LETTER OF DEVELOPMENT POLICY

1) This Letter of Development Policy describes the economic and fiscal policies that the government of the Gambia is currently pursuing to return to macroeconomic stability and protect essential public services.

2) Following a difficult political transition in January, we have inherited a looming economic crisis. The past decade has been characterized by weak fiscal management resulting to high recurring fiscal slippages, high borrowing leading to low growth. This has kept borrowing costs high thus crowding out private investment, and constraining fiscal flexibility. The debt service burden on the budget is very high, consuming more than half of government revenues. As a result, constraining government expenditure in priority areas such as health, education, and agriculture. In dealing with these major economic and financial challenges, the government intends to pursue the following priorities: (i) macroeconomic management; (ii) public sector strengthening; (iii) promotion of sustainable, inclusive growth; and (iv) investment in human capital.

3) The government is strongly committed to restoring macroeconomic stability and implementing critical structural reforms to meet these objectives. However, to implement these priorities, the government will require funding from donor partners, to support the implementation of the Gambia Emergency Development Policy Operation (DPO). The emergency program will be executed over 2017 calendar year. The aim of the DPO, aligned with the strategic priorities of government, is to strengthen the Government's fiscal position.
while restoring the provision of essential public services. In addition to funding the state budget, the program will support economic recovery.

CONTEXT

4) The Gambia is at a historical turning point, with transition to a democratically elected government committed to the rule of law, freedom of speech and socio-economic development ending the 22-years of autocratic regime. However, the new government inherited a broken economy, with severe economic mismanagement, mainly from state-owned enterprises (SOEs). In addition to these problems, the economy suffered from poor agricultural season resulting low crop production. Furthermore, the political turmoil following the elections in December 2016 affected tourism season, reducing receipts in the first quarter of 2017 by about one third. This together with large fuel import bill put additional strain on the balance of payments. The economic situation is dire and the country is faced with a very high debt, requiring substantial fiscal financing needs, an urgent balance of payments support characterized by a precariously low level of net international reserves.

5) The government has only been in office since February 2017, and our immediate priority is to prevent the situation escalating into a full-blown crisis. The parliamentary elections on April 6, 2017, resulted in an absolute majority in support of the government and a strong commitment for reform. We will now work expeditiously to restore macroeconomic stability and put policy implementation on a sound and sustainable footing. Our international development partners have been quick to re-engage and have indicated that substantial financial support could be forthcoming, necessary to cope with the acute impact of the shock and the economic mismanagement of the past. Domestically, we are committed to implementing strong fiscal measures and mitigate fiscal shocks, including maintaining fiscal discipline, drastically reducing net domestic borrowing, taking steps to put the public utility and telecom companies on a sound financial footing, protecting health services, and ensuring the sustainability of the public debt.

6) To restore and sustain macro fiscal stability, we need emergency support from our development partners (including World Bank, the African Development Bank, the European Union, IMF etc). The prospective World Bank budget support would be in the amount of $56
million. We will need close engagement with the World Bank staff to further guide policy implementation and articulate medium-term reforms over the coming year. We also recognize the need to establish a track record of strong policy implementation.

GOVERNMENT PROGRAM

7) A new National Development Plan (PAGE II) covering 2018-2021 is close to finalization. We are currently incorporating the findings of the Integrated Households Living Conditions Survey (IHS) and expect to finalize the Plan by mid-2017. It reflects The Gambia’s need for policies aimed at strengthening growth including: i) removing policy uncertainty and bringing back a degree of fiscal control to avoid crowding out private investment; ii) facilitating access to finance; iii) restoring competitiveness in trade and energy.

8) To tackle immediate urgent issues, we have also prepared an Accelerated National Response Plan (ANRP) synthesizing key priorities for 2017. The Gambia’s political impasse of December 2016 led to significant socio-economic challenges that negatively impacted the country. The Gambia’s economy relies primarily on tourism, agriculture, and remittance inflows; making it highly undiversified economy thus rendering the economy vulnerable to external shocks.

9) The purpose of the ANRP is to seek donor support financial or technical in order to widen the fiscal space and ease pressure on the budget, thereby resuscitating the economy, and putting the country on a sound socio-economic and political trajectory to be able to sustainably meet its development aspirations. The plan covers the urgent priorities for the next six-month with a view to serve as a springboard for growth and development in The Gambia. Premised on this, the priorities are based on the identification of activities that will have an immediate multiplier effect on the economy.

10) The revenue base of the Government of The Gambia is very narrow and based mainly on tax. The political impasse that the country experienced between December 2016 and January 2017, led to a downturn in economic activities and negatively impacted Government tax revenues. Tax receipts in January 2017 were GMD200 million below target. Due to this, Government expects that tax receipts will not pick up to the projected levels in the
immediate term. This, in effect, will challenge Government's ability to meet budgetary obligations. It is for this reason that the government is seeking direct budget support from development partners to enable it meet critical budgetary expenditures in key priority areas. The direct budget support will help achieve the objectives to reduce the debt service burden and maintain health and social service delivery, and the quality of basic and secondary education. It will further help mitigate the negative impact of the economic crisis and the difficult political transition, and lay the foundation for the required structural reforms.

RECENT ECONOMIC DEVELOPMENTS AND THE MEDIUM-TERM OUTLOOK

11) Macroeconomic developments in 2016 have been impacted considerably by the economic mismanagement of the previous regime and external shocks. Economic growth in 2016 is now estimated to have reached 2.2 percent, markedly lower than the 4.3 percent growth in 2015, due to limited availability of foreign exchange, weak agricultural output and the effect of the political impasse on tourism during high season. With erratic rainfall during the summer, some 90 percent of the groundnut cash crop will be lost according to the pre-harvest report. Headline annual inflation stood at 8.8 percent in February 2017, well above the CBG's target of 5 percent, driven by high food prices and the depreciation of the dalasi against the U.S. dollar. Net international reserves have fallen to a precariously low level of only US$22.3 million in February 2017, less than one month of imports cover. Even this low level is predicated on foreign exchange swap arrangements with two commercial banks totaling US$33.2 million.

12) High fiscal deficits in recent years, financed by issuing expensive domestic securities, have led to rising debt levels and interest payments. Net domestic borrowing reached 11.4 percent of GDP in 2016. The total public debt stock reached over 118 percent of GDP at the end of 2016, rising from 105.3 percent in 2015. The related high debt service on domestic debt absorbed almost half of government revenue in 2016, together with weak revenue collection due to the economic slowdown and import compression in the latter part of 2016, and unbudgeted bailouts of SOEs, severely exerting fiscal pressures. As we are now uncovering, the previous regime was systematically siphoning off or stealing funds from SOEs with more than $100 million (10.6 percent of 2016 GDP) diverted over the regime's last 2½ years alone. This greatly contributed to their financial difficulties and the need for fiscal
bailouts, as well as exchange rate pressures. Our findings so far indicate that this affected mainly the National Water and Electricity Company (NAWEC) and the Gambia Telecom and Cellular Companies (GAMTEL/GAMCEL).

13) Monetary policy was largely ineffective in the face of fiscal dominance. While the CBG kept its policy rate unchanged at 23 percent as of December 2016, it was unable to absorb the large excess liquidity in the banking system. With the slowdown of economic activity, T-bill rates have declined from their peak in mid-2016, with the 12-month rate falling from 22 percent to below 14 percent and the 3-month rate from 17.8 percent to just above 10 percent most recently. However, lending rates have remained high and banks’ risk aversion increased in light of the political developments, which, together with the massive government borrowing, has continued to crowd out private sector credit.

14) Growth for 2017 is expected to pick up marginally to 3 percent, but in the medium term we expect a return to normal growth trajectory around 5-6 percent. The recovery in 2017 is mainly predicated on the assumption of a normal agricultural season, following the poor 2016/17 harvest, and a gradual recovery in trade and re-exports. Tourism is also expected to recover, but unlikely to make up for the losses related to the political turmoil. Beyond 2017 we are optimistic that the economic outlook will be more favorable. With the return to the rule of law and policy predictability, lower interest rates and a resumption of private sector credit growth, we expect investment as well as foreign direct investment to rise strongly, in particular in the tourism sector and in commercial agriculture. Greatly improved relations with Senegal will support re-exports and trade with the sub-region and, more generally, increase regional integration. Greater and cheaper energy supply will support all economic activities, including the light-manufacturing sector.

**FISCAL MEASURES**

15) We see the return to sound macroeconomic management and stability as a key pre-condition for growth. Returning to fiscal sustainability will require strong fiscal action to bring expenditures in line with resource availability while securing donor assistance to drastically reduce domestic borrowing and interest cost. It is important to take measures now that deliver quick results, including to bolster donor support. In addition, it is equally important
to take measures that may take longer to yield results and lay the basis for sustained and inclusive growth. In this context, we see as critical to resolve the difficulties of SOEs to protect fiscal outcomes, resolve NAWEC’s external and domestic debt service arrears, and work toward resolution of cross arrears between government and the SOEs. We also see as critical that any new loan or guarantee to the benefit of SOEs or agencies be only on concessional terms and after a thorough assessment of the impact of new borrowing on debt sustainability.

16) Our development partners have given indications that substantial financial support will be forthcoming. Indications of external budget support received so far amounts to about $75 million for 2017, including ($56 million) from the World Bank, the EU ($27 million) and the AfDB ($7 million). We also intend to use the RCF proceeds of $15.6 million for budget support, and will update the Memorandum of Understanding between MOFEA and the CBG concerning the on lending and repayment accordingly.

17) We have revised our 2017 budget to take into account more realistic revenue forecast, and cut expenditures in non-priority areas while protecting budgets in health and education, with the support of the World Bank [DPF prior action #1] and in line with our discussions with the IMF. Our objective is to achieve an overall fiscal deficit of 2.5 percent of GDP, well below the level of 2016, at 9.8 percent. To compensate for revenue shortfalls in the wake of the crisis, we have identified several measures to channel revenue sources back to the budget, described below. Expenditures cuts have been made, particularly in the budget of the President’s Office, which is rather large, reflecting the previous regime’s priorities. Savings are also expected on interest payments, roughly offsetting the decline in revenue. Budget support will help to greatly reduce the remaining deficit, however, a financing gap of 0.3 percent of GDP will remain, which we intend to close through additional measures, particularly the elimination of ghost worker after cases identified through staff audits that we have launched for the civil service and the security forces.

18) We have made every effort to keep NDB low in recent months through careful prioritization of spending, and we plan to continue to do so. Along with the decline in T-bill rates this is expected to reduce domestic interest payments in 2017 by about 0.8 percent of GDP.
We will sell the presidential plane and two others that are defunct. This could yield about 0.5 percent of GDP, and sell land, including in prime tourist areas. This could yield about 0.5 percent of GDP and could trigger tourism related investment. We have incorporated these amounts in the revised budget.

We will also ensure that all fees and revenue sources previously diverted are now channeled to the budget, including from the international voice gateway, heavy metal and sand mining, and fees for the use of the container scanner in the port. We estimate that this could yield up to 1.2 percent of GDP in non-tax revenue in 2017 and have incorporated these amounts in the revised budget.

To eliminate ghost workers, we have launched staff audits of the civil service and, for the first time, including the security services, which have expanded strongly over recent years (DPF Prior Action #2). These could deliver substantial savings (expected above 0.3 percent of GDP) and would provide a sound basis for a more comprehensive civil service reform and security forces in the future that would also include subvented agencies. A decision on the appropriate size and structure of these services will be taken at a later stage and may necessitate programs to facilitate transition into other activities, preferably private employment. In the interim, we will consider stepping up our participation in peacekeeping missions of the UN and other international organizations to reduce cost of security services.

We are considering additional reform policies to reduce the bloated vehicle fleet, strengthen accountability, reducing fuel and maintenance cost and generating receipts from the sale of excess cars. This would generate estimated savings of 2 percent of GDP over the next three years.

Over the medium term we will also consider streamlining ministries and subvented agencies, downsizing and rationalizing of embassies, and streamlining of memberships in non-financial international organizations, which could yield up to 1 percent of GDP.

In the medium term we plan to recover assets stolen by the previous regime that are still held in The Gambia. We plan to vigorously pursue recovery of all stolen assets with support by the UN/World Bank StAR Initiative, but realize that recovering assets held outside of the
Gambia will be a much lengthier process. Recovered assets would preferably be used to retire domestic debt.

25) We have also launched the recruitment process for an auditor to carry out special audits of SOEs to uncover all fraud and embezzlement of funds in the past, stop leakages and strengthen SOE oversight going forward. With assistance from the World Bank (DPF Prior Action 3), these audits will cover five SOEs that have been most affected by the previous regime’s embezzlement (NAWEC, GNPC, GAMTEL/GAMCEL, GPA, SSHFC). Audits of the Central Bank of the Gambia (CBG) and of other SOEs will follow.

DEBT MANAGEMENT

26) We are cognizant of the elevated risks related to the high public debt, but are already taking measures to contain them. We have consolidated all outstanding CBG lending to the budget through various facilities into a 30-year bond at an interest rate of 5 percent with a view to not add further borrowing. We estimate that this will lead to budgetary savings in interest payments of about 0.7 percent of GDP in 2017. While we are cognizant that this will ultimately lead to the need to recapitalize the CBG at a later stage, this will provide some short-term relief to public finances. We are committed to additional measures to address the debt situation, including debt restructuring, and we have set up a Committee on Government Bond for that purpose and launched the preparation of a Debt Strategy. The first meeting took place on May 18, 2017. The committee will support the government in exploring options for further resolving the debt, including lengthening the maturity structure of domestic debt by issuing securities with longer maturities and retiring commensurate amounts of T-bills, paying down a fraction of domestic debt, and restructuring external debt. Lengthening maturities debt would help reduce rollover risk and could potentially lead to further interest savings. We have sought support technical assistance from the IMF in addressing the debt issue. We are also asking for World Bank technical assistance to help us identify options to resolve the debt with due attention to the stability of the financial sector. We have also decided to allocate at least US$ 15 million in 2017 to buy down a portion of our domestic debt held by commercial banks. We are strongly committed to this process, which will help alleviate the debt service burden further, and welcome the World Bank financial support which will help achieve this important goal.
27) Prudent debt management is needed to manage the risks associated with the large public debt while accommodating financing needed for development. We are committed to facilitate clearance of the NAWEC's and GAMTEL's remaining external debt service arrears shortly. We will set up a debt management advisory committee to improve coordination and information exchange between the relevant departments of MoFEA and the CBG, and relevant SOEs, on both domestic and external debt to better forecast debt service payments. The Government will continue to seek external grants and concessional loans to finance public investment with a minimum grant element of 35 percent. We will not incur any new external payments arrears and will not contract or guarantee any new non-concessional external debt or any external debt with original maturity of one year or less. Given The Gambia's elevated debt level and the importance of tight controls on new borrowing, the government has also agreed to consult with IMF staff before contracting or guaranteeing new concessional external loans, and guaranteeing any new domestic loans to SOEs.

ADDRESSING FISCAL RISKS FROM STATE-OWNED ENTERPRISES

28) We are in the process of ring-fencing contingent liabilities from SOEs, in particular NAWEC. These contingent liabilities represent an estimated 10.7 percent of GDP and are a critical source of fiscal risks. Negotiations with commercial banks on a restructuring of NAWEC's domestic debt, including its 5-year bond (January 2017), are advancing and we are confident that an agreement will be reached soon that will be commensurate with NAWEC's ability to repay its debt over the medium term.

29) To further contain contingent liabilities from SOEs, we have inventoried guarantees and letters of comfort issues to SOEs, and still ongoing. This has been done with the support of the World Bank. We have also issued a circular to the effect that government will not issue any more guarantees for borrowing by SOEs or other agencies unless all conditions under the 2014 Public Finance Act are met, and with due attention to the terms of the loans and the impact on external and public debt sustainability (DPF Prior Action #5). We have also decided to establish a database of SOEs-related contingent liabilities, and to publish the list of ongoing guarantees and letters of comfort on a quarterly basis on the website of the Ministry of Finance and Economic Affairs (MoFEA).
We are developing a comprehensive strategy to address the operational and financial difficulties of NAWEC and GAMTEL/GAMCEL. NAWEC and, to a lesser degree, GAMTEL/GAMCEL have been incurring financial losses, which has required repeated unbudgeted fiscal bailouts and/or debt restructuring to avoid defaults, thus contributing to the expansion of NDB. There exist substantial cross arrears between SOEs and government.

a. **NAWEC.** Over many years NAWEC suffered from presidential directives that set electricity tariffs well below cost recovery and imposed economically unviable projects in rural areas, while fuel supply cost was inflated from rent seeking by a monopoly supplier as part of a scheme to siphon off funds. No real investment occurred and generators became obsolete and expensive in operation and maintenance. Our strategy thus aims at gradually reducing operating cost through new sources of energy, particularly renewables, greater efficiency in the supply of fuel through competitive tender, and cost reductions in NAWEC's operations.

b. In the immediate term, we have liberalized the fuel supply to NAWEC with the help of the World Bank and mandated the use of international competitive bidding from NAWEC fuel purchases (*DPF Prior Action #6*). Fuel importation is now done through competitive tender, which so far has reduced the cost to NAWEC by 15 percent, thus reducing its operational losses and the need for budget resources. This is expected to generate $1.5 million in savings for NAWEC in 2017.

c. Furthermore, NAWEC's non-operating cost has been bloated by legacies of the past and arrears by its customers, including government, other SOEs and municipalities. To account for these cost factors, we have taken over arrears on the debt service on the rescheduled NAWEC bond which will provide the company some breathing room until it has regained a sound financial footing and can resume paying this debt service; and, as a next step, we plan to resolve the issue of cross arrears taking into account the results of the special audits.

d. **GAMTEL/GAMCEL** has been struggling with structural changes to the telecom market and competitors in the wireless segment. In addition, since 2013, a significant...
share of its revenue was siphoned off by presidential directive. With the support of the World Bank, we have shifted oversight over GAMTEL/GAMCEL from the President's Office to the Ministry of Information and Communication Infrastructure (MOICI) which is now in charge of the reform agenda for the two companies (DPF Prior Action #7). This will lay the groundwork for the medium-term program and reforms to boost the sector. With further assistance from the World Bank, we plan to conduct an asset valuation of government owned assets in the telecommunications sector and evaluate options for restructuring and possible divestiture, i.e., tendering for a strategic investor or management contract. In evaluating these options, we will take into account the revenue each would bring to the government under both short- and long-term scenarios.

31) Other SOEs are financially more stable albeit may not have contributed to the budget through dividend payments, including possibly due to embezzlement of funds during the previous regime (e.g., the Gambia port authority (GPA)). Having ended all embezzlement in SOEs will improve their situation, and we are confident that implementation of the reform program agreed with the World Bank will put them on a sound footing.

32) We are committed to increase transparency on the financial situation of SOEs through the audits and the publication of most recent financial statements on the website of the MoFEA (DPF Prior Actions #3 and #4). The expected result is more transparency with financial information of key SOEs available to the public, including the extent to which resources have been diverted or misused. We also plan to step up MOFEAs oversight and monitoring of SOEs' operations, financial position and contingent liabilities and fiscal risks emanating from them.

SOCIAL SERVICE DELIVERY

33) Also of urgent importance is the acute shortage of medical supplies, vaccines and related medical equipment for improved health of the population. Public health facilities are already grappling with inadequate drugs and equipment. In 2017, there is a shortfall of GMD20,000,000 on drugs, dressings and medical supplies, which has the potential to affect service delivery. This is a looming crisis that requires immediate intervention.
34) To respond to this and increase the value for money in the health sector while avoiding shortages of drugs, and with the support of the World Bank, we have shifted our purchasing model for all medical supplies from single-source procurement to international competitive bidding (ICB). This is consistent with our new National Medicines Policy. To complement this shift, the MOSHW has also issued a list of essential medicines and quantities to be procured. In addition, to avoid disruptions in the supply of drugs to health facilities, the MoHSW has also issued a list of local suppliers accredited by the Gambia Medical Board, from whom health facilities can procure emergency drugs directly in the event of shortages (DPF Prior Action #8). This is expected to represent a very small amount of resources, but will help in the event of emergencies. We expect that the proportion of health facilities reporting no stock-outs of tracer items from 37% to 60% between 2016 and 2017.

INSTITUTIONAL FRAMEWORK FOR IMPLEMENTATION OF THE PROGRAM

35) Successful implementation of our Response Plan hinges on national and international commitments to fund and operationalize the priorities identified. The government recognizes that the Response Plan needs strong political will and donor support to deliver results on its immediate reform agenda. This calls for a central coordination mechanism under the stewardship of the Ministry of Finance and Economic Affairs.

36) A strong institutional arrangement will enhance national ownership and leadership that would assure The Gambia's development partners of our political commitment for effective coordination and more efficient use of resources. The Directorates of Aid Coordination, Budget and Development Planning under the Ministry of Finance and Economic Affairs will play a central role in the implementation and management of this Response Plan.

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