessible to all Liberians within and out of the country. For FY 2012/13, total revenue collection (including grants) is projected at 27 percent of GDP.

14. There are also contingent revenues—where there are uncertainties in the timing of their collection and are currently not included in the revenue projections. Among these, US $45 million is expected from the sale of the contract for Block 13 and is dependent on the finalization of the contract negotiation. If received, and assuming that total revenue collection is on track, these resources will be aligned to specific expenditures under the PSIP.

15. Some of the money in the grant revenue is 'at risk'; this year the Government has developed a measure of risk for the grant revenue, and has put in place a strategy to minimize the risk of the grant revenue which is tied to specific deliverables. This will include regular reporting from M&As responsible for the deliverable areas, and monthly follow up by the Ministry of Finance Aid Management Unit to determine interventions required to meet targets.

16. Total expenditure in FY 2013 are expected to increase to around 33 percent of GDP from around 31 percent of GDP in the last fiscal year, reflecting a 3.7 percentage point increase in capital spending. For FY 2013, all investment projects had to be justified, scored and aligned with Government and Ministry priorities. Efforts will be exerted to improve the efficiency and execution in the implementation of projects. To do this, we plan to set up the Project Management Office (PMO) by end-December 2012 (structural benchmark) which will focus on the evaluation (project costing and appraisal) and selection process of investment projects and reviewing feasibility studies for projects. This Unit will monitor the implementation of the PSIP and capital spending component of the Agenda for Transformation. Ministries and Agencies will develop timelines for sector projects and itemized spending plans to ensure that allotments and releases of funds occur in time for them to be useful for Ministries and Agencies, and itemized plans will help with outturn reporting at the end of the fiscal year.

17. Government treasury bills in Liberian Dollars will be launched by end-December 2012 (structural benchmark) to be used for cash management purposes and for the Government's domestic financing needs.

18. Private investment promotion is a key aim of this Government's agenda, fully recognizing the importance of increasing the level of private investment as part of the effort to meet the Vision 2030 objective of middle income status. This objective cannot be achieved by borrowing and Government investment alone. With this in mind, there are planned interventions in the short to medium term which include:

a. Working with development financing institutions to provide SME guarantees: the Government will work with development partners to set up a fund to offer guarantees to small and medium size enterprises, to reduce their capital costs.

b. Promoting SMEs representative organizations: the Government has taken steps towards promoting the views of the business organizations within Liberia. This has included setting up a communication between the Minister of Finance's office and the Liberian Chamber of Commerce to find out what they believe could encourage business activity.

c. Work to equalize fees for Liberian and Non-Liberian businesses, a commitment of the Government under its WTO accession plans.

B. Governance and Public Financial Management

19. We plan to introduce a Treasury Single Account approach by end-December 2012 (structural benchmark) as a tool to strengthen the central government's cash management capacity. Line ministries and agencies (M&As) accounts will be monitored on a monthly basis to provide consolidated cash balances held by the GoL with the purpose of reducing idle balances and inactive accounts to improve liquidity management. In line with the new cash flow planning approach, line ministries have been asked to submit their rolling plans for the preparation of a consolidated annual cash plan.

20. As part of the PFM reform agenda, the introduction of IFMIS has been completed in 8 Ministries, including the 5 largest (Education, Health, Public Works, Finance, Foreign Affairs, and Agriculture); and the General Auditing Commission (GAC) has also installed the IFMIS infrastructure. The GAC should be fully connected to IFMIS, giving GAC full access to IFMIS, by the end of December 2012 (structural benchmark). The GAC will then start conducting the auditing of the FY 2011/12 budget by January 2013 using IFMIS, beginning with the 8 ministries currently connected to IFMIS. Prior to this action, full testing of the system in the above mentioned M&As will be completed by October 2012. The GAC will complete audits of the FY2011/12 budget for the eight (8) big ministries and agencies using IFMIS by end-September 2013. We will continue to rollout IFMIS to an additional 8 M&As by the end of FY 2013.

21. The Government will continue its effort to remove ghost names from the payroll system and has started work in this regard including the introduction of biometric technology to strengthen payroll controls. This will continue with all employees eventually expected to be covered by the system by end-June 2014.

22. The Government will introduce the Civil Service Management (CSM) module within IFMIS and the Human Resource Management Information System (HRMIS) sub-module within the CSM, both by end-June 2013 (structural benchmark). Currently, 22 out of 29 M&As payrolls have been cleaned up and the personnel records will be uploaded to IFMIS. Cleaning up of the remaining 7 institutions[4] will be completed by end-June 2013 (structural benchmark), including in the Ministry of Education where an attendance monitoring system with TA support from USAID is also being launched in January 2013. By end-June 2013, the payrolls of all M&As will be uploaded to IFMIS and used for payroll payments.

[4] Ministries of Education, Health, Public Works, Justice, Internal Affairs, Lands and Mines, Agriculture.

23. Progress has been made at initially strengthening of internal audits of high spending M&As, consistent with the Government's internal audit strategy. Currently, 8 out of 16 institutions have their system (institutional and human capital) in place and we plan to complete an additional 8 institutions by September 30, 2012 and fully rollout the process to all M&As by June 30, 2013.

24. The Code of Conduct Executive Order was signed by the President on the 9th of January 2012 and the Government has begun an effort to implement the Code, including having staff throughout the Government, sign copies to signify their commitment to comply with this Executive Order.

25. The Civil Service Agency (CSA) and the General Auditing Commission carried out a joint audit of the pension system to verify all people on the pension payroll. Schemes like this will continue in the future including all other payrolls.

26. The government is advancing on the introduction of the Public Expenditure Tracking System (PETS), which is expected to be in place by end-2012. It links public resources to outcomes; the framework would allow the Ministry of Finance and line ministries and agencies to track spending levels and deliverables.

27. In order to improve financial oversight of SOEs/public financial entities, an SOE unit within the Ministry of Finance will be set up by end-December 2012 (structural benchmark) which will be responsible for collecting quarterly financial reports from the 8 largest SOEs/public financial entities[5] and ensuring they are in line with the PFM law. By end-June 2013, the 8th largest SOEs will be required to report to the SOE unit within the Ministry of Finance their financial performance for the quarter January–March 2013 (Structural Benchmark). Thereafter, SOEs will regularly report their quarterly financial performance, three months after the end of each quarter. In the meantime, the Government is improving governance of SOEs by ensuring that SOEs which do not provide financial reports will not receive any subsidies. Steps will also be taken to work with SOEs to build their reporting capacity. The SOE Unit will also strengthen oversight of SOE performance to ensure timely and accurate transfer of revenues to the Ministry of Finance. By end-December 2012, the Unit, working with other GoL stakeholders, will also prepare a strategy to manage fiscal risks of SOEs and determine which SOEs should be privatized and whether or not Government subsidies should remain for enterprises.

28. Management of natural resource revenue: the Government notes the importance of ensuring that natural resource revenues are properly managed. The Government will: (i) create a resource revenue sub-unit in the large taxpayers unit of the Ministry of Finance by June 2013 (structural benchmark) to improve the monitoring of concessions to more accurately determine

[5] National Ports Authority (NPA), Liberia Electricity Company (LEC), Liberia Petroleum and Refinery Company (LPRC), National Oil Company of Liberia (NOCAL), Liberia Telecommunications Authority (LTA), Liberia Maritime Authority (LMA), Robert International Airport (RIA), Liberia Water and Sewerage Company (LWSC).

the quality and quantity of natural resource production, and exports and estimate royalty requirements; and (ii) begin reporting natural resources revenues separately in fiscal outturns starting in FY 2014.

29. The Government will prepare monthly reports (to form part of the consolidated monthly fiscal report) by December 2012, on off-budget externally financed projects reconciling data with the Budget and Expenditure offices at the Ministry of Finance.

C. Monetary Policy and Financial System

30. Monetary policy over the medium term will focus on containing inflation in Liberian dollar-denominated prices by maintaining stability in the exchange rate through the weekly foreign exchange auctions. The CBL recognizes the need to build up foreign exchange reserves to mitigate adverse shocks especially given the vulnerabilities to food and fuel price spikes and sluggish global economic growth. However, the CBL is also taking into account the high opportunity cost of holding reserves given the strong development needs and massive infrastructure gaps. To this end, the CBL aims to maintain adequate reserve coverage of about three months of imports over the medium term to buttress the macroeconomic stability while creating some policy buffers. [6]

31. An orderly and market driven de-dollarization is a strategic objective of the Government. The ongoing measures being taken to improve confidence and to promote widespread use of the Liberian dollar, including improving the quality of notes and issuing higher denomination bills, will be strengthened. Moreover, the Government will set a plan to de-dollarize public expenditure including paying all public sector salaries in Liberian dollars over the medium term. Additionally, the Government's issuance of treasury bills by December 2012 will help mop up excess Liberian dollar liquidity in the system and to encourage mobilization of Liberian dollar deposits.

32. The CBL is taking active measures aimed at strengthening the banking system and other financial institutions. Specifically, the CBL is engaging banks below minimum capital requirements to oversee recapitalization plans. As a result of this engagement, affected banks received capital injections from their foreign parents in 2011 and 2012. The CBL will continue working with banks remaining below minimum capital requirement to ensure full compliance with the capital and provisioning regulations by end-2012. Moreover, the current risk-based supervision regime of the CBL, whose first cycle of bank inspections successfully ended, will focus on emerging credit risks, aggressive monitoring of banks to ensure that they remain healthy, and improving banks' risk management. In addition, the CBL will submit to legislature a revised Insurance Act by end-June 2013 (structural benchmark) to streamline regulation in the insurance sector and establish the central bank as the sole regulator of all insurance agencies.

[6] Excluding UNMIL and iron ore related imports.

33. In order to strengthen financial inclusion and promote lending to small borrowers, the CBL will seek to improve the credit environment through: (i) strengthening the commercial court; ii) enhancing the credit reference system by widening its database and improving its accessibility; iii) establishing, by end-June 2013, a collateral registry to support execution of collateral on bad loans and improve the credit culture (structural benchmark). The monetary authority will also work together with donors to mobilize long-term financing of bank's lending to agriculture and small- and medium-sized enterprises and to improve financial literacy and business practices.

D. Debt Management, Resolution and External Policies

34. The Government has put in place fiscal rules to guide borrowing, to ensure that we never again have to ask the world for forgiveness from our debt. This Government has achieved in the last six years remarkable write downs on our debt stock of around US $4.7 billion. We will ensure, through sensible management of our finances and never again build up debt with nothing to show for the cost. Our borrowing rules will ensure that:

a. We use borrowing to boost capital, and where the cost is borne by future generations so will the benefit;

b. Total public sector borrowing (including public, publicly guaranteed debt and debt of SOEs) in foreign currency (including concessional and nonconcessional borrowing) will be limited to 4 percent of GDP in NPV terms averaged over three years.

c. The Government will seek nonconcessional borrowing, with agreement with the Fund, for specific economic viable projects with high economic and social returns and assessed by an independent entity, should the need arise.

d. Borrowing is managed sustainably and we never build a debt stock too high for repayment; the Government has set as its fiscal rules for borrowing:

   i. All borrowing must be undertaken for the purposes of investment, consistent with the Public Sector Investment Plan (PSIP)

   ii. Total debt stock must not exceed 60% of the previous year's GDP as contained in the PFM regulations.

   iii. Prior to new borrowing being undertaken a Debt Sustainability Analysis (DSA) must be carried out and presented to the Debt Management Committee (DMC) to ensure debt rules are not breached

35. SOEs taking on debt will be conditional on SOEs providing full and accurate reports of finances, as well as the presentation of an economically beneficial project with good loan terms. SOE and SOE guarantees will be included within our debt stock, in line with the PFM law.

36. The Debt Management Unit will develop a forward looking medium-term debt strategy to identify specific borrowing plans and negotiate new debt in line with the fiscal rules to achieve borrowing targets in the most cost effective way by the end of 2012. The three year strategy will be refreshed in line with annual Budget preparations to enable timely execution of new borrowing upon Budget approval.

37. We will continue making progress on finalizing bilateral and multilateral debt agreements. The debt rescheduling with BADEA has been signed, increasing the maturity of the loan to 40 years with a 5-year grace period and zero percent interest rate. The debt with Saudi Arabia has been finalized as the negotiation has been concluded and signed.

38. We are making efforts to ensure timely and accurate reporting of debt and off-budget project financing. The IDA credits have been incorporated into measures of debt accumulation in the Budget Framework Paper and have been included in sustainable debt profiles produced by the Ministry of Finance. Both IDA debt and the IMF reserves support are included in published measures of debt stock.

39. The Aid Management Unit within the Ministry of Finance will work to ensure better management of grants and off-budget aid programs ongoing in Liberia. As part of this effort we will:

a. Introduce new aid management software to track aid projects; eventually this will be rolled out to a public facing platform which will allow donors to log in and include and edit their ongoing projects.

b. Introduce a system by end-2012 to follow up on conditional grant aid: the grants which are tied to specific conditions will be identified with responsible Ministries and Agencies and will be required to provide monthly reports on progress and correcting measures to reduce future deviations.

40. We are making progress towards the WTO accession: we have submitted answers to initial questions the WTO has sent in response to our memorandum on foreign trade; and have begun technical meetings with the WTO. ECOWAS trade: the Government will work to implement the Common External Tariff (CET) by early next year, and work to remove the final tariffs on internal ECOWAS trade in line with the liberalization scheme. The CET will then form the basis for the negotiations with the WTO.

41. The CBL will implement the recommendations of a safeguards assessment that was finalized in October 2011 and will undergo an update assessment in relation to the new arrangement. In this context, we will finalize by December 2012, a Memorandum of Understanding between the CBL and the government to clarify the rights and obligations for Liberia's accounts and transactions with the IMF. These formalized institutional arrangements will be reflected in the CBL financial statements beginning with the 2012 annual accounts.

E. Other Structural Reforms

42. Concessions: we will strengthen the role of the National Bureau of Concession within negotiations and ensure it has the resources to operate effectively; and we will redraft the Petroleum Act to separate responsibility for revenue collection, oversight and regulation; and ensure that petroleum agreements are in line with the redraft. The revised Petroleum Act will be submitted to Parliament in the first quarter of 2013.

43. Risk analysis in the budget: the Government will begin producing a risk management handbook, with details of likely risks to budget execution revenue collection and debt levels. The Government will begin publishing regular reports of risk, and monitoring the risks presented to the overall macro economy.

44. Data collection and forecasting: we will expand the Government's data collection. As we recognize the importance of good data in the implementation of effective policies, measures we will take to improve data gathering will include:

a. Ensuring LISGIS has the required resources in FY 2013 to complete the planned national accounts surveys, providing us with the data required for Government policy development.

b. Commencing the household income expenditure survey and compile and publish the establishment survey (covering all registered business enterprises), both by end-June 2013 (structural benchmarks) as this is an integral part of the efforts towards better data collection and we will ensure that we work with donors to complete this.

c. Compiling national accounts for 2013 by June 2014 using the results of the completed household income expenditure and enterprise surveys.

F. Program Monitoring

45. Program implementation will be monitored with quantitative financial targets and structural benchmarks (Tables 1 and 2 below), and semi-annual reviews. Definitions of key concepts and indicators, as well as reporting requirements, are set out in the accompanying Technical Memorandum of Understanding. The first review is scheduled to be completed by May 15, 2013 based on the end-December 2012 PC and the second review by November 15, 2013 based on the end-June 2013 PC.

Table 1. Liberia: Proposed Quantitative Performance Criteria and Indicative Targets, 2012–13
(Millions of US dollars, unless otherwise indicated)

	Dec. 12	Mar. 13	Jun. 13	Sep. 13
Performance criteria 1/2/				
Floor on total revenue collection of the central government	203.0	325.7	460.0	120.3
Ceiling on new external arrears of the central government (continuous basis)	0.0	0.0	0.0	0.0
Ceiling on new non-concessional external debt of the public sector (continuous basis) 3/	0.0	0.0	0.0	0.0
Ceiling on new domestic borrowing of the central government 4/	15.0	15.0	15.0	15.0
Floor on CBL's net foreign exchange position 4/, 5/	210.0	207.0	226.0	226.0
Ceiling on CBL's gross direct credit to central government 4/	290.0	290.0	270.0	270.0
Indicative Targets				
Ceiling on gross borrowing by the public sector in foreign currency 6/	126.7	126.7	126.7	126.7
Ceiling on net domestic assets of the CBL 4/5/	-10.0	-19.0	-12.0	4.0
Ceiling on new domestic arrears/payables of the central government (continuous basis)	0.0	0.0	0.0	0.0
Floor on social and other priority spending (percent of total budgeted expenditure, excluding contingencies) 7/	30.0	30.0	30.0	30.0
Memorandum items:				
Memorandum item: Programmed receipt of external budget support and committed external financing 2/	4.4	…	49.8	…

1/ Test dates for performance criteria at end-December 2012 and end-June 2013, otherwise indicative targets.

2/ Fiscal targets are cumulative within each fiscal year (July 1-June 30).

3/ Non-concessional financing will be adjusted by amount of agreed non-concessional borrowing tied to projects independently evaluated as of high economic return.

4/ Bridge financing from the CBL is available under the program for shortfalls in programmed receipt of external budget support and committed external financing up to a maximum of US$20 million. In this event, floors will adjust downwards and ceilings adjust upwards by the extent this financing is utilized, up to a maximum of US$20 million.

5/ Includes SDR holdings net of ECF liabilities. SDR holdings converted at program exchage rate of 1 SDR=1.5844 US dollar.

6/ Three-year average annual ceiling.

7/ Includes spending on education, health care, social development services, and energy.

Table 2. Liberia: Proposed Structural Benchmarks, 2012–13

Measure	Target Date	Justification
Enhancing national accounts statistics		
Commence Household Income Expenditure Survey.	Second Review	Survey needed to validate national accounts data needed for macroeconomic policy.
Compile and Publish Results of Establishment Survey	Second Review	Survey results needed to validate national accounts data needed for macroeconomic policy.
Enhancing budget programming, control and monitoring		
Set up the state owned enterprises (SOE) Unit at Ministry of Finance.	First Review	Improve monitoring of public sector contingent liabilities and total public sector borrowing.
Reporting by 8 largest State Owned Enterprises (SOEs) on their financial performance to the SOE unit at Ministry of Finance for the quarter January–March 2013.	Second Review	Improve monitoring of public sector contingent liabilities and total public sector borrowing.
Fully connect the General Auditing Commission (GAC) to the Integrated Financial Management Information System (IFMIS) giving GAC full access to IFMIS.	First Review	Improve expenditure control for effective budget implementation.
Set up the Treasury Single Account approach at Ministry of Finance.	First Review	Move towards stronger central government liquidity management to reduce idle balances at line ministries and agencies accounts.
Create the Resource Revenue Unit in the Large Tax Payers Unit in the Ministry of Finance.	Second Review	Support effective taxation of the natural resource sector.

Improving capital spending execution and curbing current expenditure		
Establish Project Management Office (PMO) at Ministry of Finance	First Review	Monitor progress in capital spending associated with PRS2 and debt sustainability.
Introduce the Civil Service Management (CSM) module within IFMIS and the Human Resource Management Information System (HRMIS) sub-module within the CSM.	Second Review	Reduce payments to ghost workers and increase fiscal space for capital investment.
Complete clean-up of payrolls of 7 remaining Ministries and Agencies (M&As) and upload payrolls of all M&As to IFMIS	Second Review	Reduce payments to ghost workers and increase fiscal space for capital investment.
Developing the financial sector		
Issue government treasury bills.	First Review	Support financial market development and add a liquidity management tool to the central bank, and for treasury cash management purposes.
Establish a collateral registry at CBL	Second Review	Support more secure lending practices and prevent borrowers from contracting loans from multiple banks based on the same collateral.
Submit to legislature a revised Insurance Act	Second Review	Streamline regulation in the insurance sector and establish the central bank as the sole regulator of all insurance agencies.

Attachment II. Technical Memorandum of Understanding

This memorandum sets out the understandings between the Liberian authorities and the International Monetary Fund (IMF) regarding the definitions of the quantitative and structural performance criteria and benchmarks for the three-year Extended Credit Facility (ECF), as well as the reporting requirements. The definitions are valid at the start of the program but may need to be revisited during the program reviews to ensure that the memorandum continues to reflect the best understanding of the Liberian authorities and the IMF staff in monitoring the program.

I. QUANTITATIVE PERFORMANCE CRITERIA AND BENCHMARKS

A. Test Dates

1. Quantitative performance criteria have been set for end-December 2012 and end-June 2013 and quantitative performance benchmarks have been set for end-March 2013 and end-September 2013.

B. Definitions and Computation

2. **For the purposes of the program**, **the Government is defined as the Central Government of Liberia (GoL)**. This definition excludes legally autonomous state-owned enterprises whose budgets are not included in the central government budget. The operations of the central government will be presented in U.S. dollars with all revenues and expenditures that are denominated in Liberian dollars converted at the end of period exchange rate. The public sector comprises the central government, the Central Bank of Liberia, and public enterprises (enterprises and agencies in which the government holds a controlling stake—typically owns more than 50 percent of the shares, but which are not consolidated in the budget).

3. **Total Central Government revenue collection** includes all tax and nontax receipts transferred into the U.S. dollar GoL accounts at the CBL, including income and transfers from state-owned enterprises and public institutions (excluding external loans and grants). The GoL accounts at the CBL include the GoL General Account No. 2, the GoL Special Rice Fund, and the Liberian dollar account at the CBL comprising the GoL General Account. Any new accounts opened by the GoL at the CBL or at any other local financial agency shall be reported to the IMF as well. For the purposes of the program, the revenues of the GoL are measured on the basis of cash deposits in the four accounts specified above converted to U.S. dollars using the end of period exchange rate.

4. **For end-December 2012 and end-June 2013**, **social and other priority spending is defined as education, health, social development services, and energy sector spending** from the FY2013 budget of the units listed below (payment vouchers approved by the Ministry of Finance) excluding contingent expenditure. It is evaluated as a share of total budgeted expenditure, where total budgeted expenditure excludes contingent expenditure and off budget expenditure.

Education, Health, Social Development Services, and Energy Spending

	End Dec. 2012	End June 2013
Total Education and Health		
Education		
Ministry of Education		
University of Liberia		
Monrovia Consolidated School System (MCSS)		
Lofa Community College		
Nimba Community College		
Booker Washington Institution (BWI)		
Gbarnga Central High		
Forestry Training Institution (FTI)		
Cuttington University (CUC)		
National Commission on Higher Education (NCHE)		
W. V. S. Tubman Technical College (WVSTC)		
West African Examination Council (WAEC)		
Liberia Institute for Public Administration		

Education, Health, Social Development Services, and Energy Spending (concluded)

	End Dec. 2012	End June 2013
Health		
Ministry of Health and Welfare JFK Medical Center (JFKMC) Phebe Hospital LIBR Jackson F. Doe Medical Hospital		
Social Development Services		
Energy Sector		
Thermal diesel (HFO) power station Transmissions and distribution Mount Coffee rehabilitation, transmission, and distribution to Bushrod Island		

5. Social and other priority spending will be adjusted downward by the undisbursed amounts from budgeted external financing allocated to projects in the energy sector within the public sector investment program.

6. **New domestic borrowing of the Central Government** is defined as new domestic claims on the central government since the start of the program. It will be measured by the change in the stock of all outstanding claims on the central government (domestic loans, advances, and any government debt instruments, such as long-term government securities issued in the domestic market) by the banking system. The definition also includes the issuance of debt instruments by the GoL to the nonbank sector. For the purposes of measurement, all claims in Liberian dollars will be converted at the end of period exchange rate.

7. **Gross borrowing by the public sector in foreign currency** is defined as cumulated new external claims by residents and non-residents from July 1, 2012 on the public sector excluding borrowing for reserve management purposes by the CBL.

8. **The definition of external debt by the public sector,** for the purposes of the program, applies not only to the meaning set forth in point No. 9 of the "Guidelines on Performance Criteria with Respect to External Debt" (Executive Board Decisions No. 6230-(79/140) August 3, 1979, as amended and effective December 1, 2009 attached in Annex I), but also to commitments contracted or guaranteed for which value has not been received.

9. **The concessional nature of debt** will be determined on the basis of the commercial interest reference rates published by the Organization for Economic Cooperation and Development (OECD). A debt is defined as concessional if, on the date of signature, the ratio between the present value of debt computed on the basis of reference interest rates and the face value of the debt is less than 65 percent (equivalent to a grant element of at least 35 percent).

10. **The ceiling for contracting and guaranteeing nonconcessional external debt by the public sector will be set at zero continuously throughout the program period except as agreed with Fund staff**. The ceiling for contracting and guaranteeing nonconcessional debt excludes short-term (debt contracted for the period less than one year) import-related credits, rescheduling arrangements, and borrowing from the Fund.

11. **The government undertakes not to incur payments arrears on external debt that it owes or guarantees**, with the exception of external payments arrears arising from government debt that is being renegotiated with creditors, including Paris Club creditors. Arrears on external debt are defined as any unpaid obligation on the contractual due date. In cases where a creditor has granted a grace period after the contractual due date, arrears are incurred following the expiration of the grace period.

12. **New domestic arrears/payables of the government** are calculated as the difference between government payment commitments and the actual payments made on such commitments, providing for a processing period of no more than 15 days from the date of commitment. Actual payments are defined as having taken place on the date of issuance of the checks by the Ministry of Finance. Government payment commitments include all expenditure for which commitment vouchers have been approved by the Director of the Bureau of General Accounting (BGA), and expenditure that are now automatically approved, namely, wages and salaries, pensions, debt payments to the CBL and commercial banks, CBL bank charges, and transfers of ECOWAS levies into the ECOWAS account.

13. **CBL gross direct credit to central government** is defined as the sum of claims on central government, including loans, advances, accounts receivable, and any government debt instrument as defined in the monetary survey template excluding CBL purchases of treasury bills in the secondary market and non-competitive purchases in the primary market. The gross

credit to government is expressed in U.S. dollars. Claims denominated in Liberian dollars are valued at end-of-period exchange rate.

14. **The net foreign exchange position of the CBL** is defined as the difference between (a) the CBL's gross foreign reserves including SDR holdings, and (b) the sum of its gross foreign liquid liabilities, ECF arrangement liabilities, and liquid liabilities denominated in U.S. dollars. The net foreign exchange position floor at end-December 2012 and end-June 2013 is US $15 million below the projected net foreign exchange position. The net foreign exchange position of the CBL is presented in the U.S. dollar. SDR holdings are valued at a fixed rate of the U.S. dollar against SDR, 1.5844 as of June 30, 2012. Other currencies are valued at cross-rates against the U.S. dollar as of June 30, 2012.

15. **The net domestic assets of the CBL** are defined as base money minus the net foreign assets of the CBL converted into United States dollars at program exchange rates as defined in paragraph 14. Base money is defined as the stock of currency in circulation plus reserve deposits of commercial banks at the CBL, plus sight deposits of commercial banks at the CBL and plus vault cash of commercial banks. The net foreign assets of the CBL are defined as foreign assets minus foreign liabilities of the CBL balance sheet.

16. **External financing adjustor**. The program ceilings for CBL gross credit to government and CBL net domestic assets will be adjusted upward and the program floor on the net foreign exchange position of the CBL will be adjusted downward, by the amount of the difference between actual and programmed external budget support and committed budgeted external loan disbursements up to a maximum of US$20 million. The adjuster will be calculated on a cumulative basis from the start of the financial year (July 1).

Cumulative Program External Budget Support and Committed Budgeted External Loan Disbursements

(In millions of U.S. dollars)

September 2012	0.0
December 2012	4.4
March 2013	16.6
June 2013	49.8

II. PROGRAM MONITORING

A. Data Reporting to the IMF

17. To allow monitoring of developments under the program, the Ministry of Finance will coordinate and regularly report the following information to the staff of the IMF:

- Detailed reports on monthly core and contingent revenue and expenditure on both a cash and a commitment basis by budget line and a completed summary table on central government operations (monthly, within three weeks after the end of the month);
- Outstanding appropriations, allotments and commitments, and disbursements for line ministries and agencies (monthly, within three weeks after the end of the month);
- Disbursements of budget support grants and budgeted and off-budget loans, by donor (monthly, within three weeks after the end of the month);
- End-month balances in the GoL accounts at the CBL. These comprise the U.S. dollar accounts: GoL General Account; and GoL Special Rice Fund; and Liberian dollar accounts: the GoL/CBL Civil Servant Payroll Account, and the GoL General Account. Any new accounts opened by the GoL at the CBL or at any other local financial agency shall be reported to the IMF also (monthly, within three weeks from the date of the statement);
- End-of-month balances of all operating and other accounts of the line ministries and agencies receiving budgetary appropriations (monthly within three weeks after the end of the month);
- A table providing the end-of-period stock of domestic arrears accumulated and payments made on arrears during the program period, by budget category (wages, goods and services, etc) (monthly, within three weeks after the end of the month);
- The amount of new external debt contracted or guaranteed by the public sector (monthly, within three weeks after the end of the month);
- The amount of new domestic debt contracted or guaranteed by the public sector (monthly, within three weeks after the end of the month);
- A detailed report on monthly payments on external debt by category and creditors and the stock of external debt (monthly, within three weeks after the end of the month);
- A detailed report on monthly payments on domestic debt by category and the domestic debt stock (monthly, within three weeks after the end of the month);

- The balance sheet of the CBL in the monthly monetary survey (monthly, within three weeks after the end of the month);

- The full monthly monetary survey of the monetary sector (monthly, within three weeks after the end of the month);

- The detailed table of commercial banks loans and advances by sector (monthly, within three week of end of month);

- The core set of financial soundness indicators for the banking system, including the overall profitability of the banking sector (quarterly, within three weeks after the end of the quarter);

- The report on the results of foreign exchange sales/purchases by the CBL through foreign exchange auctions held by the CBL (weekly) and other currency exchange facilities;

- Regular sale of U.S. dollars by the Ministry of Finance to the CBL, including amount date, and rate of exchange (monthly, within three weeks after the end of the month);

- Indicators of overall economic trends, including but not limited to:

  - detailed tables of the monthly harmonized consumer price index (within three weeks after the end of the month);

  - daily foreign exchange rates (monthly);

  - export volumes and values by major commodity, import values by standard international trade classification (SITC), import volumes of rice (by commercial and noncommercial use) and petroleum products (monthly, within three weeks after the end of the month);

  - interest rates and commercial bank remittance inflows and outflows (monthly, within three weeks after the end of the month); and

  - production data in value and volume (monthly, within six weeks after the end of the month);

- Quarterly reports of state owned enterprise financial operations submitted to Ministry of Finance;

- The report on the status of implementation of the structural performance criteria and benchmarks specified in Table 2 of the MEFP (monthly, within three weeks after the end of the month).

18. The above data and reports will be provided in hard copies and electronically to the IMF Resident Representative to Liberia, with copies to the local IMF economist, Mr. Deline (adeline@imf.org) for further transfer to the African Department of the IMF in Washington, D.C.

19. Moreover, we will provide the Fund with such information as the Fund requests in connection with the progress in implementing the policies and reaching the objectives of the program.

Annex 1. Guidelines on Performance Criteria with Respect to External Debt

Excerpt from Executive Board Decision No. 6230-(79/140) August 3, 1979, as amended in 2009

(a) The term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

(i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. The debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(b) Under the definition of debt set out in point 9(a) above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

INTERNATIONAL MONETARY FUND

LIBERIA

November 2, 2012

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION AND REQUEST FOR THREE-YEAR ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY–BACKGROUND NOTES

CONTENTS

MANAGING NATURAL RESOURCE REVENUE IN LIBERIA: OPTIONS FOR A FISCAL FRAMEWORK[1]

1. With Liberia set to rejoin the group of countries with large mineral sectors, it is an appropriate time to consider how the fiscal framework should manage these revenue inflows. What principles should guide whether the revenues are spent or saved? How should spending be allocated across consumption and investment? How will Liberia manage volatility and uncertainty in its fiscal framework? Should savings and/or stabilization funds be created? How well have other countries managed their resource revenues?

2. This note aims to highlight the issues rather than provide definitive answers: there is no "one-size fits all" in the design of fiscal frameworks which should be tailored to country circumstances. The note is organized as follows. Section I summarizes the benefits and risks resulting from large natural resource revenue inflows; Section II outlines the challenges to fiscal policy posed by resource revenues. Section III discusses a menu of policies for managing resource wealth including experiences from Ghana and Botswana and an application of the permanent income approach.

I. CONTEXT

3. **Liberia should receive large natural resource revenue inflows over the medium- to long-term**. These will originate through exploitation of iron ore deposits and, potentially, petroleum. Revenue inflows of this magnitude offer significant opportunities, including accelerated reconstruction, development, and poverty reduction. Projections made at the time of the 2010 Article IV consultation indicated that an optimistic extraction schedule for four of the ratified iron ore projects could yield sufficient resources to finance Liberia's transition to middle income status by 2030.

4. **However, without proper management and preparation, there is a risk that the economic benefits of mineral wealth would be undermined or even dissipated**. Studies indicate that several factors associated with dependence on mineral wealth such as loss of competitiveness in agriculture and manufacturing, macroeconomic volatility, and diversion of resources to rent-seeking (Box 1).

[1] Prepared by Geoffrey Oestreicher and Kareem Ismail with input from Lamin Leigh and Enrique Gelbard (all AFR) and Chris Lane (SPR).

Box 1. The "Resource Curse"

The main negative aspects associated with natural resource wealth:

- **Dutch disease (loss of competitiveness)**: Large protracted foreign exchange inflows enter the country, bidding up the price of non-traded goods and appreciating the real exchange rate. Competitiveness declines, resources migrate to the now more profitable non-traded services sector and away from non-mineral tradable sectors.[1] In the process, the agricultural and manufacturing sectors, the mainstay of employment, decline.

- **Volatility**: International resource prices are channeled via budget to the domestic economy. If expenditure rises in years of high resource prices, then falls abruptly when prices reverse, fiscal policy becomes pro-cyclical. The resulting cycle of "boom and bust" can entail real macroeconomic and fiscal costs.

- **Governance and institutions**: Abundant natural resource revenue may engender institutionalized corruption. Capture of decision making by elite groups can lessen the incentives—even create disincentives—for development of the institutions needed for broad-based growth. Revenue institutions do not develop to their full potential. Growth suffers further as resources are increasingly diverted from productive purposes towards rent seeking.

[1] See Mastuyama (1991) and Krugman (1995) for theoretical treatment, and Ismail (2010) for empirical evidence on the Dutch disease.

II. CHALLENGES TO FISCAL POLICY IN RESOURCE-RICH ECONOMIES

5. **The presence of significant resource revenue complicates fiscal management in several respects**: (i) revenue derives from depleting an asset unlike most other revenue which has implications for the sharing of wealth between current and future generations; (ii) spending resource revenue (from exports) pumps up domestic demand and may in turn generate inflation; (iii) revenue windfalls may strain the capacity of public financial management leading to waste; and (iv) revenue volatility can be damaging if there are not some savings to smooth changes to budget spending.

6. **Conceptually, mineral wealth is an asset in an economic sense, rather than a recurrent flow**. Mineral wealth, when extracted, can be transformed into financial assets (saved), tangible assets (investment), or fund current consumption (liquidation).

7. **Intergenerational equity**. Recognition of resources as an asset raises intergenerational equity issues. For example, arguments can be made that future generations would be better provided for by leaving part of the resource in the ground, by building up financial assets, or by transforming the resource into other growth enhancing assets such as infrastructure or human capital. Choices made here will have important ramifications for the fiscal policy strategy and stance going forward.

8. **Macroeconomic stabilization**. Movements in resource revenues due to price fluctuations affect the domestic economy primarily through public spending.[2] If spending adjusts to the variation in revenue, the overall fiscal balance will remain unchanged but the level of domestic demand would clearly be altered.

9. **Scaling up spending with capacity constraints**. In capital scarce economies, such as Liberia, a good argument can be made to spend resource revenues on growth-enhancing investments. However, a sudden influx of resource revenue can strain national capacity, making it difficult to spend funds in an efficient, transparent manner. Systems, including PFM systems, may not be able to handle the new revenue volumes. Wasteful and non-productive expenditure may result unless capacity shortfalls are addressed in a prioritized manner. Where constraints are binding, a more gradual scaling up of expenditure may be warranted.

10. **Revenue volatility**. With weak access to international capital markets, fiscal buffers, i.e., savings, would be necessary to allow expenditure smoothing when there are large changes in resource revenues.

III. FISCAL FRAMEWORK OPTIONS

11. The fiscal framework needs to take account of these abovementioned challenges with a policy rule or guideline to anchor fiscal policy around an appropriate indicator (Box 2). Importantly, the anchors used in resource intensive countries frequently differ from those employed in countries lacking natural resources.

[2] But other channels exist as well. For example, higher prices might call forth more accelerated extraction which could affect domestic demand through greater economic activity at the mine site and through the value chain. Wealth effects could also play a role.

Box 2. Fiscal Indicators for Natural Resource Intensive Countries

The choice of fiscal indicator is critical for the adoption of a fiscal rule or guideline.

The **overall balance** is used in many countries without natural resources in fiscal rules or guidelines to limit borrowing and assess fiscal vulnerability, including Liberia. However, in a resource dependent country the overall balance can improve with a fiscal expansion if an increase in spending is less than the increase in resource revenue,
i.e., it encourages or disguises pro-cyclical fiscal policy.

The **non-resource balance** (the overall balance minus net resource revenue) preferably scaled to non-resource GDP is the key fiscal indicator in resource dependent economies. It measures the government impact on domestic demand and the injection of exported resource revenue into the economy.

The **current balance** excludes public investment from the overall balance. A practical drawback is that it fails to provide a clear anchor for fiscal policy.

12. **The main practical challenge for Liberia is directing the income flows from exhaustible natural resources towards investment (in both physical and human capital) while building buffers to cushion against shortfalls in resource income**. Countries with different institutional capacities and economic structures have opted for varying policy frameworks. These frameworks generally rely on fiscal rules or guidelines to finance development while building up some savings in stabilization funds and sovereign wealth funds or reserve funds. There are many frameworks in use and selected country experiences are considered next (Appendix I summarizes some country examples).

A. Price Based Rules: Chile, Mongolia, Nigeria and Ghana

13. **Price-based rules aim to smooth the usage of resource revenues**. They explicitly tackle resource price volatility. They set commodity reference prices by using a formula (such as a moving average as in Mongolia) or set by an independent panel (Chile). Revenues in excess of those expected at the reference price are saved in a stabilization fund (e.g., the excess crude account in Nigeria) and conditions are set to draw down in the case of shortfalls of revenues. By setting the price conservatively, or by other supplementary rules, longer term savings could also be incorporated into a price-based rule as is the intention in Ghana.

14. **Ghana's petroleum revenue legislation directs most petroleum revenue towards investment with some financial savings for future generations and for stabilization purposes**. Expected revenue is calculated using a 7 year average of the oil price (benchmark

price). All revenues are collected in a petroleum account which directs 70 percent of the oil revenue calculated at the benchmark price to the budget and the remainder is split between a stabilization fund and a heritage fund for intergenerational equity. Out of the funds directed to the budget about 70 percent is allocated towards long-term public investment based on national development plans and the remaining 30 percent is non-allocated spending. The petroleum act defines the conditions for the government to tap into the stabilization fund for resources. The stabilization fund covers up to 75 percent of budget shortfalls due to petroleum revenue fluctuations.

15. **The emphasis on domestic investment is appropriate if channeled towards projects with high return, but may raise efficiency issues**. Targeting a fixed share of resource income in capital spending can overwhelm administrative capacity and result in poor project execution during resource booms. Moreover, the fixed share implies volatility in capital expenditure, which may complicate accounting while making project budgets vulnerable to resource price shocks.

16. **There have been challenges in implementation**. Under the Petroleum Revenue Management Act (PRMA), the budget should be based on a crude oil reference price for each year. In 2011, the crude oil reference price was set at US$/bbl 70. It was later revised in a supplementary budget to US$/bbl 100: substantially reducing higher-than-expected petroleum revenue to be placed in the petroleum funds (stabilization and heritage). Without political will to resist such revisions, implementation can go astray.

B. Fiscal Rules on Expenditure: Botswana (since 1994)

17. **Botswana—a diamond exporter— utilizes a fiscal rule, known as the Sustainable Budget Index (SBI)**. The SBI stipulates that the ratio of government expenditure, excluding development spending and recurrent spending on health and education, to non-mineral revenues should be less than one. This rule is meant to prevent the use of resource income to directly boost wages and subsidies. It directs resource revenue towards development and human capital spending (health and education) with the remainder directed to the Pula Fund, which acts as both a sovereign wealth fund and a stabilization fund. In addition to SBI, Botswana has an expenditure target equivalent to around 30 percent of GDP.

18. **Botswana's adherence to the SBI fiscal rule has enjoyed mixed success**. The SBI fell below unity immediately after its introduction in 1994/95. The SBI exceeded unity in 2001/02, when exceptionally high custom duty revenues during 1999/00–2000/01 came to an end. In 2003/04, however, measures to raise domestic revenue, coupled with across the board cuts in all expenditures, resulted in a dramatic fall in the SBI.

19. **As in Ghana's case, the combination of the SBI with the expenditure target has some limitations**. It can result in high volatility in capital expenditure and social spending, and may result in inefficiencies when administrative and absorptive capacities are limited. At the same

time, the Pula Fund has provided a buffer for the budget, notably during the 2009 financial crisis when diamond production was halted temporarily.

C. Permanent Income (PI) Approach: Norway, Timor Leste, South Sudan

20. **While there are a number of variants of the permanent income approach, the basic principle is that consumption is limited to the actual or imputed income from saving current and future resource revenues**. In the case of Norway, petroleum revenues are saved in a sovereign wealth fund, and spending of these revenues is limited to 4 percent of the stock of assets in the Fund, i.e., the assumed long term rate of return. A variant of the PI approach, known as the annuity approach, is used in Timor Leste. The non-oil fiscal balance is set in line with estimated sustainable income (ESI), which is calculated annually as 3 percent of the sum of the petroleum fund balance and the present value of expected future petroleum receipts. Deficits can exceed the ESI if properly justified and approved by Parliament. A more extended discussion of the PI approach is contained in Annex II, while Annex III illustrates the application of the PI approach in Liberia using the annuity approach.

21. **A permanent income approach would have some advantages over structural budget rules including those applied in Ghana and Botswana**:

- it limits pro-cyclicality in fiscal policy;
- it may be more difficult for governments and pressure groups to deviate from the established rules for reasons of short-term expediency;
- it may provide a sustainable long-term fiscal framework to support the development strategy;
- it may provide additional impetus and justification for forming budgets within a medium-term framework, improving project identification and execution, and concession monitoring.

22. **However, the PI approach also has some significant limitations**:

- The spending path in the annuity approach could change dramatically from year to year if prices are volatile or new reserves identified (Annex III, Figure 3);
- There is a limited focus on short term issues, such as the impact of fiscal policy on demand, inflation and growth;
- The PI approach is consumption-based and thus silent on how capital scarce countries should allocate resources towards critical social spending and high-yielding projects,

especially when access to international capital markets is limited.[3] For example, if the return on domestic investment is higher than the return on foreign saving, then a better economic outcome can be achieved by increasing the expenditure path above that implied by the PI approach.

IV. CONCLUSIONS AND POINTS FOR DISCUSSION

23. **Fiscal frameworks (rules and guidelines) need to change to meet the challenges of large resource revenues**. While resource revenues are not yet large in Liberia, there is a reasonable argument that the institutional framework should be in place in advance so that the revenues are used most productively. Another argument is that once revenue starts flowing, vested interests would resist institutional change.

24. The price-based or structural rules have an explicit focus on coping with volatility, which may be useful in the Liberian context.

25. The permanent income approach is useful in assessing the sustainability of fiscal policies and elements of it, such as targeting the non-resource fiscal balance, can help sustain long term fiscal viability. However, permanent income estimates are very sensitive to export price projections and are thus too volatile to provide a tractable policy benchmark in the case of Liberia. Moreover, given the massive infrastructure needs and the limited access to international capital markets, Liberia is in need of policies that direct mineral wealth to public investment, which lies outside the PI approach's primary focus on consumption.

[3] See Collier et al. (2010).

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Annex I. Fiscal Frameworks in Resource Intensive Countries

(From Fiscal Frameworks for Natural Resource Intensive Developing Countries, IMF 2012 (forthcoming)

Country	*Rule PIH*	*Framework Non-PIH*	*Resource Fund 1/*	*Description*
Azerbaijan	X		R	A non-oil balance guideline (2004) consistent with constant real consumption out of oil wealth. Never observed. More recently reliance on ad-hoc balanced budget oil price. Complemented by state oil fund.
Chile		X	F	Structural balance guideline (institutionalized in 2006 fiscal responsibility law). Adjustment by long-term price of copper and molybdenum (10-year forecast) as determined by an independent committee. Targets can be changed over time. Supported by two funds (stabilization and savings).
Ecuador		X	R	Various rules (e.g., non-oil balance, expenditure growth) over time. More recent rule states that current spending can only be financed by non-oil revenue (a sort of “non-oil golden rule”). Oil funds abolished in 2008.
Equatorial Guinea		X	R	Guideline establishing that current expenditures should be limited to non-oil revenue. CEMAC convergence criteria: include various fiscal targets (e.g., a non-oil balance target). It has a fund for future generations.
Ghana			R	A petroleum revenue management framework built around a stabilization fund and a heritage fund. Benchmark oil revenue is calculated at a 7-year moving average, with 70 percent used to finance the budget. Remaining revenue allocated in fixed proportions to the funds. No fiscal anchor limiting budget deficit.
Mongolia		X	R	A ceiling on the structural deficit with structural mineral revenues estimated using a 16-year moving average of mineral prices. Combined with a ceiling on expenditure growth defined by the non-mineral GDP growth rate (useful when structural revenue is growing fast). The structural balance target can be changed every four years. Flows to a stability fund linked to difference between actual and structural revenues.
Nigeria		X	R	3 percent of GDP deficit ceiling for federal govt. computed at budget oil price. Budget oil price set every year in political negotiations, including with sub-national governments. Excess crude account receives “windfall” revenues; ad-hoc withdrawals.
Norway	X		F	“Bird-in-hand” fiscal guideline: the cyclically adjusted non-oil central government deficit as 4 percent (the expected long-run real rate of return) of the SWF assets. Guidelines are flexible: temporary deviations permitted over business cycle or if large changes in SWF value.
PNG		X		5-year medium-term fiscal strategy that sets a ceiling to the non-mineral deficit in line with “normal” mineral revenue. A portion of “windfall” mineral revenue (70 percent) can be spent up to a non-mineral deficit ceiling of 8 percent of GDP.
Russia		X	R	The budget code includes a long-term nonoil deficit target of 4.7 percent of GDP. Annual budgets underpinned by rolling three-year medium-term fiscal frameworks. Two oil funds (stabilization and savings).
Timor-Leste	X		F	Fiscal guideline based on PIH framework (constant in real terms). Non-oil balance set in line with estimated sustainable income (ESI), which is calculated annually as 3 percent of the sum of the petroleum fund balance and the present value of expected future petroleum receipts. Deficits can exceed the ESI if properly justified and approved by Parliament.

1. **The majority of resource economies manage resource revenue in a less structured manner through stabilization and savings funds**. Both are essentially government accounts with distinct operating procedures and varying degrees of integration with the budget process:

- Stabilization funds seek to stabilize resource revenues over time, but are non-accumulative as they seek to balance inflows and outflows over a cycle. A typical methodology is to establish a benchmark price of output as an approximation of a medium- to long-term average price. On the sale of output, the portion of the revenue corresponding to the benchmark price is transferred to the budget for spending, with the excess accruing to the fund. Should the actual price be less than the benchmark, the fund would subsidize the budget by the amount of the shortfall. Under such a mechanism, the fund remains solvent provided the benchmark price is not set above the actual average price observed. The same stabilization function would be performed by funds based on the permanent income approach, as these are designed to maintain a stable non-resource fiscal balance.[1] Country examples include Chile, Papua New Guinea, and Venezuela.

- Savings funds seek to establish a surplus justified usually on the concept of intergenerational equity. These surpluses can be mandated in a variety of ways, for example by the discretionary setting the benchmark price below the actual price or saving a fixed percentage of receipts (Oman, Alberta), or through adherence to the permanent income approach as discussed in Annex I.

2. **Funds vary in the degree they are integrated into the budget process**. At one extreme are the Norwegian, Timor-Leste, and South Sudan funds which are essentially government accounts and institutional arrangements to fund the budget, accumulate savings, and report on activity. At the other extreme, funds in Kazakhstan, Azerbaijan, Iran and Kuwait have discretionary authority to expend resources outside the budget process. In the middle range, some funds are characterized by institutionalized mandates to support specified areas of the economy. In general, with the exception of developed countries, integrated funds tend to be more transparent and rules based. They also avoid the pitfalls of dual administrations, conflicting macroeconomic and expenditure policies, and cumbersome earmarking that have led to a poor track record of performance in many LICs and prevented conduct of a unified fiscal policy.[2]

3. **Legislation establishing a fund and defining its policy objectives, operational objectives, and operational rules can provide strong legal support for the long term fiscal strategy**. Policy objectives include securing macroeconomic stability, ensuring that future

[1] This latter stabilization method would be more relevant to Liberia as revenues from iron ore are less directly linked to output levels than they are in oil sector production sharing agreements.

[2] The argument has been advanced that giving a fund independent spending authority may create needed centers of bureaucratic efficiency in some LICs, but there is little evidence excellence for this.

generations benefit from the resource, enhancing transparency, and improving governance. Operational objectives are the means by which these policy objectives are achieved and may include smoothing the variation in resource revenues over time, building up financial assets, and reporting on operations of the fund. Operational rules are the mechanisms by which these latter objectives are affected, for example they could comprise rules on the division of resource revenues between the budget and savings in a given year; rules governing when funds are to be permanently sequestered for future generations; and rules specifying which reports need to be produced and on what time frame.

4. **Many attempts at ad hoc stabilization and savings funds failed for reasons of political economy and capacity constraints long before errors in measurement came into play**. There are numerous examples of resource producing countries being unable to resist expenditure pressures in the short term, sometimes liquidating mineral wealth to fund current spending (Venezuela, Nigeria). Moreover, with low capacity leading to poor expenditure decisions, attempts to transform mineral wealth into tangible productive assets have frequently led to inefficiency and waste (Ecuador, Nigeria).[3]

5. **Better management of natural resource revenue is correlated with good governance, better capacity, and strong public financial management**.[4] The resource curse appears most acutely in countries with underdeveloped capacity and poor systems of governance—intuitively, large revenue inflows would do the least good in countries where they are treated in a nontransparent manner, spent on wasteful projects or diverted to private use. General policy implications are to institute measures and reforms aimed at correcting these deficiencies, including through enhanced transparency and accountability, capacity development, and institutionalization of the reforms, preferably through legislation.

[3] The economic equivalence of mineral wealth, physical assets, and human capital presupposes government has sufficient capacity to identify and execute projects efficiently. In the absence of this capacity, spending mineral revenues can result in the destruction of wealth.

[4] See Aydin 2010, Collier (2008), Alayli (2005), and Sachs (1995).

Annex II. Permanent Income Approach

1. **What would fiscal policy look like in a resource rich economy if, over the medium- to long-term, it promotes growth, maintains macroeconomic stability, and preserves intergenerational equity**? The permanent income approach presented below is capable of accomplishing these three goals. However, there are sizable uncertainties involved that can complicate practical application.

2. **In the presence of significant resource revenue, macroeconomic stability is best attained by having the fiscal target set on the non-resource fiscal balance**. This reflects the preferred treatment of mineral wealth as an asset, similar in economic terms to financial wealth.[1] Use of the asset should, therefore, be conceptualized as a financing item in the budget.

Revenue (excluding resource revenue)
less
Total expenditure
equals
Non-resource fiscal balance
Financing:
Changes in net mineral wealth
Inflow of mineral revenue
Outflow of mineral revenue
Other financing

3. **In a resource economy, it is changes in the non-resource balance—not the overall balance—that reflects the impact on domestic demand from fiscal activity**. Maintaining macroeconomic stability would, therefore, generally require that governments avoid rapid changes in the non-resource fiscal balance, unless the intention is to provide a well thought out fiscal impulse to the economy. A transparent fiscal policy would, therefore, require that the budget and fiscal process provide readily available information on the non-resource balance so that demand forces in the economy and the underlying fiscal impulse can be clearly understood.

4. **The appropriate size of the non-resource fiscal deficit is linked to the issue of intergenerational equity**.

- **Intergenerational equity requires that the net present value (NPV) of government wealth be preserved over time**. Wealth is defined in an economic sense, where its actual form is variable—wealth starts out as the NPV of minerals in the ground, and is transformed through extraction and sale to financial wealth or human and physical capital.[2] Whatever the form, the value of wealth should theoretically be conserved so that it can deliver the same real rate of return each year.

- The implication is that the size of the non-resource deficit is limited over time to the permanent income generated by the mineral wealth. This does not, however, preclude

[1] In cases where resource revenue has resulted in a sizeable build-up of financial wealth, the appropriate fiscal target would be the *primary* non-resource fiscal balance. Note that with resource wealth treated formally as a financing item, the non-resource fiscal balances collapses to the overall fiscal balance.

[2] Assuming it is not expended in current consumption or destroyed through unproductive investment.

frontloading of expenditure for productive purposes—in capital-poor countries the marginal product of capital is high, implying that well designed and efficiently executed public investment may be the best use of funds. But the requirement of sustainability, and appropriate institutional arrangements, should force governments to better justify the front loading and to design fiscal policy that is sustainable within a longer term framework.

5. **While the permanent income approach is conceptually simple and intuitive, practical application can be complex and prone to error**. Accurate measurement of the base of the mineral wealth (the actual size and quality of the resource) is difficult. Technologies are changing—which can affect the cost and profitability of extraction, alter competitive advantage, and introduce a tail risk that advances in other areas may render the resource redundant. Future prices are even more uncertain—they are volatile in the short term, with past performance being a poor predictor of long-term trends. As overly optimistic estimates of mineral wealth can lead to unsustainable fiscal and debt positions, the need for a relatively conservative approach to estimation is indicated, with clear procedures in place to justify and alter them when necessary.

6. There are only a few countries explicitly applying the permanent income approach to resource revenue:

- South Sudan and Timor-Leste estimate the NPV of mineral wealth, and then allow the budget to use the estimated permanent income arising from this wealth in each year (rate of return multiplied by NPV of mineral wealth). Essentially, the permanent income from mineral wealth is set as the non-resource fiscal deficit.[3] As exploitation of the resource is a new phenomenon, this likely implies some front loading of expenditure, as assets in the funds are as yet insufficient to generate this level of income.

- Norway has taken a more conservative "bird in the hand" approach, in which the non-resource deficit in any year is largely limited to the real return on monetized mineral wealth already accumulated. As this calculation is not dependent on estimates of the value of resources in the ground, rates of return, or future prices, it is subject to less uncertainty, but at a cost of back loading expenditure in favor of future generations.

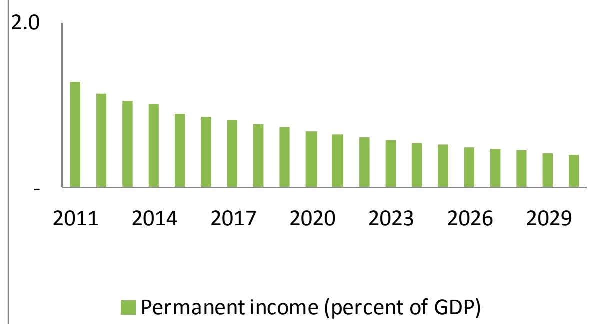
[3] Legislation in Azerbaijan also limits the non-resource (oil) deficit to the permanent income from oil wealth, but actual practice has deviated from this goal.

Annex III. Application of the Permanent Income Approach in Liberia

1. Application of the permanent income approach in Liberia would require long term adherence to a sustainable level of the non-resource deficit. This would not preclude frontloading the transformation of mineral wealth into productive assets through debt-financed investment. However, frontloading would need to be demonstrated to be consistent with macroeconomic stability with safeguards to support efficient expenditure and a sustainable debt position. Given current capacity constraints, in the short- to medium-term this would be best provided by borrowing only for well designed donor-supported and designed projects.

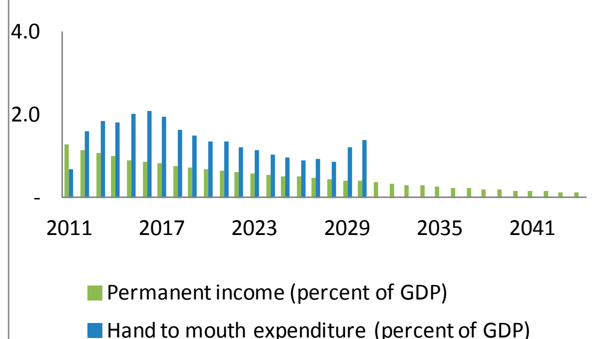
2. **As an illustration, the permanent income approach is applied to the projected revenues of the existing ArcelorMittal iron ore mine at Yekepa**. The present value (2011) of the future stream of revenues is estimated to be US $2.4 billion. The permanent income from this is calculated to be US $20 million per year at constant prices (in current prices the income would rise by inflation). Permanent income would be about 1.3 percent of 2011 GDP. As real GDP increases over time the permanent income relative to GDP would decline (Figure 1).

Figure 1. Liberia: Estimated Permanent Income from One Iron Ore project, 2011-30



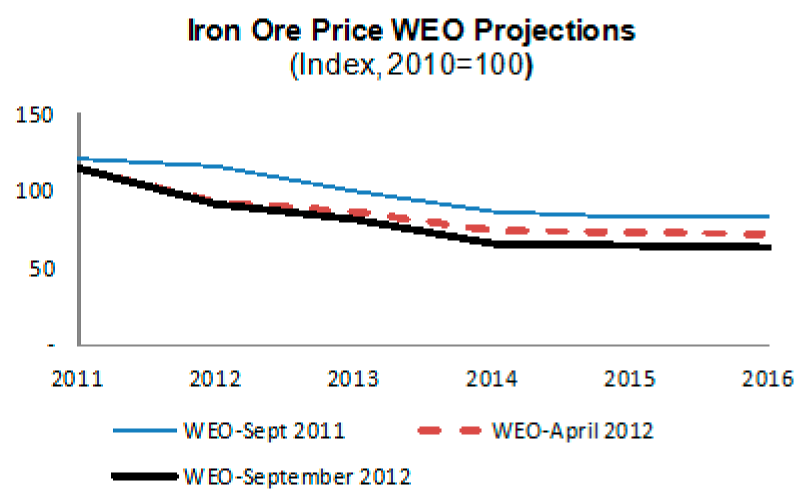
3. **Using the permanent income approach would set the non-resource deficit at the level of permanent income i.e. non-resource revenue less expenditure equals permanent income.** For comparison, a “hand-to-mouth” policy of spending all resource revenue as it is received (with no borrowing) would set the non-resource deficit as equal to the amount of resource revenue. The comparison of the permanent income approach to the “hand-to-mouth” approach shows both the stabilization and savings aspects of the permanent income approach (Figure 2). In initial years, spending would be higher in the permanent income approach, as meeting the non-resource deficit target would involve borrowing. As resource revenues rise, the permanent income approach would result in savings. When the resource runs out, there is no revenue and no spending in the hand-to-mouth approach, but spending equivalent to the permanent income

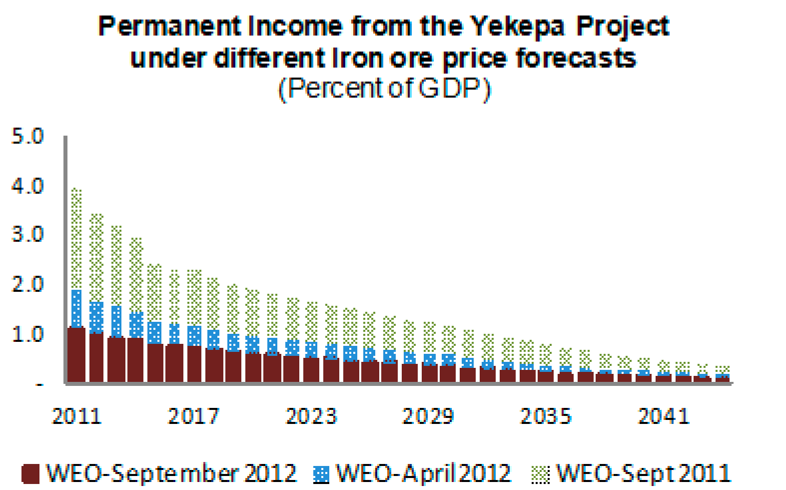
Figure 2. Liberia: Non-Resource Deficit Using Permanent Income and "Hand to Mouth" Approaches, 2011-44



continues out of income from past saving in the permanent income approach. Given current forecasts on iron ore prices, there is limited scope to frontload expenditure (the permanent income is less than "hand-to-mouth" by the second year); however, the permanent income is very highly sensitive to forecasts which highlights a key weakness of the methodology (Figure 3).

Figure3. Liberia: Volatility in the Permanent Income





Source: IMF staff estimates and World Economic Outlook.

DRIVERS OF NET INTEREST MARGINS AND BANK PROFITABILITY IN LIBERIA[1]

This note provides an analysis of regional drivers of net interest margins (NIMs)—the difference between interest income acquired by banks and interest costs paid on interest bearing liabilities such as deposits over total interest bearing assets. The analysis suggests that NIMs in Liberia are low when considering the high bank operation costs relative to peer countries. This may explain why indicators of profitability for Liberian banks are significantly lower than in the region.[2] This also suggests that the Central Bank of Liberia (CBL) should be mindful of the low bank returns when using moral suasion to lower bank lending rates as this may weaken the financial system while pressuring smaller banks out of the credit market. The note presents background on the Liberian banking system followed by an analysis of the determinants of net interest margins in the region and implications for Liberia.

BACKGROUND

1. **Bank profitability has been weak in Liberia** with returns on equity near zero or negative during 2003–11 due to:

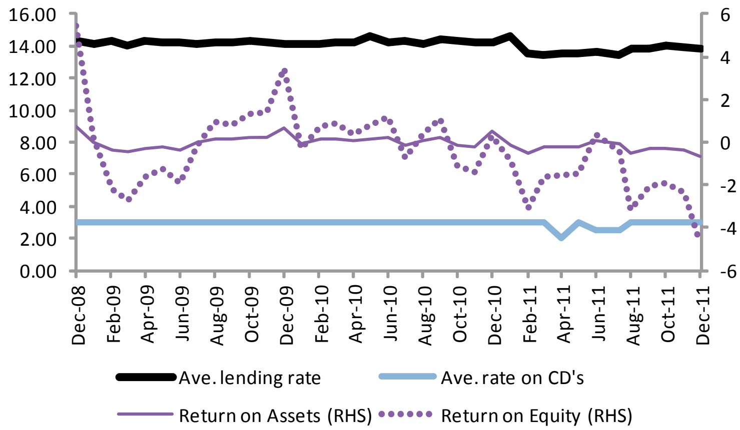
- A weak credit environment with limited supporting infrastructure (the lack of a credit reference system or credit bureau, no collateral registry, weak property rights, and limited legal enforcement on debt repayment);
- Capacity constraints at banks including poor internal controls and risk management;
- High costs of operation;
- Absence of a domestic fixed-income securities market to provide a secure investment instrument;
- Low returns on investment abroad or in foreign assets due to loose monetary policy in advanced countries (Banks are only allowed to invest in foreign assets with very short maturity and issued by top rated commercial banks and national authorities).

2. **Despite the anemic bank profitability bank lending and deposit rates have been relatively rigid**. While the increase in the number of banks may have played a role in containing lending rates through competition, Liberia's banking system is dominated by one bank holding about 50 percent of commercial bank demand deposits and lends around 40 percent of private sector credit.

[1] Prepared by Kareem Ismail (AFR).

[2] EBS/11/164 – Liberia- Staff Report for the Seventh Review under the Extended Credit Facility.

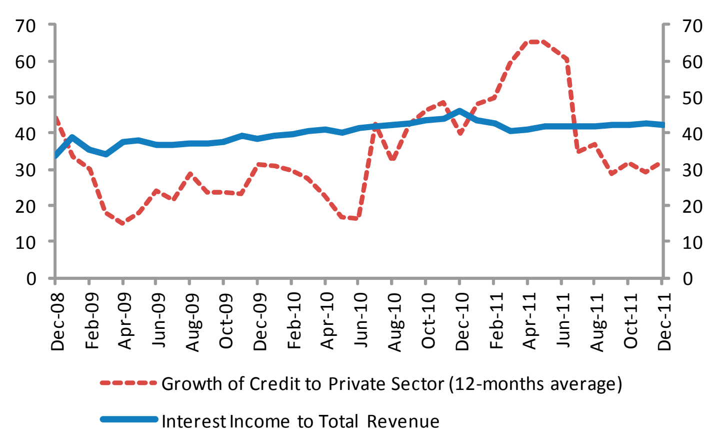
Lending and Deposit Rates in Liberia



Source: Central Bank of Liberia

3. **Despite a rapid increase in bank lending, interest income continues to play only a secondary role in bank revenue**. Non-interest income as share of revenue has remained above 50 percent declining by less than 10 percent over 2008–2011, while private credit growth averaged a brisk 34 percent per year over the same period.

Bank Income Source and Private Credit Growth



Source: Central Bank of Liberia and IMF staff estimates

REGIONAL DRIVERS OF NIMS

4. **The literature highlights high operational costs relative to assets and weak property rights as two dominant factors behind relatively high lending margins in sub-Saharan Africa**. We examine the drivers of NIMs in a dynamic panel of 86 banks across six ECOWAS

countries.[3] Property rights are generally and similarly weak within the region according to the World Bank CPIA ratings, which allows us to focus on the impact of operational costs on NIMs within the sample. We estimate the following two models using Generalized Method of Moments (GMM) and Ordinary Least Squares (OLS).

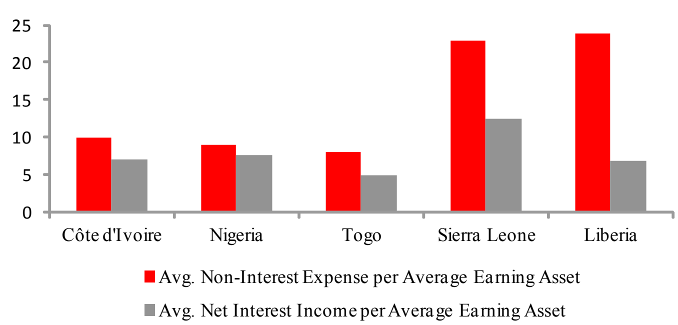
- $$NIM_t = \beta_1 NIEPA_t + \beta_2 X_{t-1} + \varepsilon_t \qquad (1)$$
- $$\Delta NIM_t = \gamma_1 \Delta NIEPA_{t-1} + \gamma_2 M_{t-1} + \upsilon_t \qquad (2)$$

We estimate equation (1) using system GMM–Blundell and Bond (1998) in Table (1) and equation (2) using system GMM–Arellano and Bond (1991) in Table (2), where NIEPA is non-interest expense as percent of average interest bearing assets and X and M are matrices of control variables. We also include OLS estimates for each model for robustness.

5. **Both GMM and OLS estimates show that high NIEPA is associated with higher NIMs across banks while lagged increases in NIEPA are associated with increasing NIMs within banks** (Tables 1 and 2). Moreover, decreasing lagged returns on assets (ROA) are strongly associated with increasing NIMs (Table 2), which is likely due to banks raising lending rates and cutting deposit rates when returns weaken.

6. **These results are difficult to reconcile with developments in net interest margins in Liberia**. Operational costs are high in Liberia with an average NIEPA for Liberian banks in the sample at 21 percent, which is more than one standard deviation above the sample mean of 11 percent. Costs are high in Liberia due to poor infrastructure—with expensive electricity and limited roads—and lack of human capital. Yet, the cumulative NIM for Liberian banks at 7 percent in 2011 is lower than the 8 percent average NIM for all banks in the sample. Also, returns on assets and equity have been persistently very low in Liberia relative to the region. In 2011, despite a sharp increase in nonperforming loans, lending and deposit rates have remained stable while net interest margins declined.

Net Interest Margins and Overhead costs (2008-2010)
(Percentage)



Sources: Bankscope and Central Bank of Liberia.

[3] Bankscope data from Côte d'Ivoire, Guinea Bissau, Liberia, Nigeria, Sierra Leone and Togo.

IMPLICATIONS FOR LIBERIA

7. **The analysis shows that overhead costs relative to assets drive net interest margins across banks in the region, which implies that Liberian banks should be expected to earn relatively high net interest margins**. The Liberian financial system has expanded rapidly since 2006 with banks nearly doubling in number, but most banks remain very small with high overhead cost and relatively few assets. Moreover, lending is highly concentrated, with two banks out of a total of nine accounting for nearly 75 percent of demand deposits and private sector credit, leaving a very small market for most banks. Additionally, poor lending controls and risk management are raising bank operational risk. While some of these factors are mitigated by most of the banks being subsidiaries of larger foreign banks that may be able to backstop liquidity and capital needs if necessary, low profits make the banking environment less attractive to potential entrants and hampers financial development.

8. **Consequently the analysis raises concerns on the repercussions of the CBL's policy to use moral suasion to lower commercial bank lending rates**. Small Liberian banks with higher operational costs relative to size are particularly vulnerable to this policy. Several of the smaller banks are operating in niche markets such as agriculture and microfinance where credit risks and operational costs are higher. The exercise of moral suasion on the small banks may risk pressuring them out of the credit market and discourage them from expanding operations, which would hamper competition. Additionally, this policy may exacerbate banking sector fragilities stemming from the anemic returns.

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Table 1. Estimation of Determinants of Net Interest Margins in ECOWAS Banks

Independent Variable: NIM	GMM-(Blundell/Bond 98) Coefficients	OLS-Coefficients
L.NIM	-.01	.515***
	(.043)	(.037)
NIEPA	.515***	.267***
	(.054)	(.033)
L. Return on Equity(ROE)	-.007**	.001
	(.003)	(.003)
L.NPL/L	-.030***	-.035***
	(.0114)	(.001)
L. Return on Assets (ROA)	.076*	.045
	(.041)	(.034)
Interaction(L.ROA*L.NPL/L)	.003***	.003***
	(.001)	(.001)
Interaction(L.ROE*L.NPL/L)	-.000***	-.000***
	(.000)	(.000)
Constant	-6.72***	.063
	(2.74)	(1.75)
Country Fixed Effects	Yes	Yes
Year Fixed Effects	Yes	Yes
Number of Banks	86	86
Number of Observations	403	403
R^2		.631

Where ***, **, and * indicate significance at 99, 95 and 90 percent confidence respectively. D indicates time difference and LD indicates lagged time difference. Standard error in parenthesis.

Table 2. Estimation of Determinants of Net Interest Margins in ECOWAS Banks Using Log Differences

Independent Variable: D.NIM	GMM-(Arellano/Bond 91) Coefficients	OLS-Coefficients
LD.NIM	-.380***	-.295***
	(.074)	(.063)
LD.NIEPA	.133**	.108**
	(.068)	(.054)
LD. Return on Equity(ROE)	.010*	.004
	(.006)	(.004)
LD.NPL/L	-.026	-.019
	(.016)	(.013)
LD. Return on Assets (ROA)	-.278***	-.170***
	(.075)	(.063)
Interaction(LD.ROA*LD.NPL/L)	.003	.002
	(.002)	(.001)
Interaction(LD.ROE*LD.NPL/L)	-.001***	-.001***
	(.000)	(.000)
Constant	3.00***	-1.019
	(1.09)	(2.99)
Country Fixed Effects	Yes	Yes
Year Fixed Effects	Yes	Yes
Number of Banks	59	76
Number of Observations	224	311
R^2		.167

Where ***, **, and * indicate significance at 99, 95 and 90 percent confidence respectively. D indicates time difference and LD indicates lagged time difference. Standard error in parenthesis.

LIBERIA: THE INVESTMENT-FINANCING-GROWTH NEXUS[1]

INTRODUCTION

1. **The Government of Liberia has set an ambitious agenda to transform the Liberian economy and to reach middle-income country status by 2030, the underlying goal of their second Poverty Reduction Strategy (PRS2).** The authorities' strategy focuses on achieving accelerated broad-based growth by scaling up investment in infrastructure and human capital. As in other low-income countries, the question is how fast public investment should be scaled up to address massive infrastructure gaps and developmental needs and the trade-offs and potential risks associated with different financing options and the required changes in fiscal policy.

2. **To address this question, we examine some preliminary results from simulations of an inter-temporal macroeconomic model used to explore the nexus between public investment, financing, and growth.** The model is designed to capture the features of low income countries (LICs) like Liberia and, where possible, has been calibrated using Liberian economic data. The analysis presented here complements the standard IMF-World Bank debt sustainability analysis.

3. **The model used in this note assumes that public investment has a high economic and social rate of return and is highly complementary toward private sector investment**. An increase in public investment therefore provides both a direct and an indirect boost to GDP growth. The model accommodates different methods of financing the investment buildup. The government may increase taxes (or reduce transfer payment), borrow from domestic markets, or borrow on international commercial markets. Concessional financing, which has so far been the primary source for Liberia, is included as an exogenous input to the model. The model also incorporates assumptions about efficiency of public expenditure (i.e. the rate at which executed investment translates into productive capital). For different levels of public investment, and assumptions about minimum available financing and efficiency of public investment, the model generates different financing options, the size of the fiscal adjustment needed, and the trade-offs on the long term path of public debt and growth.

[1] This note was prepared by Manuel Rosales (AFR) and Will Clark (RES).

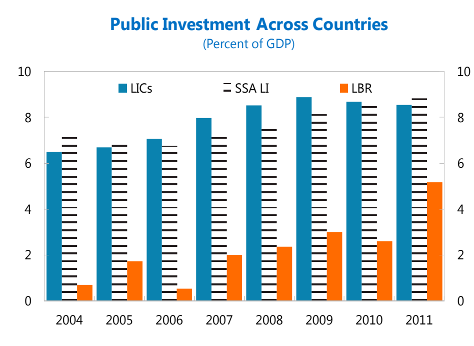
4. **The exercise yields three main policy conclusions**. First, the efficiency of public investment is important for raising the growth dividend from higher investment spending. Second, the rapid investment strategy (one in which investment is scaled up by an annual average of 14 percent of GDP) will cause debt to rise to over 100 percent of GDP if the government is not able to secure enough grants or to create enough fiscal space. Finally, a moderate to high scaling up of investment (by an annual average of 9 percent of GDP) is feasible, though it may still push debt to near its statutory limit and must be planned carefully.

5. **The note is organized as follows**: the first section provides some background on Liberia, focusing on the infrastructure and human capital needs and the government's strategy to address these needs. The second section provides a brief, non-technical overview of the model. The third section discusses the simulations, their key results, and the tradeoffs involved in each. The note ends with some concluding remarks.

I. BACKGROUND

6. **Liberia's infrastructure suffered major damage during a 17-year civil war**. The country's hydropower plant was virtually destroyed leaving the country in darkness. Roads were neglected, bringing trade to a complete halt while limiting the population's access to public services. Schools and health facilities were damaged and public institutions were abandoned, greatly affecting the country's standard of living. Along with a deteriorated infrastructure, Liberia's managerial capacity to execute infrastructure projects was completely undermined as qualified staff fled the country.

7. **Since the signing of the Peace Accords in 2003, Liberia has recorded solid economic growth averaging 7.4 percent over this nine-year period**. While this result may well reflect an initial boost associated with the recovery after the massive losses during civil war, since 2009 real economic growth has averaged 7 percent driven mostly by non-mining activities. Going forward, it is expected that the mining sector will become a more important source of growth, which is estimated to stabilize at around 6 percent.



8. **While public investment in Liberia reached 4.2 percent of GDP in FY 2011/12, it has been low—around 3 percent of GDP on average in the previous five years—and below that of other low income countries (LICs)**. Furthermore, Liberia also has a weak track record of project implementation with an execution rate of around 60-65 percent of budgeted capital expenditures reflecting legal, institutional, and managerial bottlenecks which hamper the efficient selection and effective implementation of public investment projects.

9. **Liberia is a fragile state with massive infrastructure gaps and developmental needs**:

- Per capita income is very low with 84 percent of the population in poverty ($1.25 per day);
- Employment creation has been low; according to the 2010 Liberia Labor Force Survey, 68 percent of employed Liberians work in the informal sector;
- Child mortality rate, under five, is 103 per 1,000, while the maternal mortality rate is high at 770 per 100,000 births, both of which are high compared to neighboring countries;
- Pipe-borne water—the main source of drinking water—is low and water deficiency is about 61 percent of the population. Improved sanitation (percent of population with access) is very low at only 17 percent of the population;
- Years of war affected the education system which needs to be rebuilt to deliver quality practical and vocational training. The adult literacy rate (percent of people ages 15+) is 59 percent;
- Liberia ranks at the bottom of the UN's Human Development Index (182 out of 187 countries in 2011);
- Infrastructure is weak. The country currently produces 23MW of electricity covering just 2–3 percent of the population and at the highest price in the world, access to electricity is also a constraint to small-scale manufacturing and industrial enterprises; poor roads are an impediment to trade (both domestic and cross-border) and a constraint to access public services such as education and health, especially during the rainy season;
- Aid flows are around 39 percent of GDP, including some 2 percent of GDP for budget support.

10. **Liberia successfully reached the completion point under the HIPC initiative in June 2010, helping the country to bring down its external debt from close to 150 percent of GDP to less than 9 percent**. The government's tax collections have increased substantially over the last six years (from 11 percent of GDP in FY 2005/06 to 22 percent of GDP in 2011/12) which together with the fiscal space created by the debt relief provides an important opportunity to increase public investment.

11. **The government has laid out a five-year development plan in support of the country's goal to achieve middle income status by 2030 incorporated in its PRS2**. The plan focuses on five strategic pillars—at an estimated cost of $3.3 billion over FY 2012/13 to FY 2016/17—to increase productivity, boost economic growth, and improve social inclusion—particularly among youth. The pillars are

- *Economic transformation through investing in infrastructure,* particularly rehabilitation of the hydropower plant and related transmission and distribution networks destroyed during the civil war, improvement of trunk roads, and rehabilitation and expansion of ports, and improvement in the information and communications technology. Total infrastructure investment needed is estimated at $2.2 billion, including $1.4 billion for roads and $0.5 billion in the energy sector, of which $0.2 billion is needed for the hydropower plant.

- *Human development*. The strategy aims to increase access and improve the quality of education and health, provide social protection for vulnerable persons, and rehabilitate and expand the infrastructure in water and sanitation. The estimated cost is $0.5 billion.

- *Peace, security, and the rule of law*. The Government will need to invest in the security sector to maintain a stable and peaceful environment as UN forces (UNMIL) drawdown. The expected cost is $0.4 billion.

- *Governance and public institutions*. The government plans to invest US $0.1 billion on the public sector modernization and reform agenda, decentralization and local governance, efforts and enhancing transparency and accountability.

- *Cross cutting issues*. The government intends to invest some $0.1 billion to develop youth skills and increase empowerment, child protection, gender equality, and human rights' protection.

Liberia: Agenda for Transformation Costing Summary (US$s millions)

	FY 12/13	FY 13/14	FY 14/15	FY 15/16	FY 16/17	Five Year
Pillar 1. Economic transformation	594.1	532.4	439.4	354.9	267.8	2,188.6
Pillar 2. Human development	87.2	100.9	120.8	121.1	128.9	558.9
Pillar 3. Peace, security, and rule of law	73.1	90.3	92.1	77.1	73.0	405.6
Pillar 4. Governance and public institutions	40.3	16.5	14.5	14.1	10.0	95.5
Pillar 5. Cross-cutting issues	19.5	28.7	22.5	22.1	19.2	111.9
Total	814.2	768.9	689.3	589.2	498.9	3,360.5

Source: Ministry of Finance, Agenda for Transformation (as of August 30, 2012).

It is estimated that the government will contribute between 12–15 percent of the financing required to fully implement the investment program. The remaining 85–88 percent is still unfunded. The authorities are planning a pledging donors' conference in late 2012 to secure both loans and grants to fully execute its development strategy. The model below can be used to assess the trade-offs of alternative financing options for PRS2.

II. THE MODEL

12. **The model is a small two-sector open economy framework**. A complete technical explanation of the model can be found in Buffie et al. (2012). What follows is an outline of the key features of the model.

Consumers

13. **The economy is populated with two types of agents**: savers, who have access to capital markets and inter-temporally optimize consumption and labor, and non-savers, who operate by a rule of thumb and simply consume what they earn each period.

Savers

14. **Each period, savers maximize the present discounted value of their lifetime utility** (which is just a function of consumption) by choosing how much to consume, how much to **invest**, and how much debt to incur, all subject to a budget constraint.

15. **Savers receive income from**: renting capital to firms (both traded- and non-traded goods firms); wages earned on the labor market; remittances, which act as transfer payment from the rest of the world; and net government transfers (other taxes net of current spending). They pay for: a constant elasticity of substitution (CES) basket of consumption goods; a tax on consumption; investment in new capital as well as the adjustment cost of changing the capital stock; the cost of servicing debt (both domestic and foreign) and adjusting their debt portfolio; and user fees on public infrastructure.

16. **The savers' optimization problem yields standard results**. The path of consumption depends on the real interest rate and the level of the tax on consumption. There are also three arbitrage conditions. The real interest rate on domestic bonds is equal to the real interest rate on foreign bonds, adjusted by portfolio costs. Additionally, the return on capital in the traded and non-traded sector, net of capital adjustment costs, must equal the real interest rate.

17. **The portfolio adjustment costs allow the model to capture an important feature of the market for debt in LICs**. Steep adjustment costs reflect the immobility of capital in LICs, where the private sector has a limited ability to borrow overseas and the capital account is fairly closed.

Non-Savers

18. **Savers are additionally constrained by an inability to access capital markets, and thus they do not smooth consumption over time**. Because there is no formal optimization problem for non-savers, their labor supply is fixed in each period. Income comes from wages, remittances, and government transfers. Each period, non-savers purchase a CES basket of goods and consume it in its entirety.

19. **We incorporate non-saving households to add an element of reality to the model, given the high proportion of households in LICs that consume hand-to-mouth**. The addition of these rule-of-thumb consumers into the model allows for realistic non-Ricardian outcomes.

Firms

20. **The economy is divided into traded and non-traded goods sectors, each populated by representative firms**. These firms use Cobb-Douglas technology to produce output taking as inputs labor, private capital, and effectively-produced public capital:

$$q_{j,t} = A_{j,t}(z_{t-1}^{e})^{\psi_j}(k_{j,t-1})^{\alpha_j}(L_{j,t})^{1-\alpha_j} ,$$

Here, *q* is the quantity of goods produced, *A* is aggregate factor productivity, *z* is public investment, *k* is private capital, and *L* is labor. Each of these factors is sector-specific (denoted by the subscript *j*).

21. **Inputs to production are bought in competitive markets, so profit-maximizing firms pay the marginal products for each**. Labor is inter-sectorally mobile, but capital is sector-specific. In equilibrium, the rental rate for each type of capital is the same, though the prices will not follow the same transition paths.

22. **The form of the production function captures the complementarities between public and private capital**. All else being equal, as the stock of effective public capital increases, the return on private investment and labor both increase. For any investment scaling-up, then, GDP rises by accounting identity logic, where government investment is an additive component of output, but also by increasing the incentives for private investment and labor to rise as well.

The Government

Public Investment

23. **Public investment can be thought of as a two-step process**. In the first step, the government invests in public infrastructure according to a standard accumulation equation:

$$z_t = (1-\delta)z_{t-1} + i_{z,t} \ .$$

Here, δ is the depreciation rate of public capital, and *i* is the level of investment in capital. In the second step, a portion of the public infrastructure is converted into effectively productive capital that firms use as an input to production:

$$z_t^e = \bar{s}\bar{z} + s(z_t - \bar{z}) \ .$$

The bar denotes variables at initial steady state and *s* is a parameter that governs the portion of infrastructure that is converted to effectively productive capital. Given that *s* lies on the unit interval, this feature of the model implies that one dollar of additional public investment translates to less than one dollar of effectively produced capital.[2] Note that only effective public capital increases the return on private investment by entering into the production function.

The Budget Constraint

24. **The government budget constraint requires that spending on transfers (current spending), debt service, and infrastructure investment not exceed revenue collected from a consumption tax and from user fees on infrastructure**.[3] When revenues do not meet expenditures, the resulting fiscal gap is financed through domestic borrowing, external concessional borrowing, or external commercial borrowing. External grants can also be used to finance the budget. Below, we show simulations with realistic assumptions about grants to explore their effect on the debt profile required for investment.

25. **The expenditure side of the budget constraint also contains a term meant to capture cost overruns on public infrastructure investment**. LICs have a shortage of skilled administrators, leading to public projects that are slowed by poor planning, weak oversight, or coordination problems.

26. **The interest rate on domestic debt is (quite obviously) the domestic interest rate**. The interest rate on concessional debt is assumed to be a constant negotiated rate. The interest rate on external commercial debt varies proportionally to a risk premium, defined as the ratio of the external public debt-to-GDP ratio to its initial steady state.

Fiscal Adjustment

27. **The difference between revenues and expenditures is the fiscal gap, which can be financed in the short run by borrowing or by fiscal adjustment** (i.e., taxes and transfers). In the long run, though, the tax on consumption and transfer spending must adjust to cover the entire gap.

28. **The core policy dilemma facing policymakers is the speed with which this fiscal gap is covered**. Sharp increases in the consumption tax or cuts in transfer payments are obviously painful, and policymakers would like to avoid them. If the government does not react quickly enough, or if tax increases or spending cuts are capped at restrictively low levels, interest payments on the debt will rise faster than net government revenue, causing debt to increase explosively.

[2] Empirical analysis shows that the productivity of infrastructure is high while the return on public investment is low, because not all infrastructure spending becomes public capital. See Hulten (1996) and Pritchett (2000) for details.

[3] User fees capture a fraction of the recurrent costs of maintaining public capital (i.e., maintenance and upkeep caused by capital depreciation). This feature is not meant to represent a public-private partnership model where user fees capture the cost of *financing* the infrastructure.

29. **The table below shows the main variables for Liberia.** Real per capita economic growth is assumed to be 3 percent, which reflects the average for 2009–11, which was selected to be representative as it includes two consecutive years of slow growth (2009–2010) and one year with rapid growth (2011). Given information for Liberia is limited, the value added in the non-tradable sector was set at 49.4 percent as suggested by the model.

Liberia: Steady-State Macroeconomic Variables
(In percent of GDP, unless otherwise specified)

National accounts	
Real economic growth (annual growth rate, in percent)	8.2
Real per capita growth (annual growth rate, in percent) 1/	3.0
Value added in the nontradable sector (in percent)	49.4
Government accounts	
Taxes	21.6
General sales tax rate (in percent)	7.0
Grants for budget support	1.7
Spending (net of interest)	31.0
Interest payments	0.3
Capital spending	4.1
Total debt 2/	11.7
External sector	
Current account	-34.1
Trade	-40.7
Exports	24.6
Imports	-65.4
Remittances	5.4
External debt	10.0

Source: Liberian authorities and IMF estimates.

1/ Average real per capita economic grow th over the 2009-11 period equals 2.7 percent and 3.4 percent w hen the 2012 estimate is included.

2/ For debt sustainability analysis, it excludes central government debt to the Central Bank of Liberia.

III. MODEL SIMULATION AND RESULTS

30. **A set of twelve simulations (see attached charts) demonstrate the impact on growth and debt levels of different assumptions regarding the investment path and its financing.** Starting from the steady state level of public investment of 4 percent of GDP, the baseline assumes a *moderate* scaling up of public investment (by 5.5 percentage points of GDP per year over seven years). We also tested for *intermediate* scaling up of public investment (by 9 percentage points of GDP per year) and a *rapid* scaling up (by an annual average of 14 percentage points of GDP per year). In turn, each of the three scaling up assumptions were tested for different financing options and different assumed efficiency of public investment. The twelve scenarios are as follows:

a. Baseline (moderate) scaling-up in which the public investment efficiency rate is 60 percent: the financing needs are closed with concessional borrowing.

b. Baseline (moderate) scaling-up in which the public investment efficiency rate is 60 percent: the financing needs are closed with concessional borrowing and some domestic financing.

c. Baseline (moderate) scaling-up in which the public investment efficiency rate increases to 80 percent: the fiscal gap is still closed with concessional borrowing.

d. Baseline (moderate) scaling-up in which the public investment efficiency rate is only 20 percent: the fiscal gap is still closed with concessional borrowing.

e. Intermediate scaling-up: fiscal gap is closed with concessional borrowing.

f. Intermediate scaling-up: fiscal gap is closed with a mix of concessional borrowing and an endogenous tax adjustment.

g. Intermediate scaling-up: fiscal gap is closed with a mix of concessional borrowing and an endogenous transfer adjustment.

h. Rapid scaling-up: fiscal gap is closed with additional concessional borrowing.

i. Rapid scaling-up: fiscal gap is closed with commercial borrowing.

j. Rapid scaling-up: fiscal gap is closed with a mix of concessional borrowing and commercial borrowing.

k. Rapid scaling-up: fiscal gap is closed with additional grant aid and a tax adjustment.

l. Rapid scaling-up: fiscal gap is closed with additional grant aid, commercial borrowing, and a tax adjustment.

31. **The table below shows the cumulative boost to real per capita GDP growth from each of the scenarios relative to the assumed steady-state growth rate of 3 percent, as well as the impact of the scenarios on public debt.** For assessment purposes, we present here only those scenarios which are most interesting for policy consideration and focus the analysis on the investment-financing-growth nexus.

Liberia: Growth Dividend and Impact on Public Debt from Alternative Investment Levels and Financing Strategies
(Cummulative boost to real per capita growth, in percentage points over a 10 year horizon; and percent of GDP)

	Investment scenarios and financing strategies	Growth dividend	Public debt (percent of GDP)
a.	Moderate (baseline) scaling-up: fiscal gap closed with additional concessional borrowing	9.0	42.2
b.	Moderate (baseline) scaling-up: fiscal gap closed with concessional and domestic borrowing	6.7	45.7
c.	Moderate (baseline) scaling-up: fiscal gap closed with additional concessional borrowing (high efficiency)	13.2	41.3
d.	Moderate (baseline) scaling-up: fiscal gap closed with additional concessional borrowing (low efficiency)	3.5	42.8
e.	Intermediate scaling-up: fiscal gap closed with additional concessional borrowing	13.1	49.4
f.	Intermediate scaling-up: fiscal gap closed with a mix of concessional borrowing and an endogenous tax adjustment	10.5	27.1
g.	Intermediate scaling-up: fiscal gap closed with a mix of concessional borrowing and an endogenous transfer adjustment	8.6	27.3
h.	Rapid scaling-up: fiscal gap closed with additional concessional borrowing	19.3	97.4
i.	Rapid scaling-up: fiscal gap closed with commercial borrowing	20.6	108.4
j.	Rapid scaling-up: fiscal gap closed with a mix of concessional borrowing and commercial borrowing	20.1	104.8
k.	Rapid scaling-up: fiscal gap closed with additional grant aid and a tax adjustment	15.6	51.8
l.	Rapid scaling-up: fiscal gap closed with additional grant aid, commercial borrowing, and a tax adjustment	18.3	72.7

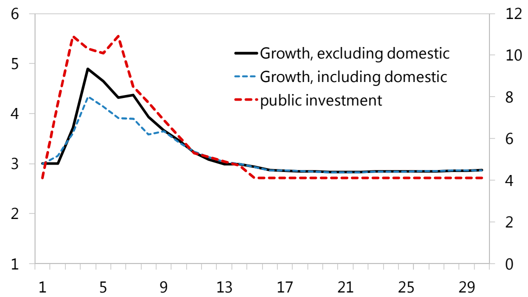
Source: IMF staff calculations.

32. **The baseline scenario (moderate scaling up of public investment) assumes that concessional borrowing is the main source of financing and there are no changes in tax policies or changes in the current level of grants for budget support**. Under this scenario, an

average increase of 5.5 percentage points of GDP in investment per annum over a seven year period contributes to an approximately 1 percentage point increase in the annual growth rate of real per capita income on average over ten years. The growth effect peaks 3–4 years after the initial investment and then gradually declines over time returning to trend growth. The cumulative growth dividend to year-on-year per capita growth equals 9 percent over a 10-year horizon with central government total debt estimated to reach approximately 42 percent of GDP at the end of year 10 compared to 11.7 percent of GDP in FY2011/12.

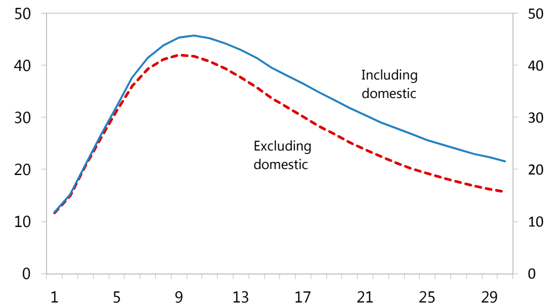
33. **We tested for the impact on growth and the debt dynamics of including domestic financing as a source of financing public investment (scenario b)**. In line with government policies in Liberia, we assumed that the government is able to raise, on an annual basis, 1 percent of GDP in funds in the domestic market. Under this scenario, the crowding out of private investment limits the cumulative growth dividend over a 10 year period to 6.7 percent and worsens the country's debt dynamics.

Liberia: Public Investment and Real Per Capita Income Growth Under a Moderate Scaling Up Strategy and Different Financing Strategies (Percentage change, y.o.y.)



Sources: IMF staff calculations.

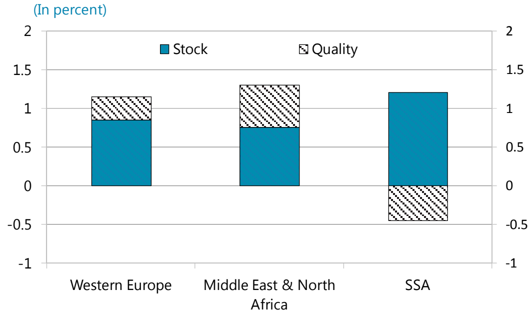
Liberia: Public Sector Debt Dynamics Under a Moderate Scaling Up Scenario and Different Financing Strategies
(Percentage of GDP)



Sources: IMF staff calculations.

34. **We also ran scenarios on the baseline for changes in the efficiency of public investment**. Several studies show that the quality of projects is critical to translate public investment into productive capital to boost growth. Calderon and Serven (2009) found the quality of public investment contributed positively to per capita growth in advanced and Middle-East and North African countries while Sub-Saharan African countries show poor performance as many projects were not properly assessed or executed.

Changes in growth per capita due to infrastructure investment
(In percent)

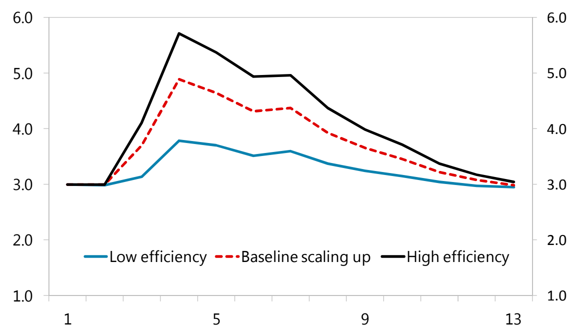


Sources: Calderon-Serven, 2009.

35. **From an assumed efficiency rate of public investment of 60 percent in the baseline scenario—the average for low income countries—we tested for higher efficiency rate of 80 percent (scenario c)**. If the government can increase the efficiency of its public investment, this

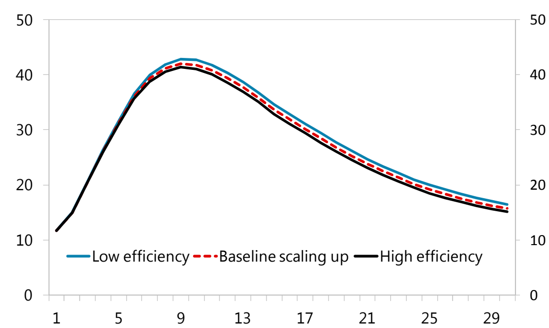
can further boost economic growth and moderately improve debt dynamics. Under the higher efficiency scenario, real per capita income growth could potentially increase by an additional half percentage point over the medium term. Getting to higher growth faster, in turn, would improve Liberia's debt dynamics. On the other hand, the same amount of investment with a lower efficiency rate of 20 percent (scenario d) would result in lower per capita growth and moderately weaker debt dynamics. These results point to the critical need for stepped up efforts to tackle bottlenecks to project implementation in Liberia.

Liberia: Real Per Capita Income Growth
(Percentage change, y.o.y)



Sources: IMF staff calculations.

Liberia: Public Debt Under Different Growth Scenarios
(Percentage of GDP)



Sources: IMF staff calculations.

36. **The results of other scenarios are as follows**. In scenario *e* (intermediate investment strategy), the government is able to secure new grants for budget support equivalent to an additional annual average of 2 percent of GDP to help finance the medium term investment plan. Still, the government needs to continue relying on concessional borrowing within the limits set by the Public Financial Management Act Regulations, which sets the ceiling on public debt to 60 percent of GDP. Under this scenario, the growth dividend to per capita GDP over a 10 year period is 13.1 percent, very similar to the high efficiency rate simulation.

37. **Scenario *f* (intermediate investment strategy)** assumes the financing gap is closed by a combination of additional grants and changes in taxes. Under this strategy, the cumulative boost to real per capita growth is approximately 10.5 percent, relatively close to the baseline scenario a. In this case, the population has access to a larger infrastructure level, but the increase in taxes required to close the financing gap constrains consumption, thus limiting the impact on growth.

38. **Scenarios *h* and *i* represent the government's rapid investment build-up strategy** with the financing gap closed entirely with either concessional or commercial borrowing, respectively. Under these two scenarios, the increase in public investment contributes to a boost in consumption and private investment to the highest possible levels in the medium term,

increasing the growth dividend between 19–21 percent. However, this strategy comes at the expense of mounting total public debt to unsustainable levels (between 97–108 percent of GDP), especially in the case of commercial borrowing, which, in the long run, will require large changes in taxes and transfers to service such debt.

39. **Scenario *k* (rapid investment strategy) assumes the government is able to secure 2 percent of GDP in new grants for budget support**, but not enough to close the estimated financing gap. In this case, the government is required to adjust the consumption tax from the start while still resorting to some additional concessional borrowing beyond what is assumed in the baseline scaling up scenario. The growth dividend in real per capita GDP over a 10-year period is approximately 15.6 percent with public debt peaking at 52 percent of GDP.

40. **The various scenarios have some caveats**. For Liberia, several of the parameters were borrowed from previous work on other LICs and Liberia-specific parameters should be treated with caution due to limited data availability. In addition, the model abstracts away from reality (e.g., only two types of consumers, agents with perfect foresight, etc.). Hence, the estimates should be seen only as a first approximation as the model should not be seen as a forecasting tool. Finally, other shocks not discussed here have the potential to change the estimates, either positively or negatively depending on the nature of the shock (i.e., a global recession or a productivity shock in Liberia).

41. **Previous work on the investment-growth nexus in Liberia points to a positive but smaller impact from scaling up investment on growth**. Yoon and Lane (2009), who focused on the macroeconomic impact of scaling up aid, found that increasing aid would have a positive, albeit limited, effect on the Liberian economy rate of growth. They estimated that increasing foreign aid by 5 percentage points of GDP only contributed to an average increase of 0.16 percent per year in growth over a 10 year period. One factor that contributed to such a lower impact compared to current work is that their analysis assumed that only 30 percent of aid was allocated to investment while the rest was directed to cover current spending, in particular for services paid abroad.

IV. CONCLUDING REMARKS

42. **The simulations presented here capture some of the costs and benefits of the three potential investment strategies**. The model results provide background to support the government's objectives and expectations to scale up public investment to stimulate the economy while flagging the risks related to debt sustainability.

43. **Some caution is required when interpreting the simulations presented here**. Liberian data is limited, the model relies on some average parameters calculated for other LICs, and, it abstracts away from reality (e.g., only two types of consumers, agents with perfect foresight, etc.). Thus the results should be interpreted with this in mind. All that being said, the model helps to gauge the relative costs and benefits of various investment and financing scenarios.

44. **As expected, the more ambitious investment program yields the larger growth dividend over the medium term, but it comes at the risk of unsustainable debt; hence assessing other options is warranted**. The intermediate scaling up option in which the government is able to secure some 2 percentage points of GDP in new grants for budget support results in stronger growth dividends and more stable debt dynamics.

45. **In addition to securing the ideal balance of financing options, there is a critical need to increase the efficiency of public investment in Liberia**. The government needs to step up efforts to tackle bottlenecks to project implementation and even more importantly to properly prioritize and select high return projects that effectively translate into productive capital.

46. **Adjustments in taxes or in current spending (net transfers) may be painful policies which may have high political costs but may be required to successfully implement the government's PRS2**. The authorities are rightly focusing on creating fiscal space to scale up public investment, but further efforts to streamlining current spending are warranted.

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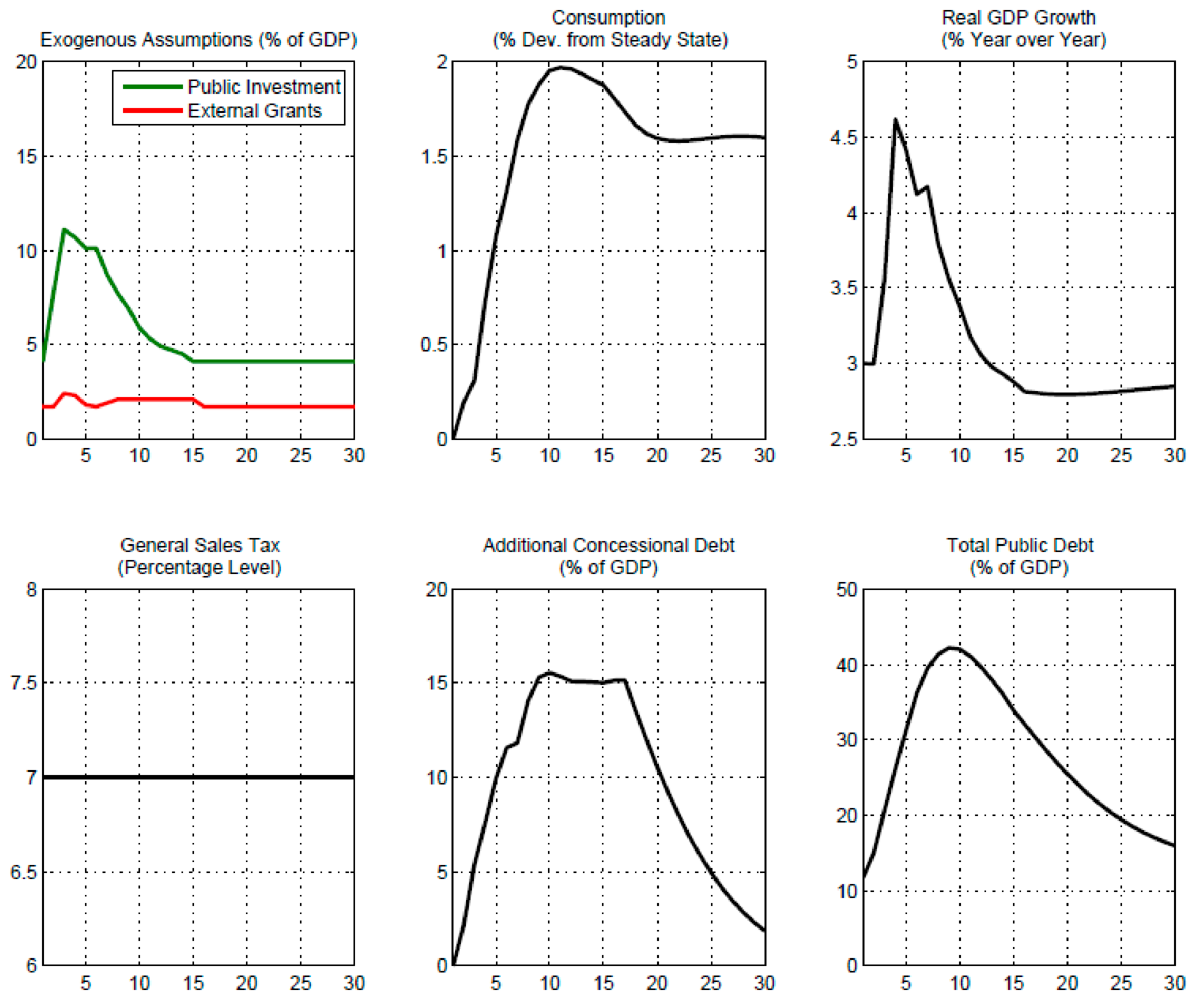
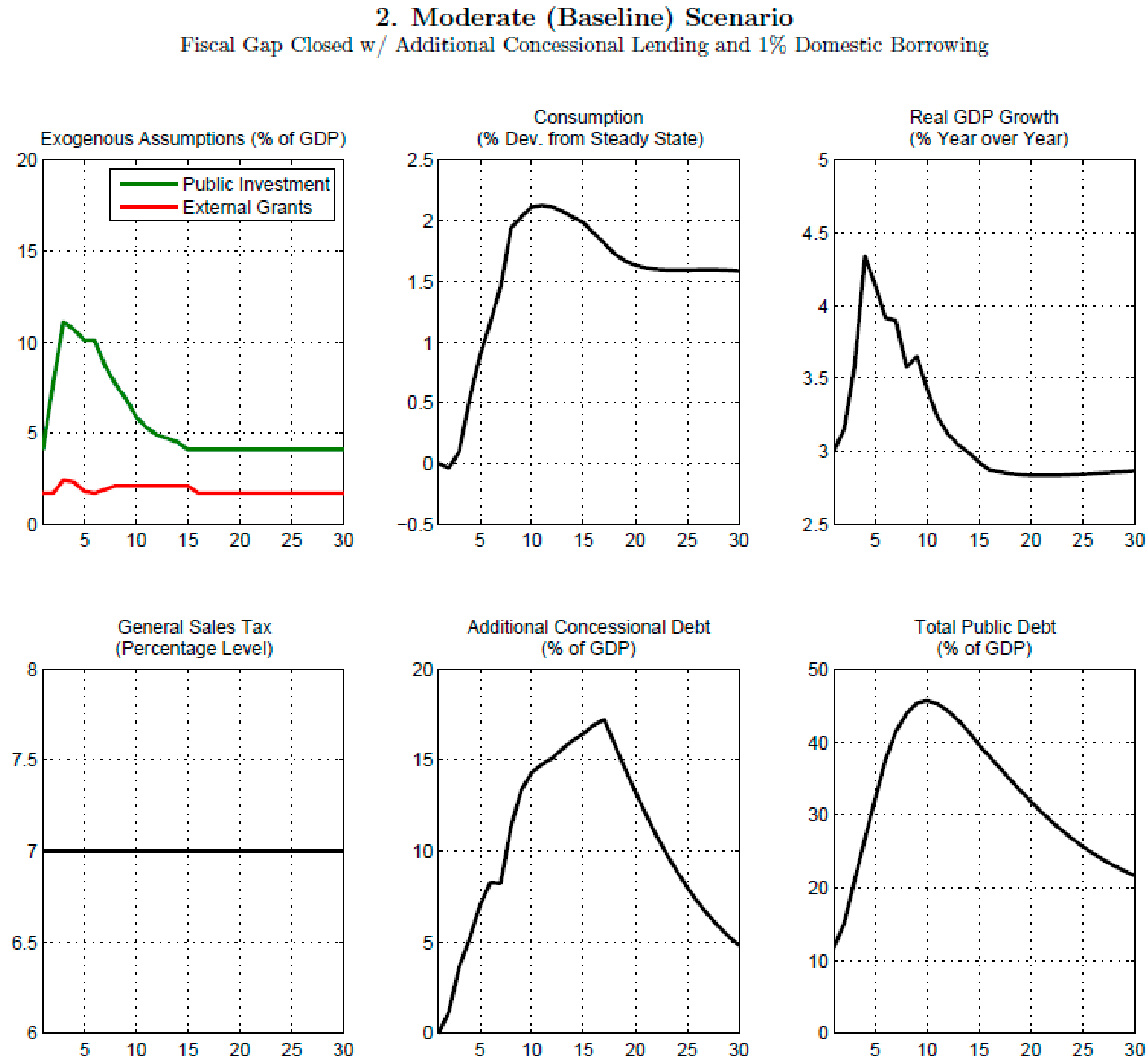
1. Moderate (Baseline) Scenario
Fiscal Gap Closed w/ Additional Concessional Lending

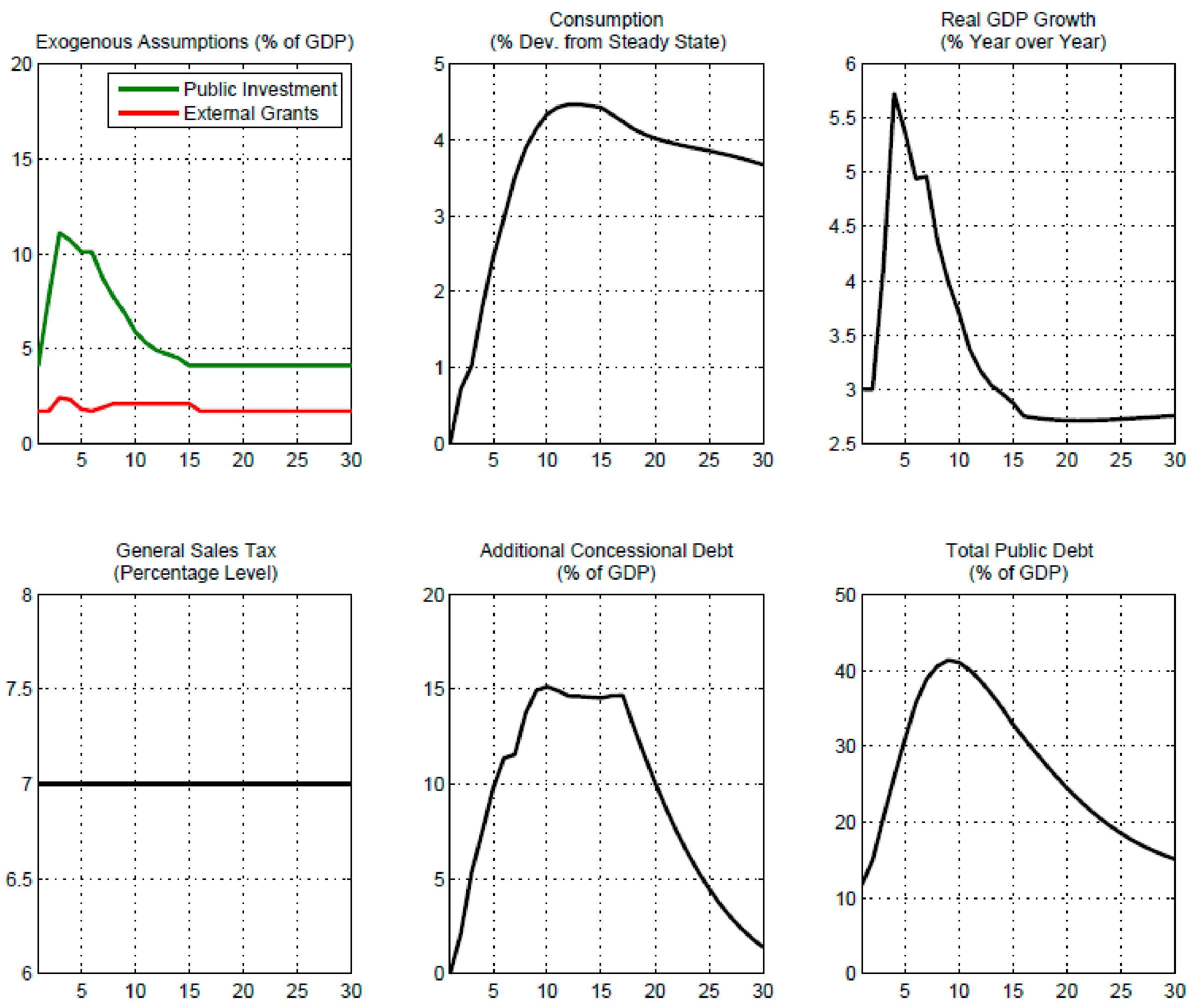




2. Moderate (Baseline) Scenario
Fiscal Gap Closed w/ Additional Concessional Lending and 1% Domestic Borrowing
Exogenous Assumptions (% of GDP)
Public Investment
External Grants
Consumption
(% Dev. from Steady State)
Real GDP Growth
(% Year over Year)
General Sales Tax
(Percentage Level)
Additional Concessional Debt
(% of GDP)
Total Public Debt
(% of GDP)

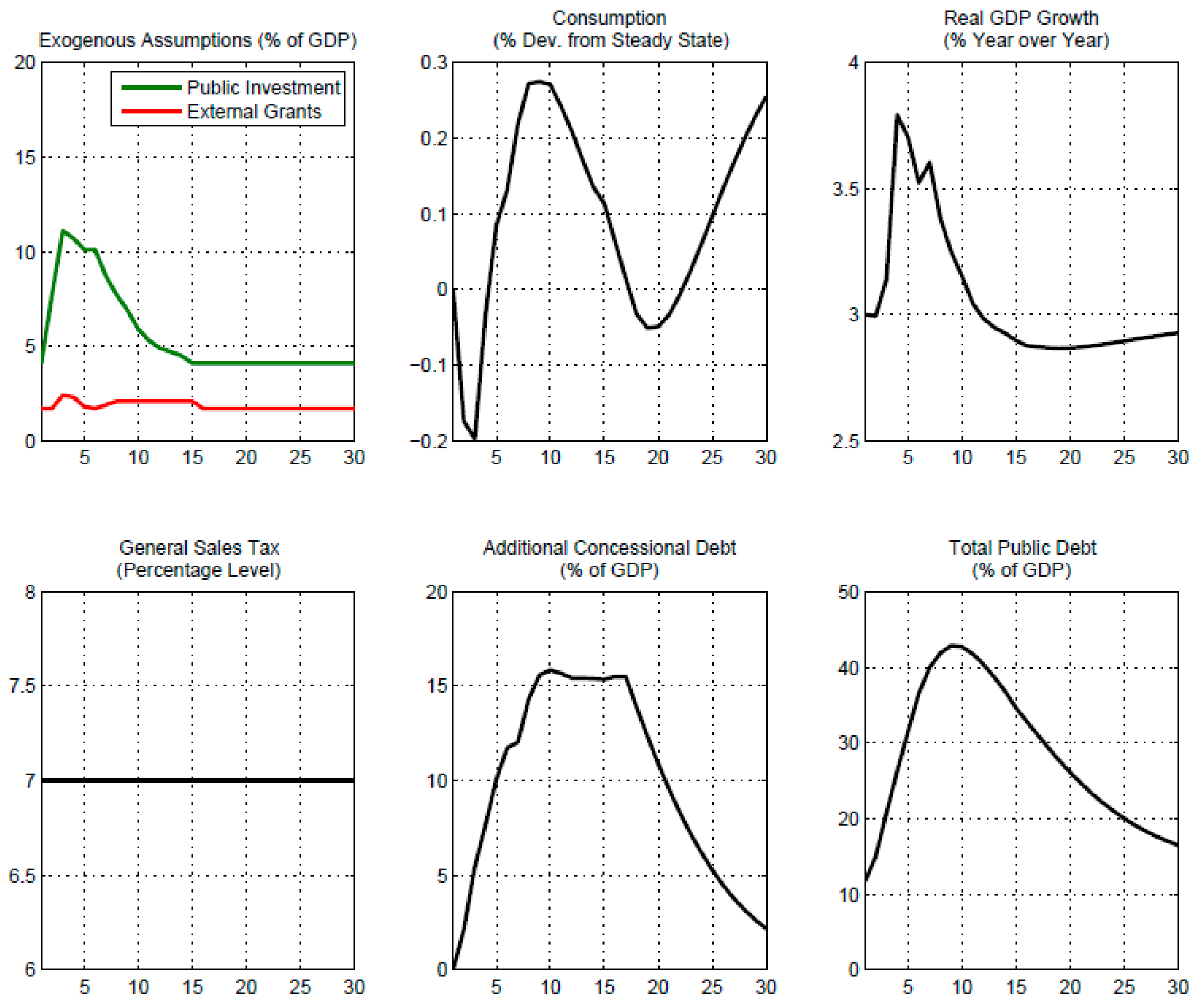
3. Moderate (Baseline) Scenario – High Investment Efficiency

Fiscal Gap Closed w/ Additional Concessional Lending

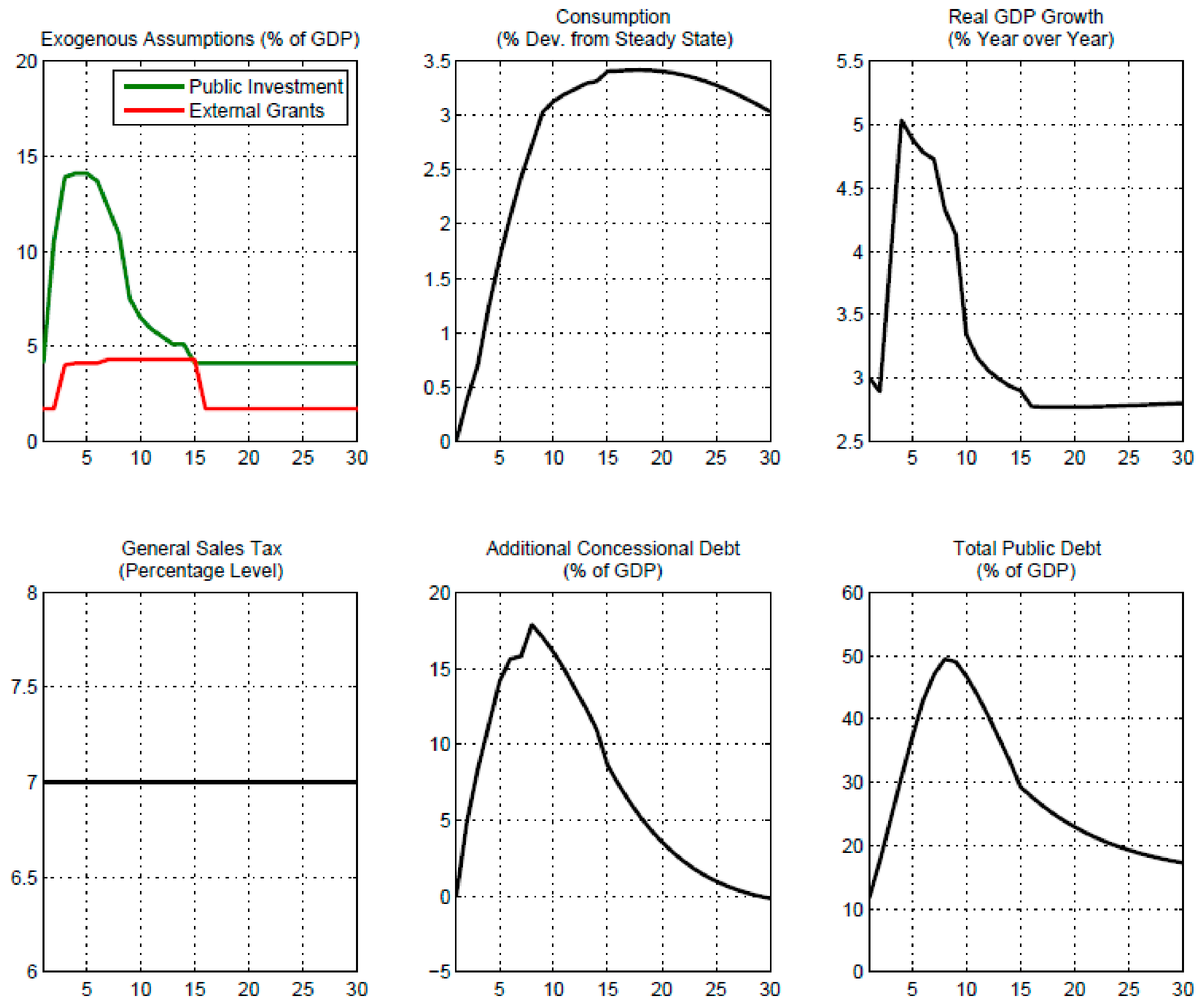


4. Moderate (Baseline) Scenario – Low Investment Efficiency

Fiscal Gap Closed w/ Additional Concessional Lending

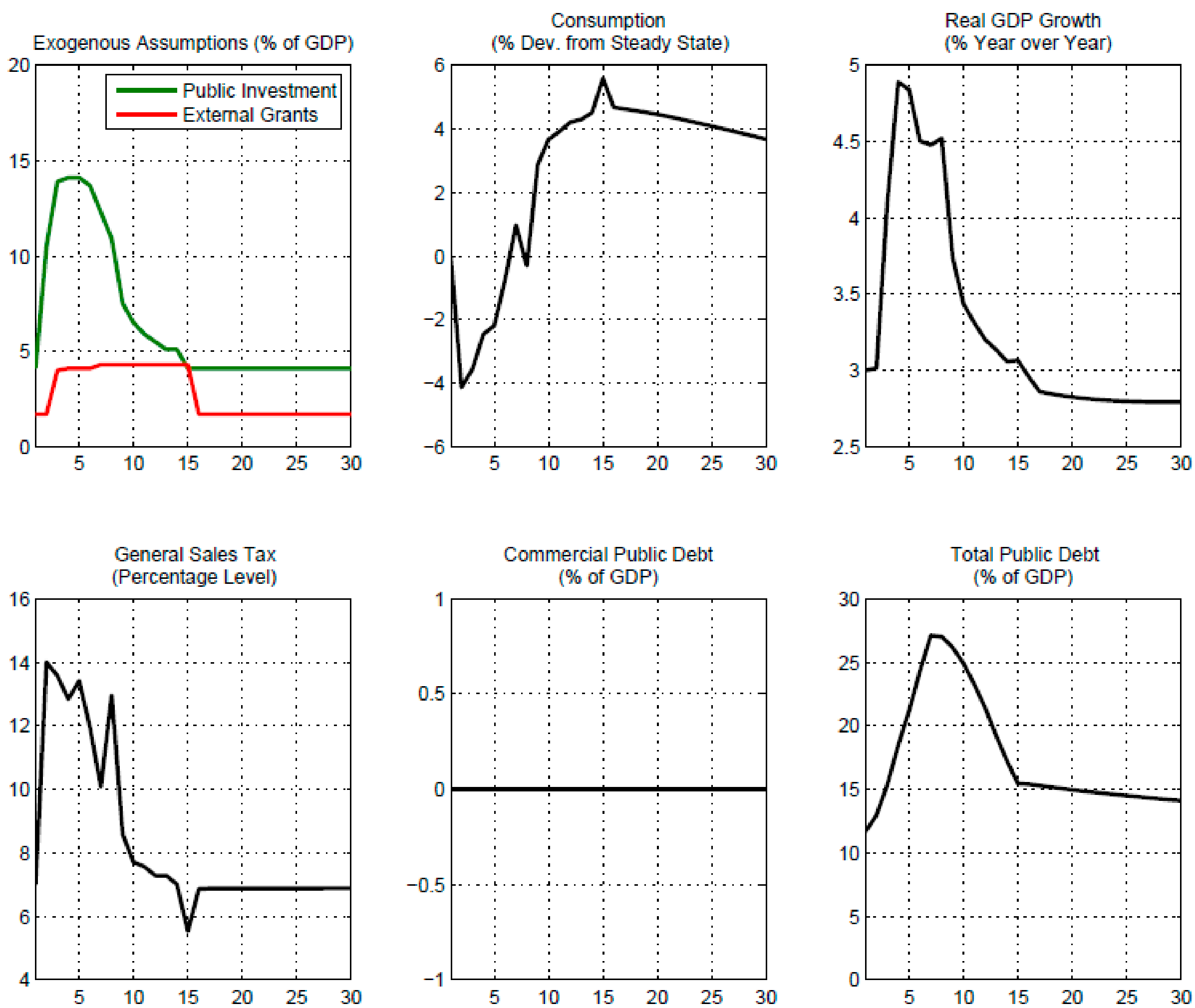


5. Intermediate Investment Scenario
Fiscal Gap Closed w/ Additional Concessional Lending



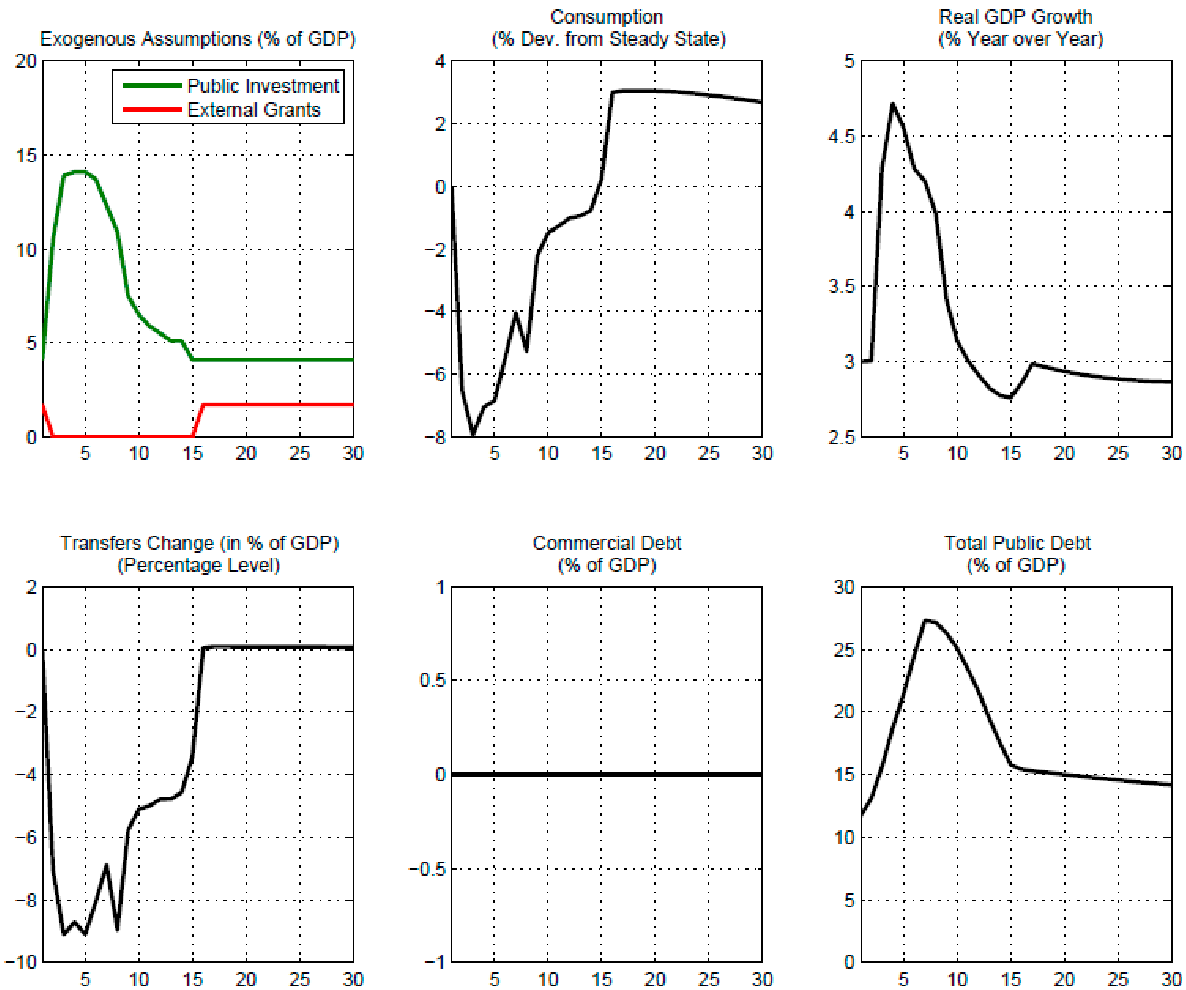
6. Intermediate Investment Scenario

Fiscal Gap Closed w/ Tax Adjustment

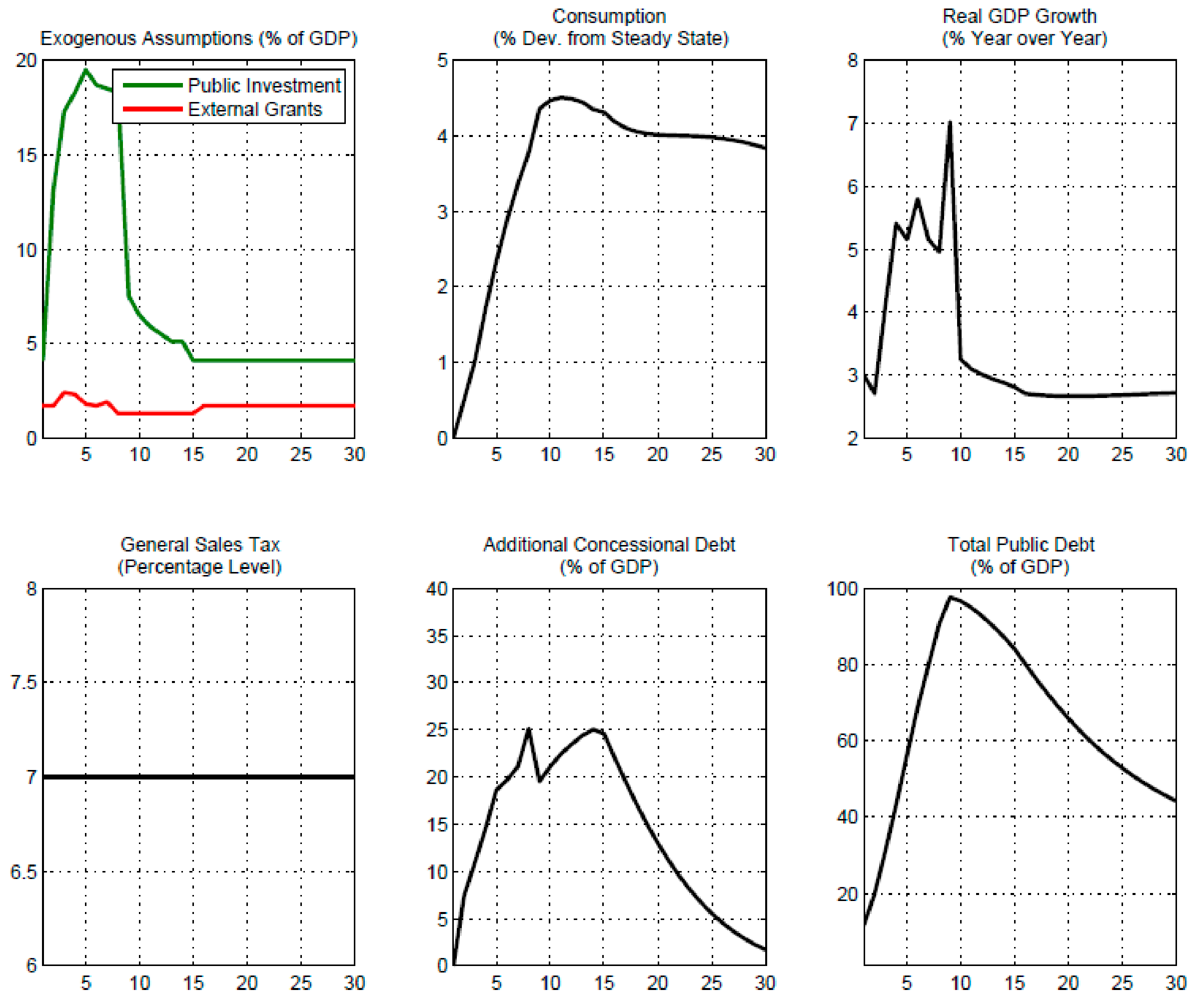


7. Intermediate Investment Scenario w/ no Grants

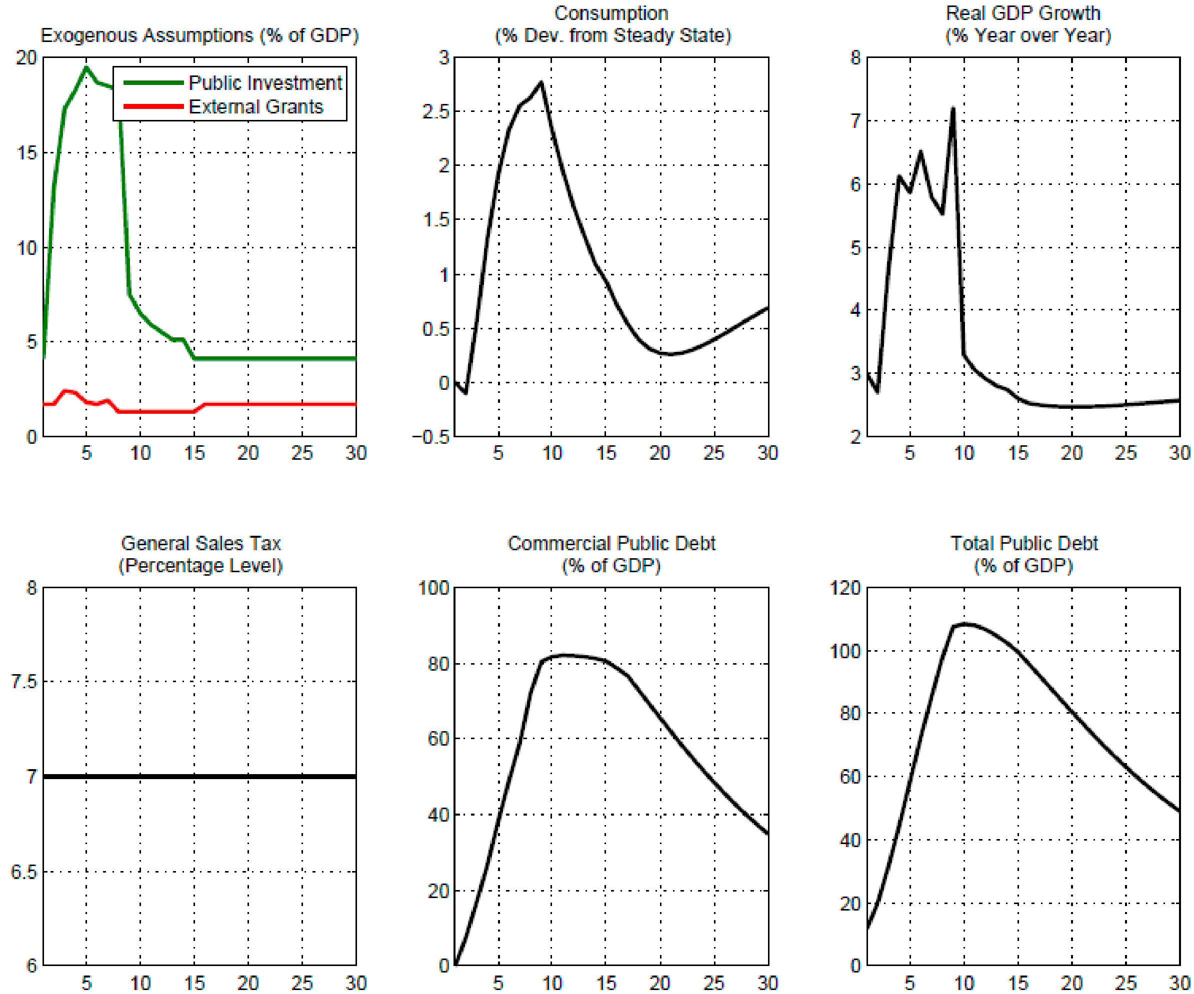
Fiscal Gap Closed w/ Transfer Adjustment



8. Rapid Scaling-Up Scenario
Fiscal Gap Closed w/ Additional Concessional Lending

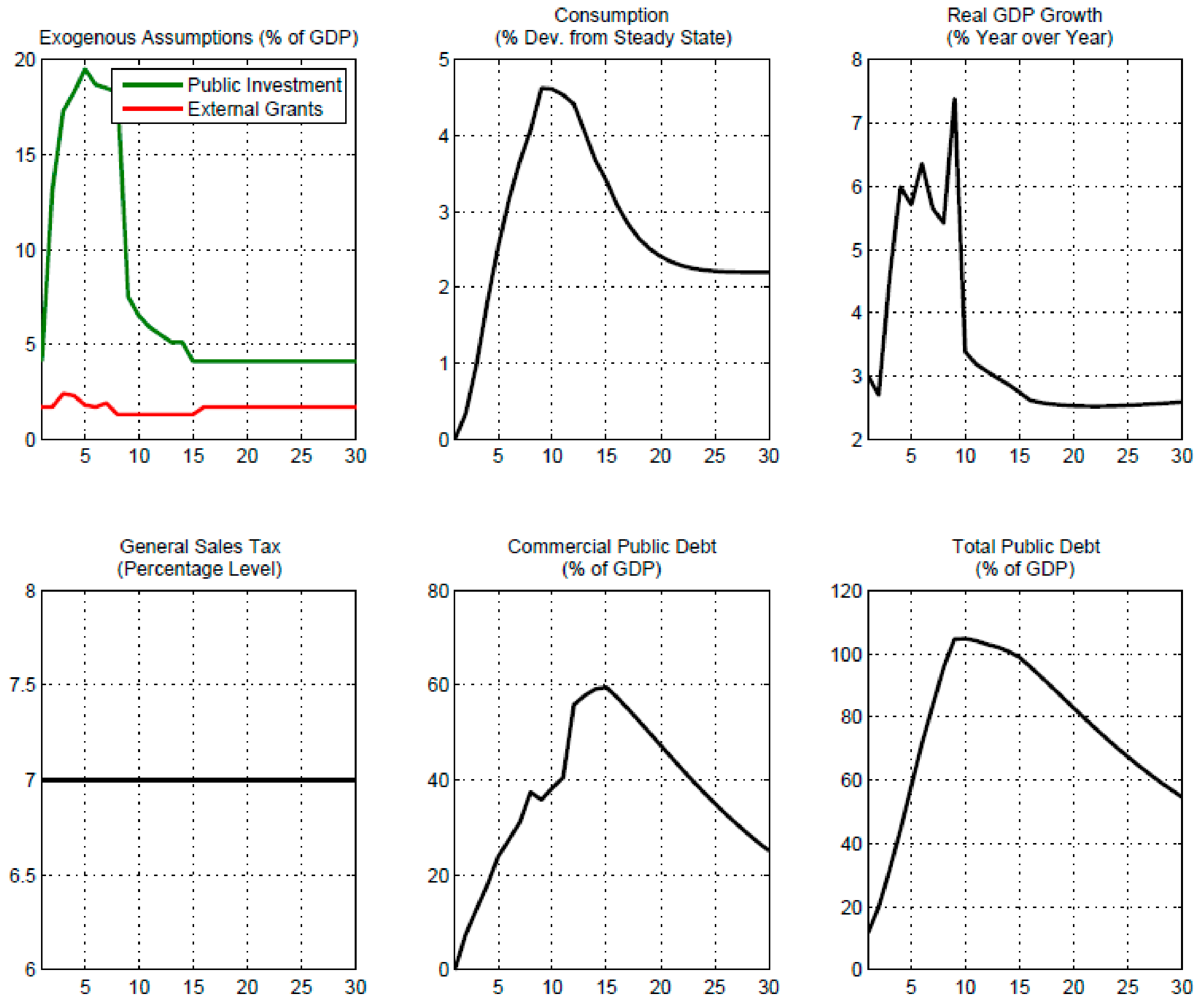


9. Rapid Scaling-Up Scenario
Fiscal Gap Closed w/ Commercial Lending

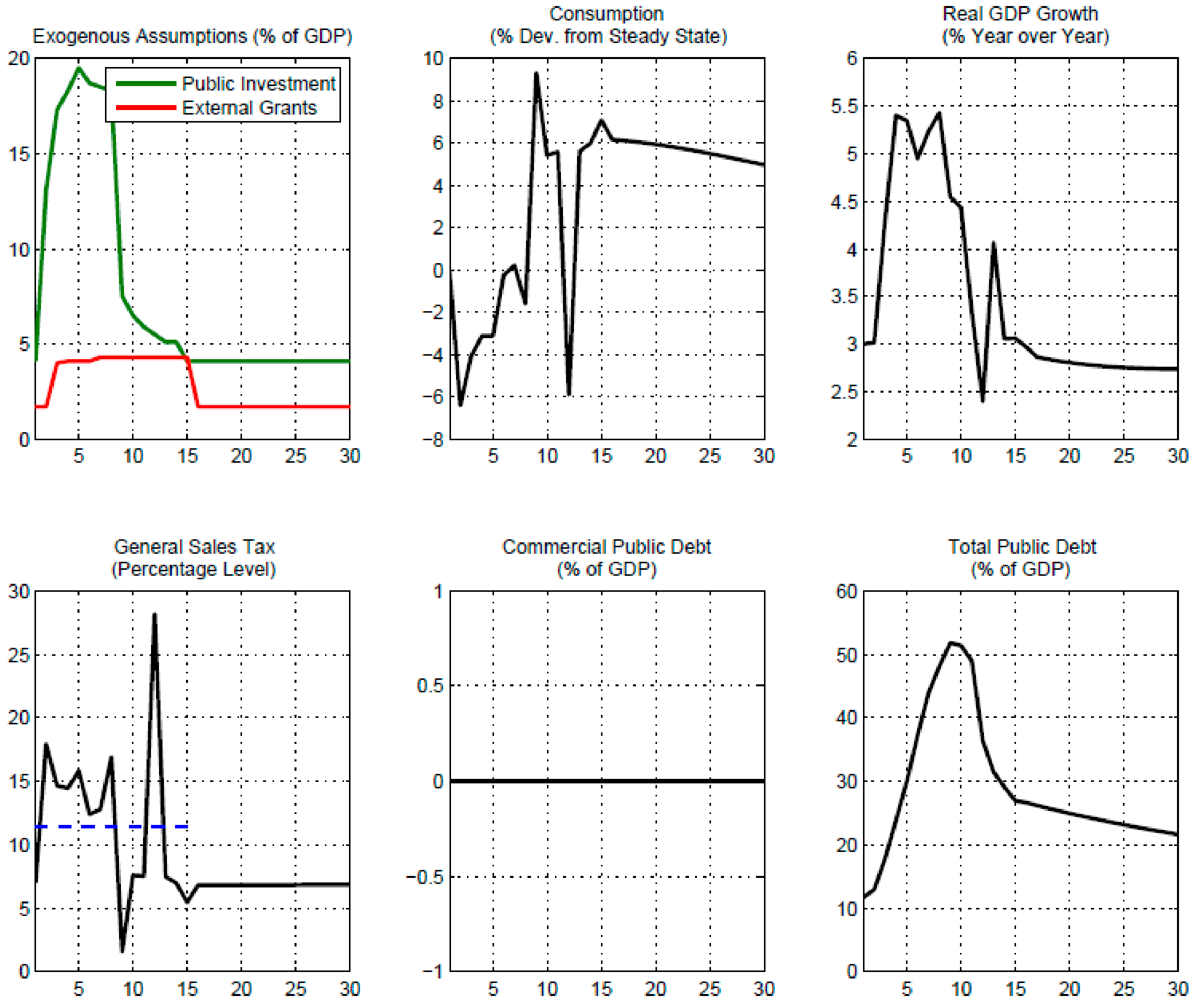


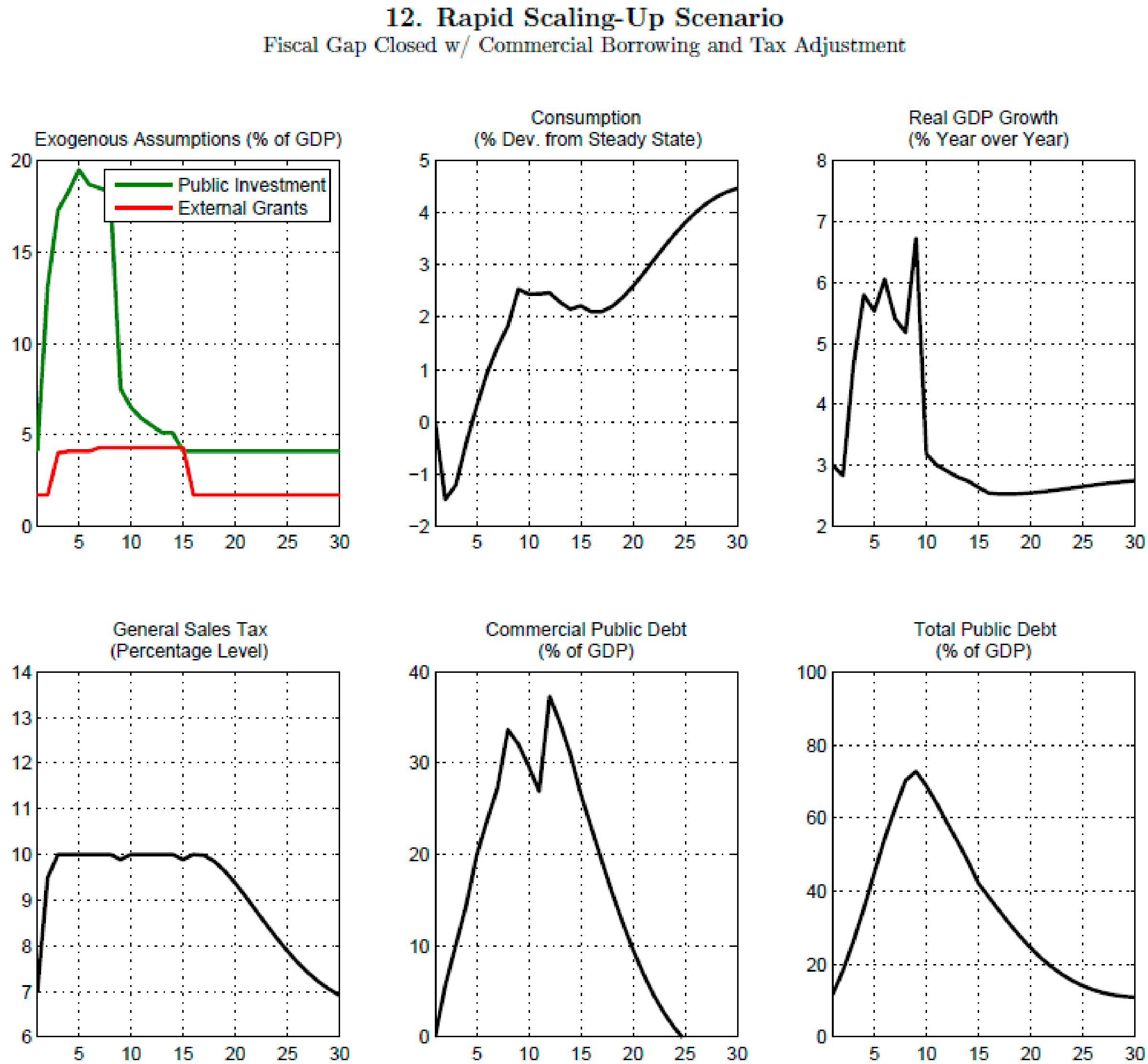
10. Rapid Scaling-Up Scenario

Fiscal Gap Closed w/ Commercial and Concessional Lending



11. Rapid Scaling-Up Scenario
Fiscal Gap Closed w/ Tax Adjustment




12. Rapid Scaling-Up Scenario
Fiscal Gap Closed w/ Commercial Borrowing and Tax Adjustment
Exogenous Assumptions (% of GDP)
Public Investment
External Grants
Consumption
(% Dev. from Steady State)
Real GDP Growth
(% Year over Year)
General Sales Tax
(Percentage Level)
Commercial Public Debt
(% of GDP)
Total Public Debt
(% of GDP)

INTERNATIONAL MONETARY FUND

LIBERIA

November 2, 2012

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION AND REQUEST FOR THREE-YEAR ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—INFORMATIONAL ANNEX

- Relations with the Fund. Describes financial and technical assistance from the Fund and provides information on the safeguards assessment and exchange rate system. Outstanding purchases and loans amounted to SDR 42.14 million (32.61 percent of quota) at end-September 30, 2012.
- Joint World Bank-IMF Work Program, 2012–13.
- Statistical Issues. Assessment of the quality of the statistical data. Weaknesses in national accounts statistics are hampering the analysis of economic developments in the country.

Prepared By

African Department (In consultation with other departments)

CONTENTS

RELATIONS WITH THE FUND

(As of September 30, 2012)

1. **Membership Status**: Joined: March 28, 1962. Article XIV

2.	**General Resources Account**:	**SDR Million**	**%Quota**
	Quota	129.20	100.00
	Fund holdings of currency	129.18	99.99
	Reserve Tranche Position	0.03	0.02

3.	**SDR Department**:	**SDR Million**	**%Allocation**
	Net cumulative allocation	123.98	100.00
	Holdings	150.08	121.05

4.	**Outstanding Purchases and Loans**:	**SDR Million**	**%Quota**
	ECF Arrangements	42.14	32.61

5. **Latest Financial Arrangements**:

	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF [1]	Mar 14, 2008	May17, 2012	247.90	247.90
EFF	Mar 14, 2008	Sep 25, 2008	342.77	342.77
Stand-By	Dec 07, 1984	Dec 06, 1985	42.78	8.50

[1] Formerly PRGF.

6. **Projected Payments to Fund**
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2012	2013	2014	2015	2016
Principal	0.00	0.00	2.10	3.69	5.46
Charges/Interest	0.00	0.00	0.11	0.10	0.09
Total	0.00	0.00	2.21	3.79	5.55

7. **Implementation of HIPC Initiative**: Enhanced Framework

I. Commitment of HIPC assistance	
Decision point date	March 2008
Assistance committed	
By all creditors (US$ Million) [1]	2,739.20
Of which: IMF assistance (US$ Million)	721.10
(SDR equivalent in millions)	440.90
Completion point date	June 2010

[1] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

II.	Disbursement of IMF assistance (SDR Million)	
	Assistance disbursed to the member	440.90
	Interim assistance	30.14
	Completion point balance	410.76
	Additional disbursement of interest income [2]	10.99
	Total disbursements	451.89

[2] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

8. **Delivery of Debt Relief at the Completion Point**:

I.	Debt relief (SDR Million)	548.53
	Financed by: Liberia Administered Account	116.20
	Remaining HIPC resources	432.33
II.	Debt relief by facility (SDR Million)	

	Eligible Debt		
Delivery Date	GRA	PRGT	Total
June 2010	342.77	205.76	548.53

9. **Safeguards Assessment**

A 2011 update assessment of the Central Bank of Liberia (CBL) found strengthened safeguards in place, including through the implementation of International Financial Reporting Standards (IFRS), independent external audits, and effective oversight of audit and control matters by the Board of Governors and its Audit Committee. Continued progress and development of relevant safeguards will be needed with the envisaged expansion of reserves and cash management activities. Also, the respective rights and obligations of the government and the CBL regarding IMF transactions need to be clarified and transparently disclosed in the CBL financial statements.

10. **Exchange Rate Arrangement**

Liberia maintains an exchange rate system that is free of restrictions on payments for current and capital transfers. The currency of Liberia is the Liberian dollar. The U.S. dollar is also legal tender. The exchange rate showed limited mobility for most of 2011 resulting in a short lived re-classification of the de facto exchange rate regime to 'stabilized arrangement' effective January 5, 2011. The de facto exchange rate regime was re-classified back to 'other managed' effective November 7, 2011 as the Liberian dollar diverged from the 2 percent six months band. The de jure exchange rate regime classification remains 'managed floating'. The exchange rate between the Liberian dollar and United States dollar at end-July 2012 was L$73.50=US$1 (mid-point between buying and selling rates)

11. **Article IV Consultation**

The 2010 Article IV consultation discussions were held in Monrovia during September 21–October 1, 2010. The staff report (Country Report No. 10/373, December 2010) was discussed by the Executive Board on December 8, 2010 and is posted on the IMF website.

12. **Technical Assistance 2009–12**

Subject	Department	Date
Resident Advisors		
Long-term Advisor for the CBL	MCM	August 2007–October 2009
Public Financial Management	FAD	July 2008–Present

Topic	Date
Fiscal Affairs Department	
Reforms and Technical Assistance Needs	February 2009
Public Financial Management—Drafting Regulations	February–March 2009
Fiscal Decentralization	February–March 2009
Public Financial Management Regulations Drafting	May 2009
Revenue Authority, Customs and Tax Administration	May 2009
Public Financial Management	June 2009
Tax Administration	September 2009
Tax Policy	November 2009
Public Financial Management	October 2010
Tax Administration	March 2010
Revenue Administration	June 2010, Sept., and Dec. 2010
Revenue Department Strategic Plan	November–December 2010
Tax Policy	November–December 2010
Public Financial Management Strategy	December 2010, March–April 2011
Revenue Department Strategic Plan	January–February 2011
Cash Flow Planning and Government Banking Arrangements	February 2011
Medium Term Expenditure Framework	March 2011 and August–Sept. 2011
County Treasury Framework	June 2011
Tax Administration	June–July and August–September 2011
Tax Policy	November–December 2011

Revenue Administration	January–February 2012
SOE Financial Reporting Framework	March – April 2012
Cash Flow Management	April 2012
Public Expenditure Financial Assessment (PEFA) Follow up	June 2012

Topic	Date
Fiscal Decentralization	September 2012
County Treasuries	September 2012
Statistics Department	
Government Finance Statistics	April–May 2009
Monetary Finance Statistics	March–April 2010
National Accounts	April 2010, and July–August 2010
National Accounts	January 2011
Balance of Payments	March–April 2011
Statistics Department Monetary and Financial Statistics	August 2011
National Accounts Compilation	September 2011
Short-term Resident Advisor on National Accounts	May – August 2012
Monetary and Capital Markets Department	
Accounting	January and August–Sept. 2009
Monetary Operations	April and October 2009
Foreign Exchange Operations	June 2009
Banking Supervision	September–October 2009
Monetary Financial Statistics	March–April 2010
Central Bank Accounting Standards	May 2010
Monetary Operations	June–July 2010
Banking Supervision	August 2010
Bank Payment Systems	December 2010
Central Bank Accounting	January–February 2011
Central Bank Modernization	March–April 2011
Bank Payment Systems	May 2011
Banking Supervision	June–July 2011
Safeguards Assessment	July 2011
Monetary Financial Statistics	August 2011
Capacity building for national payment system	September–November 2011

Central Bank Accounting	December 2011
Accounting	January 2012
Monetary Operations	January 2012
Stress Testing	January 2012
Payment Systems Law	February 2012
Banking Supervision	March–April, 2012
Legal Department	
Legal Drafting	May 2009 and December 2009
Drafting Tax Legislation	July 2010
Legal Drafting	Dec. 2010, March and August 2011

Technical Assistance Pipeline (indicative at end-August 2012)	**Estimated Date**	**Type of Assistance**
Fiscal Affairs Department		
Design, sequencing, coordination and monitoring of public financial management (PFM) reforms	2012–14	Resident Advisor
Medium term expenditure framework capacity building (multi-mission)	April–Sept. 2012	Short-term experts and Regional PFM adviser
Public Financial Management Program oversight	August 2012	Short-term expert
Cash flow management	Sept.–Dec. 2012	Short-term expert
SOE Oversight		Short-term expert
Project Oversight and Management		Short-term expert
Fiscal reporting	April and October 2012	Short-term expert
SOE Financial Reporting Framework	March– April 2012	SOE Financial Reporting Framework
Tax policy (VAT, petroleum, other)	April, May, September 2012	Short-term experts and HQ team
Tax Administration Design & Monitoring		Short-term experts and HQ team
Tax audit strategy		Short-term experts

13. **Resident Representative**

A resident representative has been posted in Monrovia since April 2, 2006. Mr. Sobolev assumed the position in July 2009.

JOINT WORLD BANK-IMF WORK PROGRAM, 2012–13

(As of October 12, 2012)

Title	Products	Timing of mission	Expected delivery date	Status
A. Mutual information on relevant work programs				
1. World Bank work program	1. Liberia Poverty Assessment	January 2010	May 2012	First delivery-June 2012. Final delivery-November 2012
	2. Fourth Reengagement and Reform Support Program	November 2010	September 2011	Signed Dec. 2011.
	3. Poverty Reduction Strategy – Support	November 2010	June 2012	Completed
	4. Public Expenditure Review Notes	November 2011	July 2013	Two Notes delivered final Note in progress
	5. Diagnostic Trade Integration Study (Update)	October 2012	July 2013	Ongoing
	6. Decentralization Policy Note	January 2013	July 2013	Ongoing
2. IMF work program	1. Negotiation successor ECF	July and Sept. 2012	November 2012	
	2. Article IV Consultation	July and Sept. 2012	November 2012	
	3. First review of ECF Program	March 2013	April 2013	
	4. Second review of ECF Program	September 2013	Sept. 2013	
	5. Managing Natural Resource Revenue in Liberia: Options for a Fiscal Framework		November 2012	Background paper
	6. Drivers of net interest margins and bank profitability in Liberia		November 2012	Background paper
	7. The Investment-Financing-Growth Nexus		November 2012	Background paper
	8. Outreach program to Legislature, private sector associations, and students		March, June 2013	
	2. Joint Staff Assessments (JSA) on the second Poverty Reduction Strategy (PRS2).	January 2013	February 2013 pending receipt of PRS from Government	
	3. Technical Assistance for PFM reforms and decentralization.			On-going
	4. Assist the authorities in developing national accounts			Ongoing

B. Requests for work program inputs				
4. Fund request to Bank	1. Country Assistance Strategy		When completed	
	2. World Bank Relations Note		As needed	
	3. Poverty Assessment		November	
5. Bank request to Fund	1. Regular updates of performance under the Fund-supported program, macroeconomic projections and data following each IMF mission		Continuous	Last update March 2012
	2. IMF Relations Note		As needed	

RELATIONS WITH THE WORLD BANK GROUP[1]

(As of September 4, 2012)

The overarching aim of the Joint Country Assistance Strategy[2] (JCAS) presented to the Board of the World Bank Group on April 21, 2009 is to support Liberia's transition from post conflict recovery to long-term development. More specifically, the JCAS, which is fully aligned with the Africa Regional Strategy and the Government's Poverty Reduction Strategy (PRS), focused on three strategic objectives: (i) rebuilding core state functions and institutions; (ii) rehabilitating infrastructure to sustain economic growth; and (iii) facilitating pro-poor growth. The World Bank's program under the JCAS involved a combination of development policy lending, investment lending and analytical work in support of the three strategic objectives.

The World Bank's indicative IDA financing for the JCAS (FY09–FY11) was US $298.0 million. With the addition of some US $120 million under the Liberia Reconstruction Trust Funds managed by the Bank, as well as other trust funds, the actual financing under the JCAS program is approximately US $530 million. The International Finance Corporation (IFC) net commitment under the JCAS was about US $16.4 million with a program focused on: improvement of the investment climate; improving the dialogue between the government and the private sector;

[1] Prepared by the World Bank.
[2] Joint with World Bank, IFC and African Development Bank.

strengthening the financial sector; supporting private participation in the economy by financing selected private sector companies in identified priority sectors including agribusiness, infrastructure, mining and manufacturing; and supporting the sustainable development of small and medium-sized enterprises.

A progress report presented to the Board on July 7, 2011 extends the current Joint Country Assistance Strategy to end FY12 to coincide with the launching of Liberia's Agenda for Transformation. The Liberia indicative allocation for the IDA16 period (July 2011–June 2014) is SDR 117.5 million, an increase of 18 percent over the IDA 15 allocation. The preparation of the new five-year Country Partnership Strategy (CPS) for FY13–17 is underway and it is expected that the CPS will be presented to the World Bank's Board in mid-December 2012.

A. Active Projects

There are currently twelve active[3] IDA projects in Liberia, including three regional projects, with a total commitment of approximately US$310.6 million of which US $145.6 million is undisbursed. Five new operations (credits) were approved in FY12 (ending June 30, 2012) for a total commitment of approximately US $191.5 million. The five new credits are summarized below:

The Liberia Smallholder Tree Crop Revitalization Support Project was approved on June 15, 2012 for US $15 million. The objective of the project is to increase access to finance, inputs, technologies and markets for smallholder tree crop farmers in Liberia, and to develop a long term development program for the tree crops sector. The project has three primary components, first of which focuses on the revitalizing the production and marketing of major tree crops including cocoa, coffee, oil palm and rubber. The second component of the project focuses on (i) institution building, including strengthening key public and private institutions involved in project planning, implementation and coordination and (ii) the preparation and validation of a master plan for targeted tree crops. The third component of the project is concerned with project coordination, management and evaluation.

The West African Power Pool (WAPP)-Cote d'Ivoire, Liberia, Sierra Leone, and Guinea Power Interconnection Project a regional energy project was approved in May 2012 for US$144.5 million. The project's development objectives are: (i) to reduce the cost of and increase

[3] Effective and/or disbursing operations.

the electricity supply at utility level; and (ii) to increase the export capability of Cote d'Ivoire. The project consists of two sub-projects which will be implemented independently. The first project which focuses on the WAPP power interconnection has two major components. The first component addresses the transmission infrastructure for the interconnection with Cote d'Ivoire, Liberia Sierra Leone and Guinea. Such infrastructure will include the overhead transmission line, the substations, the supervisory control and data system, frequency control system as well as the environmental and social management plan. The second component of the first sub-project addresses institutional framework (including the establishment of a regional transmission company) and project oversight. The second sub-project provides technical assistance to support the integration of the WAPP network; for technical studies and to build implementation capacity.

The Liberia Electricity System Enhancement Project (LESEP)-Additional Financing was approved in January 2012 for US$22 million. The objective of the Additional Financing for the Electricity System Enhancement Project is to improve and increase access to electricity in Liberia. The additional financing will provide for additional or expanded activities to scale up project's impact and development effectiveness in the following areas: 1) distribution network reinforcement and extension; 2) enhancing options for power generation through the procurement of a thermal power plant of approximately 10MW; and 3) providing modern renewable energy services through a Global Environment Facility (GEF) financed lantern exchange program.

Liberia Integrated Public Financial Management Reform Project was approved in December 2011 for US $5 million of IDA resources and approximately US $23.5 million of cofinancing from the African Development Bank, United States Agency for International Development, and Swedish International Development Cooperation Agency. The development objective of the project is improved budget coverage, fiscal policy management, financial control, and oversight of government finances of Liberia. The project has five components. The first component of the project focuses on enhancing budget planning systems, coverage, and credibility. The second component of the project is aimed at strengthening Project Financial Management (PFM) legal framework, budget execution, accounting, and reporting. The third component of the project focuses on revenue mobilization and administration. The fourth component of the project deals with enhancing transparency and accountability. The fifth and final component of the project addresses program governance and project management.

Liberia Fourth Reengagement and Reform Support Program was approved in October 2011 for US $5 million. The objectives of the operation are to support government-owned ongoing reforms to strengthen governance and improve the environment for private sector-led inclusive growth. More specifically, the RRSPIV focuses on: (i) improving the capacity for and transparency of public procurement; (ii) improving internal control procedures and the capacity for internal audit; (iii) improving revenue administration; and (iv) improving land administration to reduce conflicts and enhance the investment climate.

B. Economic and Sector Work

The World Bank has completed a series of on-demand analytical studies to support the preparation of the next Poverty Reduction Strategy (PRS)—Agenda for Transformation. This PRS is the first strategy in the context of the Government long-term vision plan—Liberia Rising 2030 which aims to take Liberia to middle income status by 2030. The analytical work includes: (i) a policy note describing underlying assumptions and baseline outcomes generated using a general equilibrium model (MAMS). The model was used to simulate the medium to long term impact of various policy alternatives on key macro variables as well as MDGs; (ii) an inclusive growth diagnostic study to assess binding constraints to economic activity in Liberia; (iii) an analysis of the options for leveraging investment activities and rents from the extractive sectors to support the development of the domestic private sector; (iv) an infrastructure diagnostics intended to help answer two key policy concerns: (a) how to prioritize infrastructure investments for economic diversification; and (b) how to leverage concessions contract for infrastructure development in Liberia; (v) a preliminary diagnostic of the state of social protection in Liberia and a comprehensive inventory on social protection interventions as a basis for debate and discussion towards the formulation of an effective social protection policy and strategy; and (vi) a Poverty Note to provide detailed analysis of some of the key determinants of poverty in Liberia and how these interact, particularly at the household level. Second on the basis of the analysis identified evidence-based policy options for reducing poverty. The World Bank is also providing technical assistance for the preparation of the Agenda for Transformation and the compilation of the national accounts in collaboration with the IMF.

C. Financial Relations (as at September 4, 2012)
(Millions of U.S. dollars)[1]

Project	Closing Date	Approval (Fiscal Year)	Net Commitment Amount	Total Disbursed	Of Which: Loan Disbursement	Total Undisbursed Balance
West Africa Power Pool APL	3/28/2013	2010	1.9	1.8	1.8	0.1
LR: Youth, Employment, Skills Project	6/30/2013	2010	6.0	4.9	3.3	1.1
Community Empowerment II	7/31/2013	2007	5.0	3.6	0.0	1.4
LR-Agriculture & Infrastructure Development Project. ERL	10/31/2013	2008	53.0	45.0	0.0	8.0
LR-Econ. Governance & Institutional. Reform TAL	12/31/2013	2008	18.0	12.5	1.5	5.5
LR-Emergency Monrovia Urban Sanitation	12/31/2013	2010	22.4	17.8	0.5	4.6
LR-Urban and Rural Infra. Rehab. Project	6/30/2014	2009	64.0	43.5	0.0	20.5
West Africa Regional Fisheries Program	12/15/2014	2009	9.0	3.6	3.6	5.4
Liberia Electricity System Enhancement Project	12/31/2014	2012	32.0	2.0	2.0	30.0
West Africa Regional Communications Infrastructure Program	9/302015	2011	25.6	20.6	20.6	4.2
West Africa Agricultural Productivity Program APL	6/30/2016	2011	6.0	1.0	1.0	4.9
LR-Road Asset Management Project	6/30/2022	2011	67.7	5.7	0.0	59.9
Total	**…**	**…**	**310.6**	**162.0**	**34.3**	**145.6**

[1] Amounts may not add up to original principal due to changes in the SDR/US exchange rate since signing.

IDA Disbursements and Debt Service (Quarterly since HIPC Completion Point)

US$ Million	Jul–Sep 2010	Oct–Dec 2010	Jan–Mar 2011	Apr–Jun 2011	Jul–Sep 2011	Oct–Dec 2011	Jan–Mar 2012	Apr–Jun 2012
Total disbursements	9.47	22.13	7.64	22.58	21.82	10.73	14.25	8.47
Repayments	0.33	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net disbursements	9.14	22.13	7.64	22.58	21.82	10.73	14.25	8.47
Interest and fees	0.05	0.00	0.00	0.00	0.00	0.00	0.00	0.07

Note: *=revised data.

RELATIONS WITH THE AFRICAN DEVELOPMENT BANK[1]

(As of September 10, 2012)

There are 11 active AfDB projects in Liberia, including one regional project, with a total commitment of approximately UA 108.2 million, equivalent to US $163.4 million, of which 33% is disbursed. A brief description of these active projects is summarized below:

1. **Economic Governance and Competitiveness Support Program**: The UA 30 million grant will finance the Economic Governance and Competitiveness Support Program. This second budget support operation aims to (i) improve PFM systems; (ii) strengthen tax and customs administration including transparency and accountability of revenue from the extractive industry; and (iii) improve business enabling environment for private sector development. It will also increase the government's fiscal space for pro-poor expenditure in line with the PRS. The program is an integral part of a broader set of interventions of the AfDB designed to support good financial and economic governance. In December 2011, the first tranche of UA 14 million was disbursed.

2. **Integrated Public Financial Management Reform Project (IPFMRP)**: The ADB's UA 3.0 million grant support for this project was approved on September 10, 2012. Supported by four donors—the ADB, World Bank, USAID, and SIDA—this US $28.55 million project represents an innovative approach for the Bank to support a comprehensive government program for PFM

[1] Prepared by the African Development Bank.

reform. By using a pooled funding arrangement, the project harmonizes support from the four donors, increasing development effectiveness while decreasing the administrative burden on the Government. The project has five components, which are mutually reinforcing: (i) enhancing budget planning and credibility; (ii) strengthening budget execution, accounting and reporting; (iii) strengthening revenue administration; (iv) enhancing transparency and accountability; and (v) project management and capacity building.

3. **Payment system development project**: This UA 5 million supplementary grant allows Liberia to join the West Africa Monetary Zone (WAMZ) Payments System Development Project. The project aims to improve the financial sector basic infrastructure in the WAMZ region through the upgrade of the payments systems of: The Gambia, Guinea, Sierra Leone, and Liberia. The project components are: Real Time Gross Settlement (RTGS) system; Retail Payments Automation (RPA), a clearing system comprising Automated Checks Processing (ACP); Automated Clearing House (ACH); Central Banking Applications (CBA) system; and telecommunication infrastructure. The project will increase participation in the formal financial sector and enhance financial flows at the regional level. This project fits under Pillar I of the Bank's proposed Regional Integration Strategy for West Africa 2011–15 on linking regional markets through trade and investment facilitation.

4. **Technical Assistance from Fragile States Facility:**

   a. **LEITI**: US $460,000 grant assistance for Multi-Stakeholders Group costs; communication and outreach, staff training and capacity building of actors involved in extractive industries transparency related activities

   b. **Public Financial Management Reforms**: US $1,000,560 grant assistance to cover operating cost for Public Financial Management Reform Unit, Macro Fiscal Unit, and Aid Management Unit.

   c. **Dagliotti School of Medicine**: US $300,600 grant assistance to retain 3 professors teaching at Dagliotti School including cost of carrying out medical research.

5. **Liberia–Urban Water Supply and Sanitation Project (UWSSP)**. This UA 25.2 million grant project aims to improve Monrovia's water and sanitation facilities. The UWSSP is complementary to the MWSRP providing the interface and rehabilitation of the water

distribution network in central Monrovia area "B". The project will: (i) provide access to adequate, safe and reliable water supply and public sanitation services in Monrovia, Buchanan, Kakata and Zwedru; and (ii) enhance the institutional, operational, management capability, and the long-term financial viability of LWSC. Project's components are: (i) Rehabilitation and augmentation of water treatment and distribution systems; (ii) Provision of public sanitation facilities; (iii) Institutional support; (iv) Environmental and Sanitation Sensitization. Expected outcomes include: (i) Reliable and affordable water and sanitation services to 50 percent of the population in Monrovia, and 75 percent coverage in Buchanan, Kakata, and Zwedru (about 700,000 total people); (ii) Social connection revolving fund to enable access by the poor; (iii) Improved projects implementation by water and sanitation sector staff; and (iv) Improved management, operation and maintenance of water and sanitation facilities.

6. **Water Sector Reform Study**: This €2.5 million study, funded by a grant from the African Water Facility, seeks to foster improved governance and comprehensive long-term development of the water sector. The study components are: (i) Development and implementation of water and sanitation sector policy and strategy, institutional reform, and capacity building; (ii) Development of tools to support water sector planning and (iii) Reinforcement of national capacities to undertake the sector reform process. Expected outcomes are: (i) Improved policy and restructured institutions; (ii) Improved implementation efficiency of WSS programs and projects; (iii) Faster development and effective utilization of resources; and (iv) Improved capacity of the water sector to manage and develop water resources.

7. **Agriculture sector rehabilitation project**: This UA 18.4 million project cost is financed by a UA 12.5 million grant from the Bank, UA 3.4 million grant from IFAD, and the balance financed in kind by the Government of Liberia. The project covers eight of the fifteen counties in Liberia. The project complements the Bank-supported Labour-Based Public Works Program (OSHD). The overall goal of the Agriculture Sector Rehabilitation project is to contribute to food security and poverty reduction. Its specific objective is to increase the income of smallholder farmers and rural entrepreneurs including women on a sustainable basis. The project is implemented under three components: Agriculture Infrastructure Rehabilitation; Agricultural Production and Productivity Improvement; and Project Management, with Agriculture infrastructure constituting 60 percent of the cost.

8. **Smallholder Agricultural Productivity Enhancement and Commercialization (SAPEC) Project**: This UA 34.08 million project will be funded by a UA 29.08 million grant from the Global Agriculture and Food Security Program (GAFSP), a UA 4.0 million ADF loan, and UA 1.0 million by in-kind contributions from the Government of Liberia (GOL). The Intervention

seeks to reduce rural poverty and household food insecurity by increasing income for smallholder farmers and rural entrepreneurs particularly women, youths and the physically-challenged. SAPEC will be implemented in 12 of the 15 political subdivisions or counties of Liberia over the 2012–2017 timeframe. The project seeks to scale-up the on-going Agricultural Sector Rehabilitation Project (ASRP) by operating in 8 of the 12 counties where the ASRP is being implemented. The 3 uncovered counties are programmed for similar interventions by the United States Agency for International Development (USAID), World Bank (WB) and other donors. The project consists of four components, namely: (i) Sustainable Crop Production Intensification; (ii) Value Addition and Marketing; (iii) Capacity Building and Institutional Strengthening; and (iv) Project Management.

9. **The Labour-Based Public Works Project (LBPWP)**: The UA 20.24 million grant project aims to contribute to the improvement of productive livelihoods and service delivery. The project objective is to rehabilitate socio-economic infrastructure and improve capacities for infrastructure maintenance. Its components are: i) Rehabilitation of Socio-Economic Infrastructure; and ii) Capacity Development for Infrastructure Maintenance; and iii) Project Management. In 2011 the Bank provided a UA 5.00 million supplementary grant from the Fragile States Facility (FSF) to enable the financing of additional costs resulting from improved designs of the project infrastructure.

10. **Liberia Bank for Development and Investment (LBDI)**: The project will involve a credit facility by the ADB of up to US $5 million in the form of a subordinated debt. This will provide LBDI with the required funding to meet the increasing demand for long-term financing from certain key sectors of the Liberian economy including SMEs, services, construction, agribusiness and light manufacturing. The loan is not yet effective for disbursement.

11. **Equity investment of US$ 0.9 million in the share capital of access bank (ABL)**: The Access Bank Liberia (ABL) is a start-up microfinance bank sponsored by lead investor Access Microfinance Holding AG in Germany, with co-support by the International Finance Corporation (IFC) and the European Investment Bank (EIB).

STATISTICAL ISSUES

(As of September 30, 2012)

I. Assessment of Data Adequacy for Surveillance
General: Data have serious shortcomings that significantly hamper surveillance. Shortcomings are most serious in the areas of national accounts, government finance, and balance of payments statistics.
National Accounts: Comprehensive national accounts data are not available. Fund staff estimate GDP by activity using the production approach and primary source data provided by the Liberia Institute of Statistics and Geo-Information Services (LISGIS). Estimates for GDP by expenditure are not available. Liberia participates in the National Accounts Module of the UK Department for International Development supported Enhanced Data Dissemination Initiative (EDDI), which aims to strengthen annual national accounts, and to improve price statistics. The national business register and national accounts questionnaires were established in December 2008. In 2009, the LISGIS conducted the first post-war National Accounts Annual Survey (NAAS) and collected information for the calendar year 2008. This survey had problems with low response rates and the results from the survey have not been published yet. A second round of so-called National Accounts Annual Survey (NAAS 2012) was conducted during July-August, 2012 and collected information for the years 2010 and 2011. Following a request from the authorities, an STA mission assisted the LISGIS in successfully conducting the field operations of the survey which resulted in a response rate of around 98 percent. The World Bank has also appointed a consultant to guide the LISGIS in various aspects of the survey. There are, however, challenges in estimating informal sector activities. A Household Income and Expenditure (HIES) Survey planned for 2012 will provide data from which such estimates may be developed. Supply and use tables (SUT) for 2008 were independently developed by a World Bank consultant to provide a benchmark estimate of GDP. The Liberian authorities requested STA to make an assessment of the SUT estimates. After a desk-based review of the results, STA noted that the SUT estimates for 2008 are not sufficiently robust to be published as official statistics and should be considered as experimental. The assessment took into account the lack of basic information and the use of many imputations and adjustments in the compilation process. It was stressed that such research results, however, serve to generate discussion with interested users and may, with appropriate improvements to source data and methodology, develop into official estimates. Through its technical assistance missions within the EDDI project, STA will continue to provide guidance on the use of existing and new source data to compile national accounts estimates and to build capacity in LISGIS to produce reliable national accounts statistics on an ongoing basis. With improved data sources (especially NAAS 2012 and HIES), it is expected that reliable GDP estimates should be available by 2014.
Price statistics: A consumer price index for Monrovia has been compiled since 2005. The Harmonized Consumer Price Index providing national coverage was officially adopted in 2007.

Government finance statistics: The Ministry of Finance regularly provides the African Department with monthly disaggregated data on budgetary central government revenue recorded on a cash basis, and expenditure recorded on both cash and commitment bases. While they are in the process of phasing-in the *GFSM 2001* framework, there is still a number of areas where the government finance statistics need to be improved: lack of legal framework to collect statistics; limited data sharing and coordination among data producing agencies; inconsistent institutional coverage of the statistics with other datasets (e.g., national accounts and monetary statistics); omission of nonmonetary transactions; limited data on stocks of financial assets, liabilities, and arrears; and incorrect reference exchange rate to convert data from Liberian dollars to U.S. dollars.

Monetary statistics: The Central Bank of Liberia (CBL) has made progress in adopting the statistical methodology recommended by the IMF's *Monetary and Financial Statistics Manual (MFSM)*. However, the reporting of monetary and financial statistics (MFS) has been suspended since September 2010. STA missions in March 2010 and August 2011 assisted authorities in advancing the introduction of standardized report forms (SRFs) and collecting data from commercial banks in accordance with the methodology in the *MFSM*. The CBL agreed to start reporting the SRFs for the central bank, other depository corporations, and monetary aggregates by end-December 2011. However, no data in the format of SRFs have been received by STA. Instead, in June 2012, the CBL renewed reporting of monetary data in the old format. The latest available data are for July 2012.

Balance of payments: Reporting is not comprehensive, and Fund staff prepares provisional balance of payments statistics for surveillance. Although some progress in collecting and reporting data has been made with STA support, there still remain several areas that need improvement particularly with regard to primary source data, methodology, compilation practices, and frequency and timeliness in data dissemination. Additionally, coverage needs to be improved, especially for: i) foreign direct investment, including direct investment in kind, that is likely to become significant as plans are underway for foreign companies to invest in mining activities; ii) technical assistance services, development aid, and compensation paid to locally employed workers of international organizations, which have a very large presence in Liberia; iii) banking sector transactions, as relevant monetary and financial statistics data are not used for balance of payments and there is a lack of financial account entries for the banking sector; and iv) other areas such as remittances, investment income, and the overall coverage of the financial account.

II. Data Standards and Quality

Participant in the General Data Dissemination System (GDDS) since October 2005.	No Data Module of the Reports on the Observance of Standards and Codes (data ROSC) is available.

III. Reporting to STA

The authorities report for the related publications (*IFS, GFSY, and BOPSY*) annual balance of payments data and government finance statistics, the latter with a considerable lag (latest available data is 2008).

Table of Common Indicators Required for Surveillance

	Date of latest observation (For all dates in table, please use format dd/mm/yy)	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	31/08/2012	12/10/2012	D	M	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	31/08/2012	12/10/2012	M	M	A
Reserve/Base Money	31/08/2012	12/10/2012	M	M	A
Broad Money	31/08/2012	12/10/2012	M	M	A
Central Bank Balance Sheet	31/08/2012	12/10/2012	M	M	A
Consolidated Balance Sheet of the Banking System	31/08/2012	12/10/2012	M	M	A
Interest Rates[2]	31/8/2012	29/08/2012	M	M	A
Consumer Price Index	31/08/2012	12/10/2012	M	M	A
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	NA	NA	NA	NA	NA
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	31/03/2012	31/07/2012	M	Q	I
Stocks of Central Government and Central Government-Guaranteed Debt[5]	31/03/2012	31/07/2012	Q	Q	I
External Current Account Balance	31/12/2011	31/07/2012	A	I	I
Exports and Imports of Goods and Services	31/12/2011	31/07/2012	A	I	I
GDP/GNP	1992	NA	A	I	I
Gross External Debt	31/03/2012	31/07/2012	Q	Q	Q
International Investment Position[6]	NA	NA	NA	NA	NA

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means, as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Interest rate data cover the saving rate, deposit rate, and lending rate.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

INTERNATIONAL MONETARY FUND

LIBERIA

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION AND REQUEST FOR THREE-YEAR ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS[1]

November 2, 2012

Approved By
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The Debt Sustainability Analysis which incorporates an increase in borrowing and public investment indicates that Liberia continues to have a low risk of debt distress. The macroeconomic assumptions are underpinned by developments in the iron ore sector. In the near term, foreign financed investment provides a boost to growth and leads to a widening of the current account deficit. Going forward, an increase in iron ore exports and a winding down of import-intensive investments support a narrowing in the current account. Consistent with the Government of Liberia's debt management policy, the DSA assumes a ceiling on annual foreign currency borrowing of 4 percent of GDP in present value terms to support public investment, particularly in energy and transportation infrastructure. The projected present value of the external debt stock would remain low and sustainable with all debt indicators below the policy-related thresholds.

[1]The LIC-DSA incorporates the following general assumptions: (i) the discount rate is fixed at 4 percent; (ii) the exchange rates are based on WEO assumptions; and (iii) the risk of debt distress based on country-specific policy-dependent thresholds, based on the country's CPIA index, which for Liberia is 3.0. All data refers to the fiscal year which runs from July to June.

I. KEY ASSUMPTIONS UNDER THE BASELINE SCENARIO

1. **Liberia has recorded solid macroeconomic performance and is increasing external borrowing for key public investment projects while maintaining low debt vulnerabilities**. Having achieved HIPC completion point in June 2010 and successful completion of the three-year IMF Extended-Credit Facility (ECF) Arrangement, the authorities are now focused on scaling-up much needed public investment, especially in energy and transport infrastructure. Increasing foreign currency borrowing to 4 percent of GDP in PV terms is in line with maintaining low debt vulnerabilities while providing room for higher public investment. External debt would rise to 27 percent of GDP in 2014/15, from 10 percent of GDP in 2011/12. Central government domestic debt at 17.6 percent of GDP in 2011/12, of which 95 percent is foreign currency denominated, is expected to gradually fall to 12.8 percent by 2014/15.[2]

2. **The key change in the baseline scenario compared with the previous DSA is a revision to the underlying level of GDP in line with new national accounts estimates (Box 1)**. Nominal GDP has been revised upwards by close to one third based on survey data which takes better account of the services sector. Growth rates between 2008 and 2012 have also been revised upward, by an average of 1.5 percentage points, because the services sector is estimated to be significantly faster growing than most non-service sectors. Overall, growth prospects in the medium-term are 1.4 percentage points higher on average than in the previous DSA, mostly related to faster than expected growth in the services sector and higher public investment in line with the authorities' draft second poverty reduction strategy (PRS2) (Boxes 2 and 3). This higher investment is financed through external borrowing in line with the agreed debt limit resulting in larger fiscal deficits in the near term. The current account is also expected to be larger than the previous DSA, by close to 5 percentage points of GDP on average in the medium term, related to lower export growth in the commodities sector.

[2] Liberia is a highly dollarized economy. The de jure exchange rate regime is classified as 'managed float'. For more information see Article IV Consultation and the new ECF Arrangement, Informational Annex (2012).

3. **There are significant risks to the baseline scenario, particularly around developments in the concessions sector and in commodity prices**. The baseline scenario takes a cautious approach on the prospects for the initiation in iron ore production and only includes operations for one concession over the projection period. As a result economic growth, exports and fiscal revenues are relatively conservative estimates. At the same time, a decline in commodity prices, particularly in the iron ore sector, could have a significant impact on investment, the external position and revenues.

Box 1. Key Baseline Macroeconomic Assumptions

Real GDP growth in the non-mining sector is assumed to accelerate in the next few years, supported by the public investment program and services sector. Real annual growth including the mining sector is expected to average 7 percent between 2012/13 and 2015/16 as production capacity in the mining sector increases. Growth then fluctuates around an average rate of 6 percent, ending at 5.5 percent at the end of the projection period. There are potential upsides to the growth projection if additional iron ore concessions begin production, ongoing petroleum exploration identifies commercially viable oil deposits, and the government succeeds in securing financing for the more ambitious development program.

Inflation in local currency (GDP deflator index) is expected to be 6 percent on average in 2012/13 and then averages 5 percent from 2014 onwards.

The merchandise trade deficit widens sharply over the next four years due to a strong increase mining-related imports. However, the strong pick-up in iron ore production in 2015 supports a gradual decline in the trade deficit.

Export growth in the near term is lower than in the previous DSA, due to lower commodity prices, particularly for rubber and iron ore. From 2012/13 to FY2014/15 export growth accelerates to a peak of 23 percent due to the initiation of iron ore exports. Exports of goods and services then slow, growing at an average of 4 percent from 2016/17 to 2029/30.

Import growth, largely driven by imports of capital goods related to the iron ore sector, is partially offset by lower imports by UNMIL as a result of the expected drawdown. Between 2012/13 and 2015/16 import growth in goods is 13 percent, while services imports fall by average of 10 percent. From 2018/19 onwards these effects are phased out and the average annual growth in goods and services is expected to be 5 percent.

The current account deficit of the balance of payments widens to 64 percent of GDP in 2013/14 in line with investment in the iron ore sector. Following this, the current account deficit narrows rapidly to 32 percent of GDP in 2015/16. Beyond this the current account narrows averaging 15 percent of GDP.

Tax revenues are projected to remain stable at around 19.5 percent of GDP during the projection period.

The external borrowing policy was agreed in the IMF ECF-supported program with annual external borrowing up to 4 percent of GDP in NPV terms on average between 2012/13-2014/15. The Government's Agenda for Transformation (PRS2) places emphasis on addressing the large infrastructure needs, particularly in the energy and transportation sectors. Part of this investment is expected to be financed through external borrowing raising external debt to GDP from 8 percent of GDP in 2011/12 to 22 percent of GDP in 2014/15. Beyond this, borrowing is expected to gradually stabilize at 2 percent of GDP in 2022/23. All new external borrowing is assumed to be on concessional (IDA) terms. Domestic borrowing, supplied through a planned Treasury bill market, is assumed constant at 1 percent of GDP per year beginning in 2016/17.

External grants (excluding UNMIL) are expected to progressively decline from 21 percent of GDP in 2012/13 to about 17 percent in 2015/16. Beyond this, grants are projected to decline to 10 percent of GDP by the end of the projection period.

Box 2. Liberia: Agenda for Transformation (2012–17)

The Agenda for Transformation is a five-year development plan that underpins Vision 2030 to achieve middle-income status by 2030. The plan focuses on investments in five strategic pillars—at an estimated cost of $3.3 billion over the five-year period—to increase productivity, boost economic growth, and improve social inclusion, particularly among youth. The pillars are

- *Economic transformation*, particularly rehabilitating the hydropower plant, roads, and ports, and updating information and communications technology;
- *Human development* especially education and health;
- *Peace, security, and the rule of law*;
- *Governance and public institutions* to modernize the public sector and enhance transparency and accountability; and
- *Cross-cutting issues* focussed on youth skills, child protection, gender equality, and human rights.

Financing the investment program

- The government plans to cover 12–15 percent of investments with its own resources and is planning a pledging donors' conference in late 2012 to secure loans and grants.

Liberia: Agenda for Transformation Costing Summary (million US dollars)

	FY 12/13	FY 13/14	FY 14/15	FY 15/16	FY 16/17	Five year
Pillar 1. Economic Transformation	594.1	532.4	439.4	354.9	267.8	2,188.6
Pillar 2. Human Development	87.2	100.9	120.8	121.1	128.9	558.9
Pillar 3. Peace, Security, and Rule of Law	73.1	90.3	92.1	77.1	73.0	405.6
Pillar 4. Governance and Public Institutions	40.3	16.5	14.5	14.1	10.0	95.5
Pillar 5. Cross-cutting Issues	19.5	28.7	22.5	22.1	19.2	111.9
Total	814.2	768.9	689.3	589.2	498.9	3,360.5

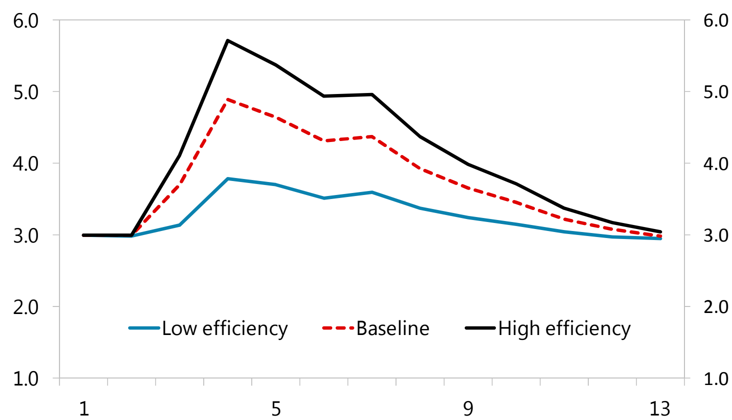
Source: Ministry of Finance, Agenda for Transformation (As of August 30, 2012).

Box 3. Liberia: Assessing the impact from scaling up investment

A dynamic economic model, calibrated to Liberia specifics, was used to simulate the macroeconomic impact of scaling up infrastructure investment and improving project efficiency.[1] As the model focuses on identifying the return from public investment relative to a stable long-term trend and other modeling differences, the estimates are not directly comparable to the underlying macroeconomic framework used in the DSA. Starting from Liberia's low base of investment of close to 3 percent of GDP, a 5 percentage point of GDP increase in investment over a seven year period was modeled.

Liberia: Real Per Capita Income Growth

(Percentage change, y.o.y)



Sources: IMF staff calculations.

Estimates suggest public investment would contribute an additional 1 percentage point each year to real GDP per capita over ten years. The growth effect peaks 3–4 years after the initial investment and then gradually declines over time. The estimate assumes an efficiency rate of public investment of around 60 percent. Assuming an improvement in the efficiency rate to 80 percent, consistent with improved project selection and strengthened execution capacity, real per capita income growth could potentially increase by an additional half percentage point over the medium term. Given the caveats associated with this exercise, the simulation should be seen as an approximation rather than a forecast.

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[1] The average for low income countries. The efficiency rate measures the rate at which executed public investment translates into productive capital. For more details see Buffie, E. A. Berg, C. Patillo, R. Portillo, and L. Zanna, 2012, "Public Investment, Growth, and Debt Sustainability: Putting Together the Pieces." IMF WP No. 12/144.

II. EXTERNAL DEBT SUSTAINABILITY

4. **Following HIPC debt relief, Liberia's external debt is forecast to rise steadily, due to increased new concessional borrowing to fund infrastructure development**. (Tables 1 and Figure 1). In the medium term, the PV of debt-to-GDP ratio is projected to rise steadily from 10.7 percent in 2012/13 to 16.1 percent by 2014/15, reaching 19.8 percent by 2018/17 and gradually declining thereafter. Debt service increases moderately over time, peaking in 2021/22. Due to the concessional nature of debt together with rising exports and revenues from iron ore production, debt and debt service indicators remain well below the country-specific debt burden thresholds. These thresholds are based on an assessment of country policies and institutions compiled annually by the World Bank (CPIA).[3]

5. **The sensitivity analysis shows that the debt indicators remain within sustainable limits** (Figure 1 and Tables 2a and 2b).

- **PV of external debt-to-GDP ratio**. Under the alternative scenario of less favorable borrowing terms the PV of external debt-to-GDP rises close to, but remains below, the 30 percent threshold. Given that the majority of debt is expected to be contracted on fixed interest rates, the impact of this scenario is likely to be more limited. The historical scenario shows that if key macroeconomic variables return to their average between 2004/05 to 2011/12 debt reaches close to the threshold of 30 percent of GDP towards the end of the projection period. However, as noted in the previous DSA the risk associated with this scenario is low due to very unreliable historical data following the end of an extensive period of political and social instability.[4] In addition, the historical scenario is relatively less severe than the previous DSA due to the revision to GDP data and higher private external financing flows.
- **PV of external debt and debt service-to-exports ratio**. The PV of external debt-to-exports ratio is most sensitive to the historical scenario, interest rate shock and export growth shock but remains below the threshold of 100 percent. The debt service ratio remains well below the threshold of 15 percent in all scenarios.

[3] See Classification of Low-Income Countries for the Purpose of Debt Limits in Fund-Supported Programs: 2011 Update (IMF, 2011). With a CPIA rating below 3.25 on average for the past three years, Liberia is classified as a "weak" policy performer. This implies debt burden thresholds of 30 percent for the PV of debt-to-GDP ratio, 100 percent for the PV of debt-to-exports ratio, 200 percent for the PV of debt-to-revenue ratio, 15 percent for debt service-to-exports ratio, and 18 percent for the debt service-to-revenue ratio.

[4] The historical scenario relies on averages between 2004/05 to 2011/12.

- **PV of external debt and debt service-to-revenue ratio**. The PV of external debt-to-revenue ratio is slightly sensitive under alternative and stress scenarios showing some sensitivity to exports and less favorable borrowing terms. Both the debt and debt service-to-revenue ratios are well below the policy thresholds in all scenarios throughout the projection period.

III. PUBLIC SECTOR DEBT SUSTAINABILITY

6. **Following the resumption of new borrowing after debt relief, the baseline scenario of all public debt indicators will rise moderately** (Figure 2, Table 3). Under the baseline scenario the PV of public debt-to-GDP rises slightly to 25 percent of GDP and remains broadly stable. The PV of debt-to-revenue ratio rises to a peak of close to 90 percent of GDP and then follows a slight downward path towards the end of the projection period. The PV of debt service-to-revenue ratio follows a similar trajectory, rising to 5 percent of GDP over the projection period.

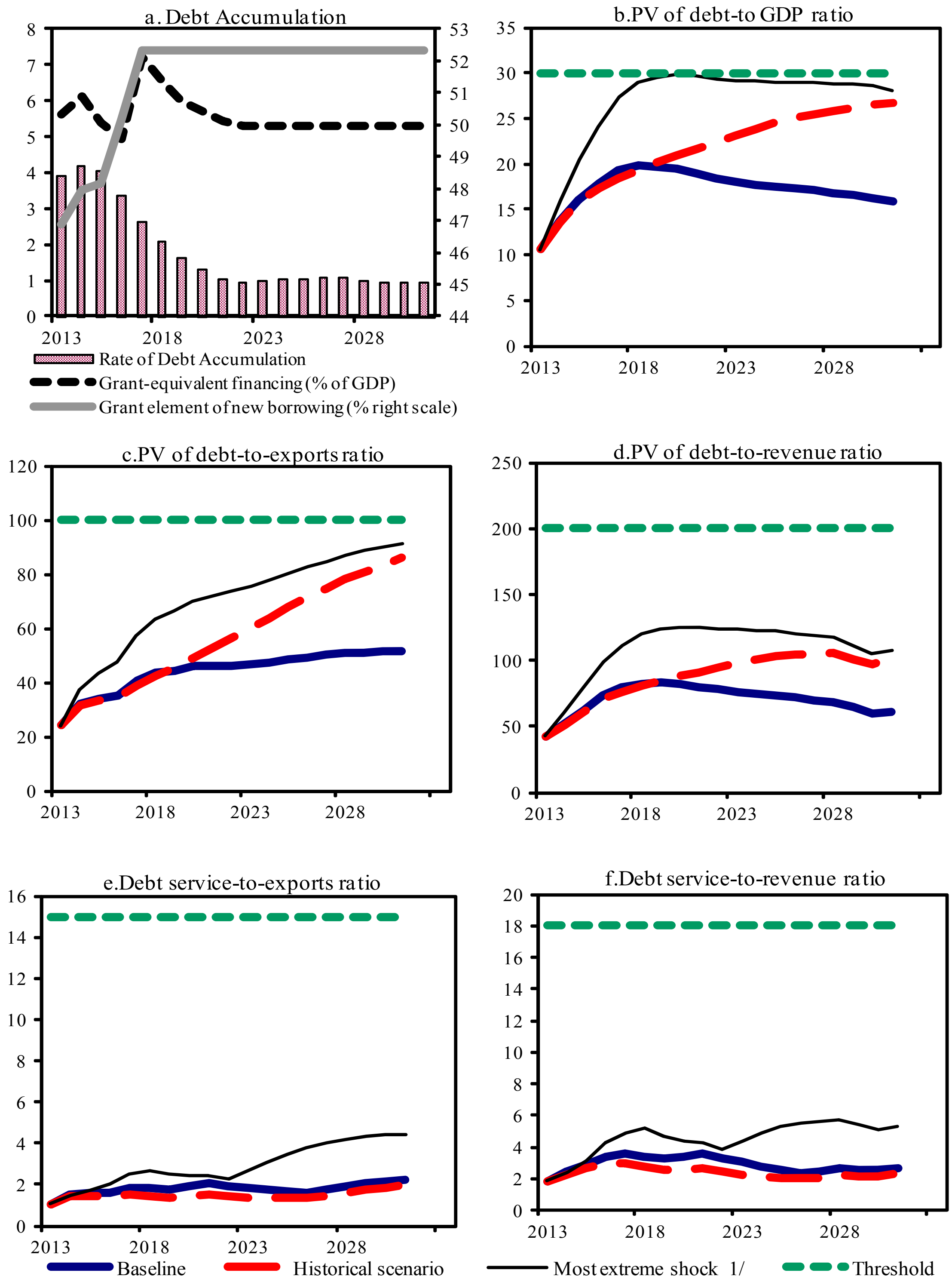
7. **Alternative and shock scenarios highlight the potential risks associated with a lower GDP growth** (Table 4). Under the alternative scenario of a shock to GDP growth in 2013/14 and 2014/15[5] the PV of debt-to-GDP ratio will increase from 10.8 percent in 2010/11 to about 90 percent by the end of the projection period. The PV of the public debt-to-revenue ratio also deteriorates under the growth shock scenario, reaching close to 300 percent by the end of the projection period. However, the debt service-to-revenue ratio will remain reach around 15 percent under an alternative scenario of lower GDP growth.

IV. CONCLUSION

8. **The increase in debt in Liberia to finance much needed public infrastructure investments is consistent with maintaining low debt vulnerabilities**. The authorities are committed to borrow only for investment and to maintain debt sustainability. The underlying macroeconomic assumptions and DSA results were discussed with the authorities. In the baseline scenario, which assumes new foreign currency borrowing of 4 percent of GDP on concessional terms, increased investment, and moderate rates of growth, all external debt burden indicators remain below their policy-dependent thresholds. While there are risks to the baseline, particularly from adverse changes in commodity markets, the key debt and debt service indicators remain below the indicative thresholds.

[5] Defined as a one standard deviation shock to average GDP growth between 2004/05-2011/12, implying growth of -2.7 percent in both FY14 and FY15.

Figure 1. Liberia: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2013-2033 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2023. In each figure it corresponds to a terms shock where public sector loans are on less favourable terms.

Table 2a.Liberia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013-2033
(In percent)

	Projections							
	2013	2014	2015	2016	2017	2018	**2023**	2033
PV of debt-to GDP ratio								
Baseline	11	14	16	18	19	20	**18**	14
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	11	14	16	17	18	19	**23**	27
A2. New public sector loans on less favorable terms in 2013-2033 2	11	16	20	24	27	29	**29**	26
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	11	14	16	18	19	20	**18**	14
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	11	15	22	23	25	25	**22**	16
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	11	13	15	17	19	19	**17**	14
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	11	22	21	22	23	24	**21**	15
B5. Combination of B1-B4 using one-half standard deviation shocks	11	7	-5	-2	0	1	**3**	8
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	11	19	23	25	27	28	**25**	20
PV of debt-to-exports ratio								
Baseline	24	32	34	35	40	43	**47**	51
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	24	32	33	34	39	42	**60**	95
A2. New public sector loans on less favorable terms in 2013-2033 2	24	37	43	47	57	63	**76**	93
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	24	32	33	35	40	43	**46**	50
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	24	36	60	60	67	71	**74**	72
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	24	32	33	35	40	43	**46**	50
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	24	51	43	43	49	52	**55**	54
B5. Combination of B1-B4 using one-half standard deviation shocks	24	17	-12	-5	-1	3	**9**	33
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	24	32	33	35	40	43	**46**	50
PV of debt-to-revenue ratio								
Baseline	43	52	62	73	79	83	**76**	63
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	43	51	61	71	76	81	**98**	118
A2. New public sector loans on less favorable terms in 2013-2033 2	43	60	79	99	112	121	**123**	115
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	43	52	63	73	80	83	**77**	64
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	43	55	86	96	102	105	**94**	70
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	43	50	60	70	76	79	**73**	60
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	43	83	80	90	96	99	**89**	67
B5. Combination of B1-B4 using one-half standard deviation shocks	43	27	-19	-9	-1	4	**12**	35
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	43	73	87	102	111	116	**107**	88

Table 2b.Liberia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013-2033 (continued)
(In percent)

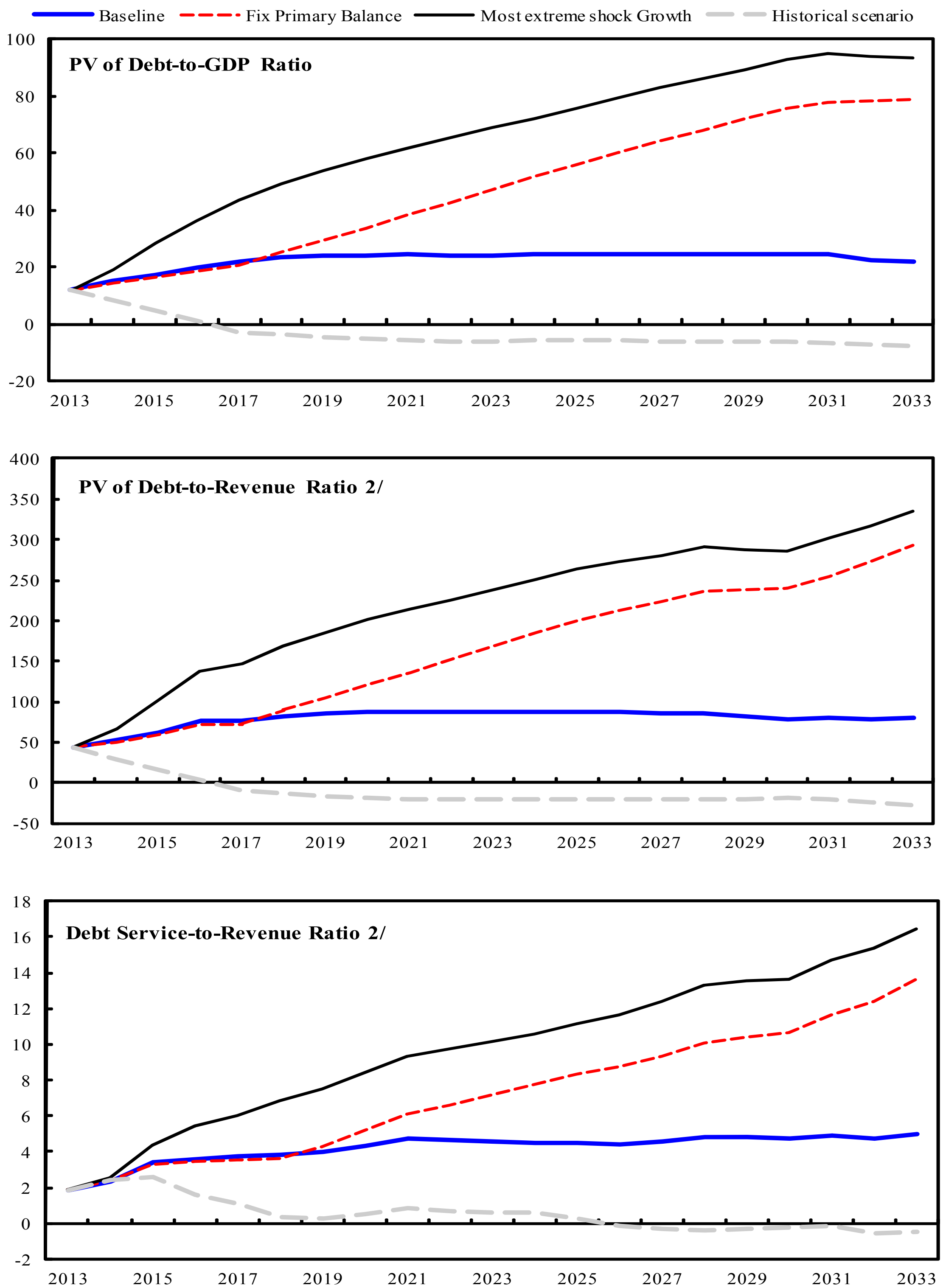
Debt service-to-exports ratio

Baseline	1	2	2	2	2	2	**2**	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	1	1	1	1	2	1	**1**	2
A2. New public sector loans on less favorable terms in 2013-2033 2	1	2	2	2	3	3	**3**	5
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	1	2	2	2	2	2	**2**	2
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	1	2	2	2	3	3	**3**	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	1	2	2	2	2	2	**2**	2
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	1	2	2	2	2	2	**2**	3
B5. Combination of B1-B4 using one-half standard deviation shocks	1	1	2	1	1	1	**2**	1
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	1	2	2	2	2	2	**2**	2
Debt service-to-revenue ratio								
Baseline	2	2	3	3	4	3	**3**	3
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2013-2033 1/	2	2	3	3	3	3	**2**	3
A2. New public sector loans on less favorable terms in 2013-2033 2	2	2	3	4	5	5	**4**	6
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	2	2	3	3	4	4	**3**	3
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	2	2	3	4	4	4	**3**	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	2	2	3	3	3	3	**3**	3
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	2	2	3	4	4	4	**3**	3
B5. Combination of B1-B4 using one-half standard deviation shocks	2	2	2	2	2	2	**2**	1
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	2	3	4	5	5	5	**4**	4
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	48	48	48	48	48	48	**48**	48

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Figure 2.Liberia: Indicators of Public Debt Under Alternative Scenarios, 2013-2033 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2023.
2/ Revenues are defined inclusive of grants.

Table 3.Liberia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2010-2033
(In percent of GDP, unless otherwise indicated)

	Actual			Average 5/	Standard Deviation 5/	Estimate	Projections								
	2010	2011	2012			2013	2014	2015	2016	2017	2018	2013-18 Average	2023	2033	2019-33 Average
Public sector debt 1/	142.8	10.0	11.7			17.1	23.4	28.0	32.6	36.9	38.8		38.3	32.4	
o/w foreign-currency denominated	142.7	10.0	11.7			17.1	23.4	28.0	31.6	35.0	36.1		32.6	25.2	
Change in public sector debt	-131.4	-132.8	1.7			5.4	6.2	4.6	4.6	4.3	1.9		-0.4	-1.3	
Identified debt-creating flows	-37.6	-133.0	1.8			4.8	5.4	3.9	4.2	4.7	0.2		-1.6	-1.4	
Primary deficit	-0.5	0.4	3.1	-0.3	2.1	5.9	6.5	6.0	6.5	6.1	2.6	5.6	0.6	1.1	0.9
Revenue and grants	23.5	26.4	27.8			27.3	28.8	27.6	26.0	28.7	28.2		27.9	27.0	
of which: grants	1.1	2.8	1.7			2.4	2.3	1.8	1.6	4.3	4.3		4.3	4.3	
Primary (noninterest) expenditure	23.0	26.9	31.0			33.2	35.3	33.6	32.5	34.8	30.8		28.5	28.1	
Automatic debt dynamics	-3.9	-21.4	-1.3			-1.0	-1.1	-2.1	-2.3	-1.4	-2.3		-2.1	-2.5	
Contribution from interest rate/growth differential	-17.6	-11.7	-0.9			-0.9	-1.1	-1.5	-1.8	-1.9	-2.6		-2.2	-1.8	
of which: contribution from average real interest rate	-2.8	-2.1	-0.1			0.0	0.0	-0.1	-0.2	-0.2	-0.2		0.0	-0.1	
of which: contribution from real GDP growth	-14.8	-9.6	-0.8			-0.9	-1.1	-1.4	-1.6	-1.7	-2.4		-2.1	-1.7	
Contribution from real exchange rate depreciation	13.8	-9.7	-0.4			-0.1	0.1	-0.6	-0.5	0.5	0.3		...	...	
Other identified debt-creating flows	-33.2	-112.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	-33.2	-112.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-93.8	0.2	-0.1			0.6	0.9	0.7	0.4	-0.5	1.7		1.2	0.1	
Other Sustainability Indicators															
PV of public sector debt	...	...	9.5			12.0	15.0	17.0	19.6	22.0	23.3		24.2	21.7	
o/w foreign-currency denominated	...	...	9.5			12.0	15.0	17.0	18.6	20.1	20.6		18.6	14.6	
o/w external	...	...	7.9			10.6	13.8	16.1	17.8	19.3	19.8		18.0	14.3	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	-0.3	0.9	3.6			6.4	7.1	6.9	7.4	7.2	3.7		1.8	2.5	
PV of public sector debt-to-revenue and grants ratio (in percent)	…	…	34.1			44.0	52.1	61.8	75.6	76.8	82.5		86.6	80.5	
PV of public sector debt-to-revenue ratio (in percent)	…	…	36.3			48.3	56.7	66.1	80.6	90.3	97.2		102.3	95.6	
o/w external 3/	…	…	30.2			42.7	51.9	62.4	73.0	79.1	82.7		76.2	63.1	
Debt service-to-revenue and grants ratio (in percent) 4/	0.9	1.6	1.8			1.9	2.4	3.4	3.6	3.7	3.9		4.6	5.0	
Debt service-to-revenue ratio (in percent) 4/	1.0	1.8	1.9			2.1	2.6	3.6	3.8	4.4	4.6		5.4	5.9	
Primary deficit that stabilizes the debt-to-GDP ratio	130.9	133.2	1.4			0.5	0.2	1.4	1.9	1.8	0.6		1.0	2.5	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	5.7	7.2	8.5	5.0	7.7	8.6	6.9	6.4	6.1	5.6	7.1	6.8	5.8	5.4	5.8
Average nominal interest rate on forex debt (in percent)	0.0	0.1	1.1	0.4	0.5	1.4	1.2	1.0	0.9	0.8	0.8	1.0	0.8	0.8	0.8
Average real interest rate on domestic debt (in percent)	3.0	-7.5	-6.5	-5.8	6.3	-4.8	...	...	...	17.1	11.2	7.8	6.7	3.0	6.1
Real exchange rate depreciation (in percent, + indicates depreciation)	5.4	-7.4	-4.7	-4.3	4.4	-0.9	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	0.4	11.4	9.7	10.1	4.3	6.0	4.3	7.6	6.8	3.3	4.2	5.4	5.1	8.2	5.5
Growth of real primary spending (deflated by GDP deflator, in percent)	0.1	0.2	0.3	0.2	0.4	0.2	0.1	0.0	0.0	0.1	-0.1	0.1	0.0	0.0	0.1
Grant element of new external borrowing (in percent)	...	...	...	…	…	46.9	48.0	48.2	50.2	52.3	52.3	49.6	52.3	52.3	...

Sources: Country authorities; and staff estimates and projections.

1/ The public sector comprises the central government, the Central Bank of Liberia (CBL), public enterprises and other official entities.

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are derived over 2004/05 to 2009/10.

Table 4.Liberia: Sensitivity Analysis for Key Indicators of Public Debt 2013-2033

(In percent of GDP, unless otherwise indicated)

	Projections							
	2013	2014	2015	2016	2017	2018	2023	2033
PV of Debt-to-GDP Ratio								
Baseline	12	15	17	20	22	23	24	22
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	12	8	5	1	-3	-4	-6	-8
A2. Primary balance is unchanged from 2013	12	14	16	18	21	25	47	79
A3. Permanently lower GDP growth 1/	12	16	19	23	28	31	49	109
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	12	19	28	36	44	49	69	93
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	12	10	8	12	14	16	18	17
B3. Combination of B1-B2 using one half standard deviation shocks	12	10	7	13	19	23	37	53
B4. One-time 30 percent real depreciation in 2014	12	19	19	20	22	23	25	24
B5. 10 percent of GDP increase in other debt-creating flows in 2014	12	25	26	29	31	32	31	26
PV of Debt-to-Revenue Ratio 2/								
Baseline	44	52	62	76	77	82	87	80
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	44	29	16	4	-10	-13	-21	-28
A2. Primary balance is unchanged from 2013	44	50	59	71	72	89	168	293
A3. Permanently lower GDP growth 1/	44	54	68	89	95	109	172	380
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	44	66	101	137	147	169	239	335
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	44	36	31	45	49	56	64	65
B3. Combination of B1-B2 using one half standard deviation shocks	44	34	25	51	65	80	129	194
B4. One-time 30 percent real depreciation in 2014	44	64	68	78	77	81	88	87
B5. 10 percent of GDP increase in other debt-creating flows in 2014	44	87	96	110	108	113	112	98
Debt Service-to-Revenue Ratio 2/								
Baseline	2	2	3	4	4	4	5	5
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	2	2	3	2	1	0	1	-1
A2. Primary balance is unchanged from 2013	2	2	3	3	4	4	7	14
A3. Permanently lower GDP growth 1/	2	2	4	4	4	5	8	17
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	2	3	4	5	6	7	10	16
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	2	2	3	2	3	3	4	4
B3. Combination of B1-B2 using one half standard deviation shocks	2	2	3	2	3	4	6	10
B4. One-time 30 percent real depreciation in 2014	2	3	5	5	5	5	6	7
B5. 10 percent of GDP increase in other debt-creating flows in 2014	2	2	5	5	5	5	6	6

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 12/143
FOR IMMEDIATE RELEASE
December 14, 2012

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2012 Article IV Consultation with Liberia

On November 19, 2012, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Liberia.[1]

Background

Since the last Article IV consultation concluded in December 2010, prudent fiscal policy and strengthened public financial management have contributed to a near doubling of government revenue, resumption of direct budget support, and initiation of significant infrastructure development projects without accumulation of expenditure arrears. Monetary policy has focused on accumulating reserves, which sizably outperformed expectations during the period. Financial policies focused on strengthening the banking system and promoting intermediation.
Economic activity remains robust in 2012, with inflation moderating at or near single digits and the exchange rate is stable. Following resumption of iron ore exports in 2011—for the first time since the end of the civil war—real GDP growth is estimated at close to 9 percent in 2012, driven by mining, construction, and services albeit growth in agriculture and forestry remains sluggish. Foreign direct investment is increasing. Following spikes in food and fuel prices in 2011 and early 2012, U.S. dollar-denominated inflation declined to under 4 percent by end-June and is expected to remain in single digits through end-2012. The trade deficit has widened since 2010 reflecting concession-financed capital imports and rising food and fuel import prices which

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

more than offset the increase in iron ore exports. Reserve coverage has remained relatively stable at about 2½ months of imports.

While medium-term prospects are bright, notably in the commodity export sectors, broad-based growth is necessary to reduce high levels of underemployment and widespread poverty. To this end, the authorities' draft second poverty reduction strategy focuses on achieving accelerated broad-based growth through scaling up of investment in infrastructure and human capital, raising agricultural productivity, employment creation, especially youth employment, and deepening financial markets. To support this strategy, efforts are needed to create fiscal space for higher capital spending by containing personnel costs and other current transfers, while future commodity revenues would need to be channeled to infrastructure financing and capacity building to enhance competitiveness. Financial sector development and improving access to credit would help support the private sector. Further reforms are necessary to improve public financial management, governance, and the business environment.

Executive Board Assessment

Executive Directors welcomed Liberia's progress in improving macroeconomic and social conditions under the recently concluded Extended Credit Facility (ECF) arrangement. Directors noted that the economic outlook is favorable, but that daunting policy challenges remain, including safeguarding macroeconomic stability and strengthening the foundation for broad-based and lasting growth.

Directors emphasized the need to expand fiscal space for infrastructure and social spending. They considered that the FY2012/13 budget is appropriately focused on increasing public investment, but called for additional efforts to contain current spending beyond the recently adopted rule for public sector wages.

More broadly, Directors highlighted the need to strengthen public financial management and address capacity constraints that hamper capital spending. They stressed the importance of keeping external borrowing within sustainable levels, seeking external concessional financing, and strengthening the management of foreign aid. Directors also recommended putting in place a framework for managing natural resource revenue, which would bolster Liberia's ability to cope with export price volatility and improve governance.

Directors supported efforts to strengthen the implementation of monetary policy. They welcomed the authorities' pursuit of de-dollarization and their plans to improve liquidity management through the issuance of treasury bills. Directors also saw merit in increasing official foreign exchange reserves as a buffer against shocks.

Welcoming the authorities' progress in implementing risk-based supervision and improving the payments system, Directors highlighted the importance of further promoting financial intermediation. Directors expressed concerns, however, about elevated non-performing loans in the banking system, and called for heightened vigilance by the authorities.

Directors agreed that accelerated structural reforms on a broad front remain essential to raise Liberia's growth path and reduce poverty. Steps to improve the business climate and lay the groundwork for private sector development and employment remain a top policy priority.

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

Liberia: Selected Economic and Financial Indicators, 2009–13

	2009	2010	2011	2012 Proj.	2013 Proj.
	(Annual percentage change, unless otherwise indicated)				
National account and prices					
Real GDP	5.3	6.1	8.2	8.9	8.3
GDP deflator (US dollars)	-1.7	5.4	10.6	5.0	1.1
Nominal GDP (millions of US dollars)	1,155.1	1,291.9	1,545.4	1,767.5	1,934.4
Consumer prices (annual average)	7.4	7.3	8.5	6.6	5.6
External sector					
Exports, f.o.b.	-39.7	40.4	77.0	23.8	14.3
Imports, f.o.b.	-19.0	17.4	49.9	33.3	16.1
Terms of trade (deterioration -)	-9.2	76.8	16.1	-24.1	-2.5
Average exchange rate (local currency per U.S. dollar)	68.3	71.4	72.2	…	…
Gross official reserves (millions of US dollars)	312.2	391.4	425.1	452.0	462.0
Import coverage of reserves (months) [1]	3.2	3.5	2.9	2.2	2.1
Central government operations [2]					
Total revenue and grants	13.5	22.6	30.2	23.0	9.7
Of which: total revenue	5.2	30.2	21.7	29.3	6.5
Total expenditure and net lending	26.3	13.4	35.7	34.3	19.9
Of which: current expenditure	24.2	16.4	23.5	44.3	5.9
capital expenditure	41.5	-6.2	131.7	-7.8	111.8
Money and credit					
Reserve money	12.4	33.9	49.7	13.8	12.1
Broad money (M2) [3]	36.7	35.4	34.6	17.4	12.6
Credit to private sector	31.5	40.1	32.4	14.4	9.4
	(Percent of GDP)				
External sector					
Current account balance					
(including official grants)	-28.8	-32.8	-34.1	-52.4	-62.4
(excluding official grants)	-148.2	-152.0	-149.3	-131.5	-97.4
Trade balance	-36.4	-35.5	-40.7	-49.5	-53.0
Exports, f.o.b.	13.3	16.7	24.6	26.7	27.9
Imports, f.o.b.	-49.7	-52.2	-65.4	-76.2	-80.9
Central government operations [2]					
Total revenue and grants	20.7	23.5	26.4	27.8	27.3
Of which: total revenue	18.6	22.5	23.6	26.1	24.9
Total expenditure and net lending	21.9	23.1	27.0	31.0	33.3
Of which: current expenditure	18.9	20.5	21.8	27.0	25.6
capital expenditure	3.0	2.6	5.2	4.1	7.8
Overall fiscal balance (including grants)	-1.2	0.5	-0.6	-3.2	-6.0
Public external debt	145.4	8.8	10.7	12.1	14.8

Sources: Liberian authorities and IMF staff estimates and projections.

[1] Excluding imputed UN military services imports.

[2] Fiscal year ending in June on a cash basis (debt service payments shown after all debt relief).

[3] Defined as Liberian currency outside banks plus demand, time, and savings deposits in Liberian and US dollars.

INTERNATIONAL MONETARY FUND
EXTERNAL RELATIONS DEPARTMENT

Press Release No. 12/449
FOR IMMEDIATE RELEASE
November 19, 2012

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves Three-Year, US$78.9Million ECF Arrangement for Liberia

The Executive Board of the International Monetary Fund (IMF) today approved a three-year Extended Credit Facility (ECF)[1] Arrangement for Liberia in an amount equivalent to SDR 51.68 million (about US$78.9 million). The overall amount of the program represents 40 percent of Liberia's quota in the IMF and approval enables the immediate disbursement of SDR 7.382 million (about US$11.3 million). The Executive Board also concluded the 2012 Article IV consultations with Liberia, which will be detailed in a Public Information Notice in due course.

Following the Executive Board's discussion of Liberia, Mr. Min Zhu, Deputy Managing Director and Acting Chair, made the following statement.

"Liberia made strong macroeconomic gains under the recent Extended Credit Facility (ECF) arrangement supported by the Fund. Economic growth has been robust; inflation has been largely contained; international reserves have been built up; and external debt has been reduced through substantial debt relief. However, further reforms are needed to promote broad-based growth, reduce poverty, and create jobs, particularly for the youth.

"The new ECF arrangement aims to support the authorities' second poverty reduction strategy. The policy priorities focus on safeguarding macroeconomic stability and laying the basis for faster and diversified growth through a substantial scaling up of infrastructure and social investments.

"Growth will be underpinned by sound macroeconomic policies, higher investment, and vigorous implementation of structural reforms. Fiscal reforms focus on containing current spending, particularly the wage bill, and strengthening budget execution and controls, through improvements in public financial management. An increase in external debt limits will allow a scaling up of critical growth-enhancing investments while maintaining debt sustainability. Measures are also planned to further improve governance and transparency, including financial

[1] The Extended Credit Facility (ECF) has replaced the Poverty Reduction and Growth Facility (PRGF) as the IMF's main tool for medium-term financial support to low-income countries. It provides for a higher level of access to financing, more concessional terms, enhanced flexibility in program design, and more focused, streamlined conditionality. Financing under ECF currently carries a zero interest rate, with a grace period of 5½ years, and a final maturity of 10 years.

oversight of state-owned enterprises, streamlining procurement procedures, improving project execution, and establishing a natural resource revenue unit at the Ministry of Finance. Financial sector reforms focus on reducing vulnerabilities and improving access to credit."

Recent Economic Developments

Liberia made strong macroeconomic gains under a successful ECF program initially approved in 2008 for three years and later extended to May 2012 (see Press Release No. 12/165). The short- to medium-term outlook remains favorable, although subject to considerable risks. Following an initial post-conflict boost, economic growth has averaged 7 percent a year since 2009 (mostly from non-mining activities before the resumption of iron ore exports in late 2011), while inflation has been largely contained at or near single digits. With the resumption of iron ore exports in 2011, real gross domestic product (GDP) growth is estimated at close to 9 percent in 2012, supported by strong growth in the mining sector and expansionary fiscal policy to accommodate a scaling up of infrastructure investment.

Foreign direct investment is increasing. Following spikes in food and fuel prices in 2011 and early 2012, U.S. dollar-denominated inflation declined to under 4 percent by end-June and is expected to remain in single digits through end-2012. The trade deficit has widened since 2010 reflecting concession-financed capital imports and rising food and fuel import prices which more than offset the increase in iron ore exports. Reserve coverage has remained relatively stable at about 2½ months of imports.

Nevertheless, Liberia's macroeconomic stability has been hard won and its development challenges are daunting. It remains a poor country, with massive infrastructure gaps and large development needs. Poverty remains pervasive (at 84 percent of the population), and Liberia ranks near the bottom of the UN's Human Development Index (HDI) and is unlikely to meet many of its Millennium Development Goals.

Program Summary

The ECF arrangement will support the authorities' program to accelerate broad-based growth and poverty reduction, aligned with their Poverty Reduction Strategy, while maintaining macroeconomic stability. Consistent with these objectives, the program has three central objectives:

- Creating fiscal space for higher capital spending by containing personnel costs and other current transfers;

- Strengthening the financial sector through reducing vulnerabilities and improving access to credit; and

- Underpinning growth with structural reforms to further improve public financial management, governance, and the business environment.

Statement by Mr. Momodou Bamba Saho, Executive Director for Liberia
November 19, 2012

Introduction

My Liberian authorities thank the Executive Board, Management and staff for their continued support, particularly since the end of the civil conflict. They appreciate staff input in identifying the policy opportunities and challenges as well as presenting options for the structural transformation of the economy. While significant progress has been achieved in transitioning from post-conflict reconstruction to the path of macroeconomic stability, underpinned by a credible medium-term fiscal framework and sound policies, more remains to be done in the areas of infrastructure and social development to spur robust inclusive growth.

Against this backdrop, my authorities have clearly articulated a comprehensive medium-term strategy to help toward the end goal of reaching middle income status by 2030 in their second generation Poverty Reduction and Growth Strategy (PRS-II), referred to as the "Agenda for Transformation". The authorities' ambitious agenda focuses on investments in infrastructure, human development and institutions to accelerate broad-based growth and attain middle income status. However, the implementation of my authorities' development agenda is severely challenged by inadequate fiscal space and dwindling external financing. It is in this regard that they are asking for the Executive Board's approval of their request for a successor Extended Credit Facility to consolidate macroeconomic stability and boost growth while supporting their Agenda for Transformation.

Recent economic developments

Supported by a strong medium-term fiscal framework and sound macroeconomic policies, economic performance during 2008-2010 was impressive, with real GDP growth averaging 5.9 percent. Inflationary pressures however heightened, due largely to the spike in global food and fuel prices while gross international reserves increased substantially over the period. The external current account deficit widened, reflecting the broad-based expansion in imports to meet the increased domestic demand as the economy expanded. During this period, the country received HIPC debt relief resulting in a large reduction in external debt.

Macroeconomic performance in 2011 continued to be robust with real GDP growth estimated at 8.2 percent compared to 6.1 percent in 2010, reflecting increased activity in agriculture and the resumption of iron ore exports. Inflation increased to 11.4 percent in 2011, largely because of the surge in global food and fuel prices, which also contributed to the widening of the external trade deficit. The exchange rate of the Liberian dollar remained stable and gross international reserves stood at 3.0 months of import cover at the end of 2011.

Outlook

My authorities' overriding policy objective over the near to medium term is to restructure the economy so that it will grow faster, create more jobs, spread the benefits of growth more widely and thereby reduce inequality. As a result, they are determined to invest in key infrastructure and sectors that have high economic and social returns as well as expansionary economic benefits. To this end, real output growth is projected to rise to 8.9 percent in 2012. The major risk to maintaining single-digit inflation in 2012 remains the high global food and energy prices.

My authorities' Agenda for Transformation prioritizes increased allocation of resources to the development of roads, ports, power and water infrastructure as well as human capital. Accordingly, they seek to gradually increase real output growth in the outer years as investment in basic infrastructure and agricultural productivity are realized. The medium-term outlook envisions single digit inflation, decelerating from 11.4 percent in 2011 to 6.6 percent in 2012. With the volatility in the Liberian dollar subsiding, the Central Bank of Liberia (CBL) is expected to rebuild gross international reserves over the medium term.

Fiscal policy

My authorities are committed to maintaining fiscal sustainability over the medium term by pursuing prudent fiscal management, while creating much needed fiscal space to support their Agenda for Transformation. In this context, the overarching objective of fiscal policy is to maintain a sustainable fiscal position consistent with the Public Financial Management Law of 2009. To meet these objectives, a Budget Framework Paper has been prepared outlining some of the macroeconomic assumptions and funding plans for the national budget.

Cognizant of the need to intensify revenue mobilization, my authorities plan to introduce new taxes on inbound telephone calls. They also intend to strengthen the large tax payer unit. In this regard, they plan to establish a natural resource unit in the large taxpayers unit, which will help to monitor prices and ensure that government receives the optimal amount of tax from the sector. In addition, the authorities are working on a new petroleum policy to maximize future revenue windfalls from the oil sector. In this regard, a draft petroleum policy has been prepared and national consultations are ongoing. The draft policy will inform the new petroleum law and management of petroleum revenue. The authorities are working with FAD in these efforts. In the area of tax administration, my authorities are addressing revenue leakages. They plan to launch a robust anti-smuggling campaign and comprehensive audits starting with the largest 20 tax payers, including banks, logging and insurance companies. In addition to these new measures, my authorities plan to maintain the tax reforms introduced last fiscal year.

On expenditure, my authorities are creating fiscal space to boost public investment. This year, the budget allocates sufficient resources to capital projects in order to meet the government's infrastructure investment program. Special attention is given to the restoration of power, rebuilding of roads and ports as well as investing in youth empowerment while augmenting capacity for national development. In the medium term, the authorities intend to complete the Mount Coffee hydroelectric plant and link it to the West African Power Pool to provide cheaper electricity. In this respect, my authorities introduced key fiscal rules. They intend to spend no more than 34 percent of the budget on personnel costs and no more than 15 percent of capital expenditures on administrative overheads, among other things.

Monetary policy

The thrust of monetary policy in 2012 and over the medium term is to maintain price stability in order to support the government's objective of achieving sustainable economic growth and broad-based development. At the moment, efforts are being made to widen the scope of monetary policy instruments available to the CBL to enhance the potency of monetary policy, including the introduction of a Treasury-bill market.

Financial sector policy

In the recent past, the CBL has endeavored to transform the Liberian financial landscape and enhance the soundness of the financial system. This has involved improving access to financial services and taking steps to ensure a relatively stable exchange rate, while strengthening the reserve position of the CBL. Going forward, financial sector policy will continue on the path of reform to promote viability of the banking system, with emphasis on further improving the credit environment and reducing the level of non-performing loans. Furthermore, work will focus on deepening the financial system, increasing private sector access to credit, strengthening consumer protection and consolidating the renewed confidence in the banking system.

The monetary authorities will continue to strengthen the capacity of the regulation and supervision department in critical skills such as risk-based supervision, information technology-based examinations and international financial reporting standards. Already work is in progress to develop a framework for stress testing and conducting macro-prudential analysis of the banking sector as part of efforts to strengthen early warning tools and addressing issues of systemic risk on a more proactive and timely basis.

In promoting financial inclusion, the CBL is committed to supporting the establishment of specialized rural community financial institutions in partnership with interested banks. These institutions will be owned by the local communities and would assist in mobilizing local savings while providing the much needed financial services to the respective communities. In addition, the CBL has been working with credit union movements in Liberia, leading to the hosting of a national congress for credit unions in April 2012 where the internal governance policies and procedures of the Liberian Credit Union National Association were revised and adopted.

Debt management policy

In spite of the post HIPC low risk of debt distress, improved public debt management remains a priority to the authorities. They remain committed to observing the rules governing debt and to never again accumulate an unsustainable debt burden. To meet the required levels of investment in order to fully implement the Agenda for Transformation and position Liberia on a trajectory to a middle income country by 2030, the government intends to pursue opportunities to borrow within sustainable levels. The borrowing will be done responsibly in accordance with the following fiscal rules:

- All borrowing must be undertaken for the purposes of investment, consistent with the public sector investment plan;

- Total cumulative outstanding debt stock, including domestic debt, must not exceed 60 percent of previous calendar year's GDP as contained in the PFM Regulation; and

- Prior to new borrowing being undertaken a debt sustainability analysis must be carried out and presented to the debt management committee to ensure debt rules are not breached.

Meanwhile, all efforts will be made to ensure that all borrowing is done on concessional terms consistent with the Fund's concessional threshold. However, non-concessional financing for certain projects may be considered in consultation with the Fund.

Conclusion

My Liberian authorities remain mindful of the challenges ahead and are committed to proceed with their five-year medium term development plan, the Agenda for Transformation and the long term strategy, Liberia Rising 2030 to attain middle income status. In this regard, they are resolute in their commitment to implement appropriate revenue enhancing measures to mobilize substantial resources to complement external funding to finance their development plan. However, given the large financing gap and the need for implementing sound macroeconomic policies, my authorities consider the Fund's and other development partners' support essential to achieving their post-conflict development needs.