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INTERNATIONAL DEVELOPMENT ASSOCIATION

PROGRAM DOCUMENT FOR A PROPOSED

DEVELOPMENT POLICY GRANT

IN THE AMOUNT OF SDR 20.6 MILLION

(US$30 MILLION EQUIVALENT)

INCLUDING SDR 6.9 MILLION

(US$10 MILLION EQUIVALENT)

IN CRISIS RESPONSE WINDOW RESOURCES

TO THE

REPUBLIC OF SIERRA LEONE

FOR THE

EMERGENCY ECONOMIC AND FISCAL SUPPORT OPERATION

December 10, 2014

Macroeconomics and Fiscal Management
Africa Region

REPUBLIC OF SIERRA LEONE—GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of November 20, 2014)

Currency Unit	= Leone
US$1.00	= Le 4,881

ABBREVIATION AND ACRONYMS

AfDB	African Development Bank
BSL	Bank of Sierra Leone
CRW	Crisis Response Window
DFID	Department for International Development (United Kingdom)
DPO	Development Policy Operation
ECF	Extended Credit Facility
EEFSO	Emergency Economic and Fiscal Support Operation
FDI	Foreign Direct Investment
GBAA	Government Budgeting and Accountability Act
GDP	Gross Domestic Product
IDA	International Development Association
IFC	International Finance Corporation
IMF	International Monetary Fund
JAS	Joint Assistance Strategy
MDAs	Ministries, Departments and Agencies
MDBS	Multi-Donor Budget Support
MOFED	Ministry of Finance and Economic Development
NRA	National Revenue Authority
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
RCB	Rokel Commercial Bank (Sierra Leone) Limited
SDR	Special Drawing Rights
SLCB	Sierra Leone Commercial Bank Limited

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REPUBLIC OF SIERRA LEONE
EMERGENCY ECONOMIC AND FISCAL SUPPORT OPERATION

TABLE OF CONTENTS

ANNEXES

TABLES

The Emergency Economic and Fiscal Support Operation for Sierra Leone was prepared by an IDA team comprising Cyrus Talati, Gregory Smith, Daniel Weise, Ismaila Ceesay, Yusuf Foday, Errol Graham, Shunsuke Mabuchi, Patrick Umah Tete, Sydney Godwin, Nani Makonnen, Dora Harris, Christine Makori, and Maiada Kassem, under the overall guidance of Francis Ato Brown, Country Manager.

GRANT AND PROGRAM SUMMARY

REPUBLIC OF SIERRA LEONE

EMERGENCY ECONOMIC AND FISCAL SUPPORT OPERATION

Borrower	Republic of Sierra Leone.
Implementing Agency	Ministry of Finance and Economic Development (MOFED).
Financing Data	IDA Grant. SDR 20.6 million (US$30 million equivalent) including SDR 6.9 million (US$10 million equivalent) from the IDA Crisis Response Window.
Operation Type	Standalone development policy operation; Single tranche.
Pillars of the Operation and Program Development Objective(s)	Program development objective is to ensure that the Government's Ebola Response Plan can be executed through adequate budgeting and transparent use of resources, consistent with strengthening longer-term fiscal management and transparency. **Pillar 1:** Strengthen budget management and reduce fiscal risks heightened by Ebola. **Pillar 2:** Improve transparency and accountability for public resources.
Result Indicators	1. Clinical and non-clinical workers paid through the formal hazard payment system, disaggregated by gender (%). 2. Audits of hazard payments by the Internal Audit Department of MOFED (number). 3. Aggregate report from banks including opening and closing balances and summary of receipts and payments (monthly). 4. Estimate of fiscal contingent liability (yes/no). 5. Supplementary Budget for 2014 sanctioned by Legislature (yes/no). 6. Budget execution rate (% of appropriation; 75.4% in September). 7. Mineral Lease Agreements published on the internet or otherwise (% of total Lease Agreements on record). 8. Coverage of 2013 revenues from extractive industries publicly reported (%).
Overall Risk Rating	Substantial
Operation ID	P146726

PROGRAM DOCUMENT FOR A

PROPOSED EMERGENCY ECONOMIC AND FISCAL SUPPORT OPERATION

TO THE REPUBLIC OF SIERRA LEONE

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1. INTRODUCTION AND COUNTRY CONTEXT

1.1 This program document seeks the approval of the Executive Directors for a proposed stand-alone Emergency Economic and Fiscal Support Operation (EEFSO) in the amount of SDR 20.6 million (US$30 million equivalent) including SDR 6.9 million from the IDA Crisis Response Window (CRW),[1] to the Republic of Sierra Leone. The proposed operation will support government efforts to respond to the unprecedented challenges posed by an Ebola Virus Disease epidemic, through its *Revised National Ebola Response Plan* which aims to address and reverse the Ebola crisis rapidly, thereby cushioning the impact of the same on its development plan, *An Agenda for Prosperity*. The latter is the third Poverty Reduction Strategy Paper (PRSP-3) covering the period 2013-18. The main aim of the PRSP-3 is to promote inclusive growth, economic diversification and value-addition.

1.2 The proposed operation was originally designed to be the first in a series of three development policy operations, but this has given way to the urgency of supporting efforts to halt the spreading epidemic. Recent uneven progress on structural reforms has reinforced the need to maintain a focus on the medium term hence the proposed operation also contains elements considered necessary for ensuring post-Ebola recovery. Notably some of the prior actions previously agreed have been retained as they remain essential for Sierra Leone's economic recovery and future prospects, once the epidemic has been brought under control and ended. The two pillars of the proposed operation—(i) Strengthen budget management and reduce fiscal risks heightened by Ebola; and (ii) Improve transparency and accountability for public resources—both respond to the dual needs of the Ebola crisis and the medium term. In recognition of the health emergency resulting from Ebola the financing under the proposed operation has also been doubled.

1.3 As with the previously approved CRW-funded Ebola response projects, this program document also seeks the approval of Executive Directors to provide the financing of the project from the CRW in the amount of US$10 million equivalent entirely on grant terms rather than on Sierra Leone's standard IDA terms as is prescribed for financing from the CRW.[2] The use of

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[1] A note presented to the Board on October 28, 2014, entitled "Ebola: Update on World Bank Group Response and Request for Additional Crisis Response Window (CRW) Resources", informed the Board of Management's intention to allocate an additional financing of $270 million from IDA's CRW bringing the total CRW allocation to support the Ebola response to $420 million.

[2] Under the CRW's implementation framework for IDA17, the terms of assistance for CRW financing are identical to those under which regular IDA assistance is provided to a particular country. For FY15, Sierra Leone will receive 50 percent of its regular IDA financing on credit terms and the balance of 50 percent on grant terms.

grant financing is appropriate in light of the demonstrable regional and global positive externalities that will flow from mitigating the spread of the deadly virus in the affected countries and reducing the risk of it spreading to at-risk neighboring countries, as well as the rest of the world. The operation will thereby be benefitting the Sierra Leonean and the global community, by minimizing the economic impact of the outbreak and protecting lives and livelihoods of the populations at large.

Country context

1.4 **Broad-based economic performance since the end of the civil war in 2002, averaging nearly 6 percent GDP growth annually and 4 percent in per capita terms until 2010, has underpinned the reconstruction effort and subsequent social progress in Sierra Leone**. Since 2010 large inflows of Foreign Direct Investment (FDI) and the onset of iron ore production and exports in 2011, have lifted GDP growth rates to average 17.6 percent annually during the period 2010-2013. These positive developments could not mask the enormous challenges that continued to face the country: a legacy of inadequate basic services that pre-dated the civil war, a significant infrastructure deficit which confounds development prospects, and weak public sector capacity, all amidst a weak governance environment. Despite the challenges the peace has been maintained and three successful national elections have been held reflecting a degree of political maturity.

1.5 **Natural resource development and management play an important role in the *Agenda for Prosperity* which envisions harnessing such resources for achieving middle-income country status by 2035.** The emphasis on a development strategy linked to natural resources stems from the recent commencement of large scale iron ore mining and an offshore oil exploration boom. The latter has generated some windfall licensing revenues and the former has raised expectations regarding future revenue inflows which may in the event appear optimistic.

1.6 **The advent of the Ebola virus in May 2014 and the subsequent acceleration of the outbreak in late July has put immeasurable strain on government and society more broadly, and is putting the solid achievements of the last twelve years at risk**. Under these circumstances another notable achievement of the same period—the transition out of *fragile state* status could also be threatened.[3] Successfully confronting the spread of the Ebola virus is therefore critical given the potential implications for the state.

1.7 **The recent positive economic prospects led to increased spending pressures manifested through fiscal slippage in 2011-12, and a strong consolidation effort in 2013 which saw some reversal in early 2014**. Fiscal developments in the first half of 2014—prior to the emergence of Ebola—reflected some reversion due to revenue underperformance combined with heightened spending. Early government actions to address the revenue administration challenges had to give way to confronting the more pressing needs of the Ebola epidemic.

[3] Under the World Bank definition of *Fragile Situations*, a country needs to meet one of two criteria to be classified as such: the first relates to a harmonized score on the Country Policy and Institutional Assessment ratings below a threshold, which Sierra Leone has risen above; and the second requires the presence of a peacekeeping mission presently or within the past three years. The last UN mission departed Sierra Leone less than three years ago.

Nonetheless the fiscal management challenges remain significant and addressing these successfully will remain critical steps in Sierra Leone's recovery from the current crisis.

1.8 **The 2014 outbreak and escalation of the Ebola epidemic has led to an unprecedented toll in human lives in Sierra Leone, as well as Liberia and Guinea.** The outbreak[4] originated in rural Guinea in late 2013, and spread into neighboring Sierra Leone and Liberia in the second quarter of 2014 where it has accelerated into an epidemic. As of December 8, 2014, there had been 1,742 recorded deaths in Sierra Leone out of 7,798 suspected, probable and confirmed cases of Ebola.[5] Experts believe that the true numbers may be two to four times larger, due to underreporting.[6] The figures mask an important fact—namely that the fatality rate in this epidemic is 71 percent. The social cost has been high and deprivation intense, as Ebola has now spread to all of the country's 13 districts, including the capital.

1.9 **The fear and sense of panic that it has generated is resulting in the more routinely sick being denied medical care as the health system has broken down**. The disease has also exacted a high price on the country's health system, with more than one hundred health workers among the dead including ten doctors but the true toll on the health system and the population is considerably higher. Fear of contracting the disease has led most private hospitals to shut down, as have four public hospitals. Consequently simpler more treatable illnesses such as malaria or pregnancy related complications could now spell a death sentence for those afflicted.

1.10 **The Bank responded in early-August by reallocating US$6 million to Sierra Leone in available funds under the existing Reproductive and Child Health Project 2, so as to make resources available immediately: Thereafter the Executive Board approved an Ebola Emergency Response Project in an amount equivalent to US$105 million in mid-September covering the three countries.** Sierra Leone received US$28 million under the project which was for control and stabilization of the epidemic. These resources have been disbursed fully to the government and UN agencies implementing the response, and rapidly utilized for medical supplies and equipment, food and logistics, social mobilization and contact tracing activities, payment to international health workers, and hazard pay and other benefits for health workers. Subsequently the Board approved additional financing in the amount of US$285 million (US$98 million for Sierra Leone) with the resources to be focused on supporting scale-up of community based care and community-led activities for faster detection, isolation and treatment and safe burials, and accelerated deployment of foreign medical teams among other things.

1.11 **The emerging economic impact has already resulted in significant downward revisions to projected GDP growth to 4 percent for 2014 from an 11 percent initial projection, with the risks being to the downside.** Fiscal constraints from both the revenue and expenditure side have placed considerable pressure on public finances. Sporadic shortages of essential goods and food which have resulted from measures implemented to control the spread of the disease—such as closure of certain markets—have also led to some price spikes.

1.12 **Economic management challenges had emerged prior to the Ebola outbreak, reflected in fiscal slippage, slow progress on structural reforms and policy reversals.** Thus

[4] Hereafter the term Ebola is used to refer to the virus, the disease or the epidemic outbreak.
[5] World Health Organization, "Ebola Response Roadmap: Situation Report," December 8, 2014.
[6] World Health Organization, "Ebola Response Roadmap," August 28, 2014.

while the immediate and urgent priority is to respond to the Ebola threat and contain the spread of the disease, of near-equal importance is the need to support the government and maintain the dialogue on structural issues through this difficult period. The post-Ebola economic recovery and restoration of medium term growth will be critically dependent on establishing and implementing a coherent and realistic economic reform and recovery program centered on structural reforms and the Bank is engaging the authorities in this.

Poverty Developments

1.13 **The national poverty rate declined to 53 percent in 2011, from 66 percent in 2003 on the back of robust economic growth, matched by an improvement in the $1.25/day international measure which declined from 59 percent to 57 percent over the period.** With more than half of all households involved in agriculture as their main occupation, rural areas provided the impetus to this improvement with headcount poverty declining from 79 percent in 2003 to 66 percent in 2011. Improvements in urban poverty were led by urban centers outside the capital, Freetown which saw urban poverty decline from 47 percent in 2003 to 31 percent in 2011. Inequality improved over the period as poorer districts experienced relatively higher growth rates. Reflecting this national inequality has decreased with the Gini coefficient declining to 0.32 in 2011, from 0.36 in 2003. As a result of these trends income poverty in Sierra Leone shows little spatial variation. Notably, however, despite the good overall progress the number of poor has remained steady probably due to high population growth.

1.14 **Sharp reversals can be expected in the progress on poverty reduction given the scale and reach of the Ebola epidemic which has accelerated significant in November 2014.** The two districts where it emerged and which were the most severely affected accounted for 24 percent of the poor. They are also districts considered to be the agricultural bread basket of Sierra Leone. Most agricultural households cultivate rice, the main food crop. Hence the potential disruption to food supplies in particular and agriculture more generally could be profound, particularly as these districts have been subjected to quarantine, established to control the spread of the Ebola virus.

1.15 **Public service delivery is weak overall and more so for rural inhabitants with health indicators ranking the country's health care system a bottom performer on a global scale**.[7] The civil war interrupted education for many, leading to some of the highest percentages of the working age population with no education in sub-Saharan Africa—56 percent of adults over the age of 15 years, reported that they had never attended school. There has been a strong catch-up among younger cohorts, however, which is closing the gap. Electricity access rates are low by international standards, around 10 percent nationally with only 0.1 percent of rural dwellers reporting electricity as their main source of lighting. Thus progress has not been as good on the dimension of poverty concerned with access to essential services.

[7] In 2013, Maternal mortality (modeled) was 1,100 per 100,000 births; and Under-5 mortality was 160.6 per 1,000. World Development Indicators accessed on October 30, 2014, http://databank.worldbank.org/Data/Views/reports/tableview.aspx

2. MACROECONOMIC POLICY FRAMEWORK

A. RECENT ECONOMIC DEVELOPMENTS

2.1 **Although the economic effects of the Ebola epidemic are still unfolding it is evident that a sharp slowdown in economic activity is underway in 2014 that has already seen recent annual GDP growth projections made in June, revised from 11.3 percent to 4.0 percent (Table 2.1).** Following a real GDP increase of 20.1 percent in 2013—fuelled mainly by increased output from the two large iron ore mines and solid growth in the agriculture, construction and services sectors—GDP growth in the first half of 2014 was broadly in line with projections. As in 2013 the main driver of expected double digit growth in 2014 was expanding iron ore production although at a slower pace as the two mines approached designed capacity. The effects of the Ebola outbreak are all falling on the second half of 2014, when it is estimated that real GDP contracted at an annual rate of 2.8 percent.

Table 2.1: Sierra Leone: Selected Economic Indicators, 2009-17

	2009	2010	2011	2012	2013	2014	2015	2016	2017
						------------------Projected-----------------			
	--------------------Annual Percentage Change, unless otherwise indicated-------------------								
National accounts and prices									
GDP at constant prices	3.2	5.3	6.0	15.2	20.1	4.0	-2.0	1.5	2.5
GDP deflator	8.6	17.9	17.4	12.0	8.0	3.9	8.5	9.5	6.8
GDP at market prices (billion leone)	8,183	10,161	12,755	16,453	21,356	23,066	24,529	27,262	29,862
Consumer prices (end-period)	10.8	18.4	16.9	12.0	8.5	10.0	14.0	9.5	7.5
Consumer prices (average)	9.2	17.8	18.5	13.8	9.8	8.7	12.6	11.5	7.5
External Sector									
Terms of Trade	-2.6	6.8	0.3	4.9	-4.1	-12.6	-3.8	0.5	0.2
Exports of goods (US$)	-1.0	33.8	6.2	202.0	66.0	4.3	7.0	16.4	7.1
Imports of goods (US$)	-2.6	60.7	85.2	20.2	-19.9	7.6	2.7	1.7	3.8
Average exchange rate (Le/US$)	3,410	3,988	4,349	4,344	4,357	..	..	..	..
Nominal effective exchange rate (- depreciation)	-26.7	-8.9	-4.1	1.0	-1.1	..	..	..	..
Real effective exchange rate (- depreciation)	-0.7	2.2	8.7	14.7	3.6	..	..	..	..
Gross International reserves (mths of imports)	4.1	2.0	1.8	2.2	2.3	2.5	2.4	2.5	2.4
Money and Credit									
Domestic credit to the private sector	45.4	31.5	21.8	-6.9	11.7	4.8	-3.5	5.6	9.9
Base money	19.7	34.6	13.0	18.5	17.6	9.5	10.9	11.3	8.9
M2	28.3	21.8	20.0	23.1	21.0	10.2	10.9	11.3	10.8
91 day treasury bill yield (percent)	14.0	24.5	23.4	22.4	8.0	..	..	..	..
	--------------------------------------Percent of non-iron ore GDP--------------------------------------								
National Accounts									
Gross capital formation	9.3	24.3	42.2	28.6	24.6	18.3	16.5	17.9	19.3
Government	5.5	7.7	9.0	8.2	6.4	8.3	7.5	7.8	8.3
Private	3.8	16.5	33.1	20.3	18.2	10.0	9.0	10.0	11.0
National savings	2.8	5.0	-17.0	-4.1	12.2	4.1	1.3	8.6	10.1
External Sector									
Current account balance (incl official grants)	-6.5	-19.3	-45.0	-30.9	-12.4	-14.2	-15.2	-9.3	-9.2
Current account balance (excl official grants)	-9.9	-24.5	-48.8	-33.6	-13.6	-17.1	-18.2	-10.5	-10.4
External public debt (incl IMF)	28.9	30.7	32.6	27.8	25.2	28.0	28.9	30.5	31.7
Central Government Budget									
Revenue	9.0	9.9	11.5	12.2	12.7	11.4	10.7	12.0	12.7
Grants	6.1	5.3	5.6	4.1	3.0	5.0	3.9	3.3	3.2
Total expenditure and net lending	17.7	20.4	21.6	21.9	17.6	22.4	20.2	20.5	21.2
Overall balance (before grants)	-8.6	-10.5	-10.1	-9.7	-4.9	-11.0	-9.5	-8.5	-8.5
Overall balance (incl grants)	-2.5	-5.1	-4.6	-5.6	-1.9	-5.9	-5.6	-5.2	-5.3
Memorandum Items:									
GDP (US$million)	*2,400*	*2,548*	*2,933*	*3,788*	*4,915*	*5,200*	*5,346*	*5,761*	*6,128*
Non-iron ore GDP (US$ million)	*2,400*	*2,548*	*2,926*	*3,528*	*4,140*	*4,434*	*4,855*	*5,232*	*5,599*

Source: IMF and Bank staff estimates.

2.2 **Key sectors underpinning non-iron ore growth, notably agriculture, construction, services, transport and tourism have been adversely affected as a result of the Ebola epidemic**. Real non-iron ore GDP is now expected to be flat in 2014, down from the budget projection of 6.0 percent. Agriculture has been disrupted due to quarantines in effect over 5 of the country's 13 districts, which cumulatively account for as much as 40 percent of agricultural output, although the extent of lost production remain unknown. In some cases, the transport restrictions—designed to curtail the spread of the disease—have prevented produce from reaching markets, while in others production has been affected due to the direct effects of the disease. A sharp drop off in visitor arrivals has also occurred—across all categories including business and tourism—which in turn has had significant knock-on effects throughout the economy especially in the services sector.

2.3 **The economic consequences of Ebola were initially disproportionate to the direct human loss because of the considerable fear and panic it generated and the subsequent aversion behavior exhibited by both domestic and external economic agents.** In time, habituation on the part of domestic economic agents leads to a degree of normalcy, but at much lower levels of economic activity. The generally low literacy levels prevailing in the country have posed a formidable challenge particularly with regard to a strong communications effort, so essential to curbing the spreading epidemic. The sharp intensification of Ebola transmission since mid-November 2014, now suggests that the direct economic consequences of the disease are sure to be far higher than initially considered.

2.4 **Leading indicators of the slowdown in economic activity and aversion by the external community all show sharp reductions by September 2014**. The effect of the severe disruption to economic activity in 2014 will be less than might be expected due to the broad based and robust growth achieved over the first 6 months of the year, which is not expected to be unwound despite the sharp slowdown now evident in many indicators. On the economic front, a sharper decline may be expected in 2015.

2.5 **Expectations that strong mining sector growth in 2014 would shield the economy from the worst of the Ebola related slowdown were dashed when one of the two iron ore miners, London Mining Plc, operator of the Marampa mine became insolvent, in mid-October 2014 and the other miner, African Minerals Ltd. (AML) halted production in early December for much the same reasons.** Although the proximate cause of their demise was the large decline in global iron ore prices to 5-year lows in September, the overlay of the Ebola undoubtedly clouded prospects for London Mining to restructure its finances and transition out of its difficulties. Although the two operations accounted for nearly one-fifth of GDP, the direct economic effects are expected to be relatively small in 2014, given the timing of this event late in the year. The Marampa mine was subsequently acquired by the Executive Chairman of AML, operator of the larger iron ore mine at Tonkolili.

2.6 **The economic effects in 2015 and beyond could be ruinous if both mines cease operating for a prolonged period, and the social consequences would be devastating due to the loss of wage employment which would affect a combined workforce of some 3,000**. Local suppliers and other businesses would also be adversely affected as both operators would be unable to discharge their liabilities. Hence the ripple effects of such an event on local businesses would be severe. Sharply lower international commodity prices in 2014 have also curtailed royalty income to Government.

2.7 **Consumer inflation continued to trend lower over the first half of 2014 after declining from 9.8 percent over the year to December 2013 to around 6.5 percent at mid-year.** This reflected lower world food prices, increased agricultural production and currency and fuel price stability. Disruptions to supply chains and lower domestic production as a result of the Ebola virus appears to have been the cause of a lift in inflation rates to around 7.5 percent in September 2014. Current projections are for inflation to continue rising to near 10 percent at year-end. The terms of trade for 2013 deteriorated further than earlier projected from -1.6 percent to -4.1 percent because of lower mineral prices, and is now projected to decline significantly further over 2014-15, by -12.6 percent, and -3.8 percent.

2.8 **With iron ore production up strongly in 2013 the trade balance recorded a surplus of US$0.5 billion**, up from a deficit of just under US$800 million in 2012. The current account deficit declined by much less to -12 percent of non-iron ore GDP, however, reflecting a dramatic increase in the income deficit on account of mineral company debt service. Prior to the outbreak of Ebola the trade balance was expected to continue to improve. Now with expected adverse impacts on exports and higher Ebola related imports (of food, medical supplies and equipment), the trade surplus is expected to remain around 2013 levels and the current account deficit to deteriorate modestly further. Following completion of the investment phase of the two iron ore mines in 2012, FDI inflows slowed to US$369 million in 2013 from US$707 million in 2012.

2.9 **Fiscal performance improved in 2013 after lackluster performance over 2010-12.** In 2012 the budget deficit (on a cash basis) reached Le 943 billion (5.6 percent of non-iron ore GDP), nearly double the budgeted deficit of Le 507 billion, reflecting a deterioration in non-mineral revenues and increases in expenditure over most categories (Table 2.2). With the need to finance the large, unbudgeted, fiscal overhang being the dominant concern in early-2013 and with prescribed limits on central bank financing being invoked, the application of approved 2013 budget envelopes was abandoned and following the reelection of the government, it moved decisively to restore budget control and accountability. The Government's newly formed cash management committee met weekly and expenditures were approved only for essential categories, whilst additional revenue was mobilized.

2.10 **Over the first half of 2014 execution of an ambitious and expansionary budget showed signs of deterioration prior to the emergence of Ebola**. Downside risks appear to have emerged from the fragile fiscal position due to Sierra Leone's low tax base and underlying expenditure pressures from high salaries, infrastructure investment and expenditures contained in 2013 that led to fiscal slippages.[8] Revenue underperformance was significant as collections by the National Revenue Authority (NRA) fell sharply across most categories, particularly for import duties, import GST and extractive sector revenues. Overall, over the first six months of 2014, domestic revenues were around Le 79 billion (about US$18 million) below revised programmed levels, while expenditures were Le 79 billion above the same.

[8] Extended Credit Facility, First Review, June 2014, IMF.

2.11 **Financing the higher than programmed first half deficit appears to have been particularly challenging** and resulted in payment delays (accumulation of significant withheld cheques) for most categories of recurrent expenditure and tighter expenditure controls late in the half year. At end-June 2014 the float stood at Le 316 billion compared with a programmed level of minus 11 billion. Financing constraints were also apparent with the Ways and Means Advance Facility from the central bank being close to its fully drawn statutory limit and the issuance of treasury bills to the market rising towards IMF domestic financing program limits by mid-year.

Table 2.2: Sierra Leone: Central Government Budget, 2009-17

	2009	2010	2011	2012	2013	2014	2015	2016	2017
							Projected		
	Percent of non-iron ore GDP								
Total revenue and grants	15.2	15.3	17.1	16.4	15.7	16.5	14.6	15.3	15.9
Revenue	9.0	9.9	11.5	12.2	12.7	11.4	10.7	12.0	12.7
Tax	6.8	9.3	10.9	11.5	11.7	10.7	9.9	11.1	11.8
Non-tax	2.2	0.6	0.6	0.7	0.9	0.7	0.8	1.0	0.9
Grants	6.1	5.3	5.6	4.1	3.0	5.0	3.9	3.3	3.2
Total Expenditure and Net Lending	17.7	20.4	21.6	21.9	17.6	22.4	20.2	20.5	21.2
Current expenditures	12.2	12.7	12.6	13.7	12.1	13.6	12.8	12.9	12.9
Wages and salaries	4.9	5.3	5.4	6.1	5.9	7.0	7.1	7.2	7.2
Goods and services	4.3	4.2	3.1	3.0	2.9	3.9	3.1	2.8	2.9
Subsidies and transfers	1.8	1.6	2.2	2.7	1.7	1.6	1.6	1.5	1.5
Interest payments	1.3	1.6	2.0	1.9	1.7	1.2	1.0	1.5	1.5
Capital expenditures	5.5	7.7	9.0	8.2	6.4	8.1	7.5	7.8	8.3
Foreign financed	4.2	4.3	6.2	5.2	4.1	5.4	5.6	6.0	6.2
Domestic financed	1.3	3.5	2.8	3.0	2.3	2.7	1.9	1.9	2.1
Net lending	0.0	0.0	0.0	0.0	-0.9	0.1	-0.2	-0.2	0.0
Contingency Expenditure (Ebola related)	0.0	0.0	0.0	0.0	0.0	0.6	0.2	0.0	0.0
Overall balance									
Before grants	-8.6	-10.5	-10.1	-9.7	-4.9	-11.0	-9.5	-8.5	-8.5
After grants	-2.5	-5.1	-4.6	-5.6	-1.9	-5.9	-5.6	-5.2	-5.3
Financing	2.5	5.1	4.6	5.6	1.9	5.9	6.1	5.2	5.3
External financing (net)	1.9	1.6	2.4	3.4	1.6	3.9	3.1	3.4	3.6
Domestic financing (net)	0.6	3.5	2.2	2.2	0.3	2.0	1.7	1.8	1.7
Bank	1.3	4.1	0.5	1.4	1.7	2.8	1.5	0.9	0.7
Non-bank	-0.8	-0.6	1.6	0.8	-1.4	-0.8	0.2	0.9	1.1
of which: change in arrears			-0.4	-0.5	0.1	-0.2	-0.1	0.0	0.0
of which: float (cheques payable)	-0.6	-0.8	1.3	0.4	-1.2	-0.1	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	1.2	0.0	0.0

Source: IMF and Bank staff estimates.

2.12 **In the face of the economic developments noted above, government revenues appear to be crumpling due to the reduced economic activity and a reduction in tax compliance**, adding to an underperformance related shortfall in the first half of the year. The revenue loss attributed to Ebola and non-Ebola related effects is projected to be about US$85 million equivalent for 2014 (Table 2.3). On the expenditure side the government initially allocated US$37 million equivalent for additional unplanned expenditure related directly to the Ebola response covering both the health and social aspects; this amount has since been increased to US$41 million. Combined with the revenue declines noted above, a total impact of around US$140 million was estimated, (US$153 million with inclusion of capital expenditure adjustments). Actual spending needs are changing frequently since these estimates were made and the costs to the budget may be higher.

2.13 **Development partners have stepped up to the financial challenges confronting the government in financing the 2014 budget as a result of Ebola, by increasing their planned financial support with an additional US$137 million, which should provide the Government the necessary flexibility to fund most of the additional financing needs.** In September the IMF augmented its existing program with Sierra Leone under the Extended Credit Facility **(**ECF) and provided the equivalent of US$39.8 million. The Multi-Donor Budget Support (MDBS) partners comprising the European Union, the United Kingdom Department for International Development (DFID), the African Development Bank (AfDB), and IDA have collectively increased their previously programmed support for 2014 by more than two and a half fold, for a total of about US$100 million. As noted below, this, together with some measures by Government should be adequate to largely cover budget financing needs in 2014.

Table 2.3: Sierra Leone: Fiscal Effects of Ebola, 2014

	-----Leones billions------		------------------US$ millions------------------		
	Pre-Ebola	Revised Est.	Pre-Ebola	Revised Est.	Difference
Tax and Non-Tax Revenue	2,613	2,247	603.0	518.6	-84.5
Current Expenditure	2,556	2,797	589.9	645.5	55.6
of which: Health response	0	165	0.0	38.0	38.0
Social response	0	13	0.0	3.0	3.0
Capital expenditure	1,665	1,610	384.3	371.6	-12.7
Total Expenditure	4,221	4,407	974.2	1,017.1	42.9
Overall balance before grants	-1,608	-2,160	-371.1	-498.5	-127.4
Grants	740	949	170.8	219.0	48.2
Overall balance after grants	-868	-1,211	-200.3	-279.5	-79.2
(percent of non-iron ore GDP)	*-4.2%*	*-5.9%*	*-4.2%*	*-5.9%*	*-1.8%*

Source: Ministry of Finance and Economic Development and Bank staff estimates.

2.14 **Most of the international assistance being mobilized in the face of the growing Ebola epidemic is outside the national budget.** The Government's efforts are being spear-headed by the National Emergency Response Center of the Ministry of Health and Sanitation with the support of international partners including WHO, UNICEF, WFP and many others. Much of IDA's support under the Ebola Emergency Response Project is going directly to finance the immediate health and social response by international partners, while some has been used to procure goods for them such as medical supplies and food for quarantined households. A portion also goes to the national budget, for example in the case of hazard payments for workers directly involved in the Ebola response. Most of the international assistance received, whether in kind or in cash, is coordinated with the National Emergency Response Center.

2.15 **While the response to the Ebola epidemic has rightly taken precedence over the economic reform agenda, the continuation of what appears to be a structural decline in**

non-mineral revenue collections compounded by the unexpected lower contribution from the extractive sector remains a serious challenge that is likely to grow in magnitude due to increased taxpayer non-compliance resulting from Ebola. With significant financing constraints appearing in the system through the year, MOFED and the central bank have yet again been preoccupied over the first half of 2014 with the challenging and time-consuming task of reprioritizing commitments and payments on a frequent basis. This preoccupation has distracted the Government from planned improvements in public financial management, budget execution and planning, and public investment management processes and raises the prospects of a large fiscal overhang building up by year end.

2.16 **Monetary policy was accommodative over the first three quarters of 2013.** This resulted from: (a) high levels of seasonal liquidity in the system over the first half year; (b) government refraining from new net issuance of bills; and (c) the central bank having exhausted its supply of marketable securities that would have been required to sterilize the liquidity. The outcome was that yields on government bills declined dramatically (to a range of 3-10 percent by end-2013 from 19-26 percent one year prior). Treasury bill yields continued to decline over 2014 with short term yields tumbling to below 2 percent by mid-2014. System liquidity remained at high levels in 2014 reflecting a widening of the domestic fiscal deficit over the first half of 2014 and net foreign exchange inflows, neither of which could be sterilized by the central bank because of a lack of marketable securities and weak profitability and capital ratios. The Government tapped the market over the June-July 2014 period for around Le 156 billion resulting in bill yields increasing by 1-2 percent. The effective withdrawal of non-bank financial institutions, including the pension fund (National Social Security and Investment Trust), from the treasury bill market due to both negative real yields and declining liquidity has exacerbated the depressing impact on yields.

2.17 **Over the year to July 2014, M1 grew by 35 percent and broad money by 18 percent.** Domestic money bank holdings of government securities increased nearly 40 percent and private sector credit growth has been subdued with growth of only 6 percent over this period. Retail lending interest rates remain at elevated levels despite the decline in government security yields and inflation. The significant growth in the narrow money supply remains a major concern. At end-July 2014, banks held cash and liquid deposits at the central bank amounting to Le 411 billion, equivalent to 9 percent of commercial bank assets (compared to 6 percent 2 years earlier).

2.18 **Application of more rigorous prudential lending standards by the central bank in first-half 2014 has led to higher provisioning levels for bad and doubtful debts by commercial banks.** The two large state banks (accounting for 30 percent of private sector system lending) have had their private sector lending programs effectively halted because of serious prudential concerns regarding their loan books. Both now appear to have negative regulatory capital with bad debt provisions being increased from Le 44 billion at end-March 2014 to Le 155 billion at end-June 2014. Both state banks have had their management heads replaced over the past year. Whilst some loan recoveries were achieved over the first seven months of 2014, these are unlikely to be sufficient to restore bank capital ratios and profitability concerns will remain.

2.19 **With real yields on short term securities now decisively negative and with the commercial banks holding a large and increasing share of treasury bills, rollover risk for the Government has increased substantially**. With the duration of the domestic debt portfolio remaining quite short (around 9 months), the yield curve is likely to be quite steep, posing additional risks for any longer term issuance. Because the current yield curve is unlikely to be sustainable and with any significant movement upwards posing substantial fiscal risk, the Government intends to formulate a risk management framework that would accompany its debt management strategy. Furthermore, the transmission mechanism that should result in lower retail rates and higher private sector lending growth appears dysfunctional. This reflects the tighter prudential requirements on an existing small, poorly performing loan book of the banking sector, solvency issues at the larger state banks, a very high cost structure in maintaining branch networks (largely due to electricity generation and water supply costs) and the sharp decline in profitability in all banks. Ebola will only exacerbate these problems and with expected write offs on loans from the state banks, private sector credit growth is expected to remain subdued over 2014-15.

2.20 **After depreciating 27 percent relative to the U.S. dollar in 2009, 8 percent in 2010 and 4 percent in 2011, the market determined Leone remained relatively stable between 2012 and end-July 2014**. This reflects a flexible exchange rate policy, FDI inflows associated with the new iron ore projects, official inflows and more recently an improvement in the trade balance from the commencement of iron ore exports. Gross international reserves stood at US$420 million at end-2012 (3.1 months non-iron ore import cover) and US$473 million at-end 2013 (3.4 months non-iron ore import cover) and US$554 million at end-August 2014 (about 3.6 months). While the official leone exchange rate has been stable in first half 2014, it has begun to depreciate steadily since July. The parallel market rate has also widened recently, probably reflecting tighter central bank controls on repatriation of foreign currency and possibly tax and duty evasion, as well as outflows associated with uncertainty over the Ebola.

2.21 **Sierra Leone's nominal public and publicly guaranteed external debt, including IMF and principal arrears, was estimated at US$1.026 billion[9] at end-2013 equivalent to 25 percent of non-iron ore GDP, comparing favorably with 28 percent at end-2012**. About 66 percent of this debt is owed to multilateral creditors, 14 percent to bilateral creditors, and 19 percent to commercial creditors. The largest multilateral creditors are the IMF (US$137 million), World Bank Group (US$242 million), the AfDB (US$87 million) and the Islamic Development Bank (US$55 million). Debt to external commercial creditors consists of arrears accumulated before and during the civil war. A debt-buy-back operation is under preparation, with World Bank assistance, to extinguish all eligible commercial debt.

2.22 **Domestic debt[10] amounted to US$450 million (10.9 percent of non-iron ore GDP) at end-2013, about one-third of total debt on issue**. With the contraction of the fiscal deficit in 2013, public domestic debt increased modestly by US$46 million in 2013 but declined as a percentage of non-iron ore GDP from 11.5 percent at end-2012. Most of the debt is held by commercial banks (71 percent of marketable securities) and the non-bank public (22 percent of marketable securities). To lessen rollover risk, the authorities have achieved modest increases in

[9] All external loans contracted by state-owned enterprises are guaranteed by the government.
[10] Including central bank overdrafts but excluding accounts payable.

the duration of the domestic debt portfolio from 6 months at end-2010 to 8.3 months at end-2012 and 9.1 months at end-2013. Despite this rollover risk remains significant with a domestic portfolio duration of less than 1 year, particularly given the expansion of securities on issue at negative real interest rates and with an increasing concentration in the commercial banks including the ailing state banks. Domestic interest payments increased from 1.4 percent of non-iron ore GDP in 2010 to 1.7 percent in 2012, and with falling yields, declined to 1.5 percent in 2013. It is unlikely, however, for this declining trend to continue given the planned increase in domestic securities on issue and the un-sustainability of negative real yields over the medium term.

B. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

2.23 **Given the expected deceleration in the growth of iron ore production from 2014 and the lagged impact of the Ebola epidemic, real non-iron ore GDP growth is projected to decelerate over the 2014-15 period.** There is great uncertainty about the outlook as both iron ore mines are loss making under current international prices (which were at 5 year lows in early September 2014), with one under new ownership. Notably, the significant decline in the prices of iron ore and other minerals, if sustained or shows further deterioration, will adversely affect government mineral revenue projections, national income and the external accounts, at least over the near to medium term.

2.24 **The impact of Ebola on exports and health-related imports, has led to a sharp decline in the projection of a growing trade surplus reaching nearly US$750 million in 2015, now falling below US$150 million.** Consequently the current account deficit rises from around US$0.6 billion to US$0.7 billion, with the modest trade surplus more than offset by commensurate increases in the income and services deficits. Direct investment and project grants may now be insufficient to cover the current account deficit and a balance of payments deficit in excess of US$275 million (about 5.7 percent of non-iron ore GDP) is expected to develop in 2015. Import cover of 3.9 months of reserves is programed for 2015, and expected to be maintained over the medium term.

2.25 **The deepening of the Ebola epidemic has rightly altered Government priorities substantially with most of the medium term public financial management reforms being placed on hold.** Revenue projections for 2015 have been scaled back considerably with the overall loss expected to be nearly two and a half times higher than in 2014, equivalent to some US$215 million. Expenditure increases occasioned by the need to respond to the ongoing health emergency are continuously revisited and as a consequence are difficult to project firmly. As a result the fiscal deficit is projected to remain elevated at 6 percent of non-iron ore GDP in 2015.

2.26 **Fiscal risk from the financial sector in terms of roll over risk and higher implicit contingent liabilities relating to recapitalization has elevated.** Monetary policy needs adjustment to achieve a normal, positive real interest rate yield curve. High money supply growth rates, particularly M1, and the accommodative stance of the central bank have resulted in negative real yields on government securities. While this has lowered domestic interest costs significantly, it is likely to have increased rollover risk. Negative real yields are not sustainable. There has been a decisive shift in government security holdings away from non-bank financial institutions toward banks—narrowing the market in public debt securities. Application of more rigorous prudential standards and foreign exchange controls that have resulted in a large increase in provisions for bad and doubtful debts and reduction in the volume of foreign exchange transactions, coupled with a dearth of bankable projects, has meant that lower interest rates have not translated into higher private sector credit growth. Instead, bank profitability and capital levels have both declined sharply. Ebola has not to date affected bank deposit levels although there has been a shift away from time and foreign currency deposits toward demand deposits.

2.27 **Fiscal risks are mounting—not only from a decline in international commodity prices and the impact of the Ebola epidemic—but from other sources including a deteriorating financial sector, what appears to be a structural decline in non-iron ore revenues and a significant expansion in non-discretionary spending**. The challenge for the Government will be to deal effectively with Ebola as well as heightened community expectations of mineral and post-election boom aspirations and the dire need to increase poverty-related and public infrastructure spending. This will be challenging given the fast moving nature of the epidemic and related new spending demands that it is generating, while revenues respond inversely and significant constraints exist on the capacity to finance expenditures from the domestic financial sector. In this respect it is imperative to address structural policy and infrastructure issues and improve public financial management to give Sierra Leone the best chance of a speedy post-Ebola recovery.

2.28 **The challenge for Government and central bank is to maintain a prudent and well capitalized banking system and facilitate the financing of government's fiscal requirements particularly through this difficult Ebola period**, whilst enhancing the environment for bankable projects and private sector credit growth. In this respect, whilst the Government is preoccupied currently with its financing needs, it remains committed to the rehabilitation of the state banks, and consideration is being given to strengthening the central bank's balance sheet. A risk management plan is being developed alongside debt management arrangements, the duration of the domestic debt portfolio is being lengthened and the market in government securities is being broadened.

2.29 **The relatively stable currency has come under pressure since mid-July due to Ebola related pressures, reversing recent concerns about real effective exchange rate appreciation and the effects on competitiveness.** The pace of nominal depreciation with respect to the U.S dollar has increased recently as the Leone has fallen by about 8.3 percent over July-October. Notwithstanding these short term pre-occupations the Government will need to be cognizant of *Dutch disease* issues over the medium to long term. The recent central bank instruction to enforce foreign exchange control laws on currency movements on the commercial banks appears to have reduced foreign exchange holdings by the banks and related transaction fee income. These measures have resulted in some downward pressure on the nominal exchange rate while parallel market spreads have increased.

2.30 **The three main sources of risk to the outlook are emerging from the Ebola epidemic, the growth outlook in the world economy and difficulties to enhance domestic economic management**. The duration and spread of the Ebola virus is highly uncertain and the costs difficult to quantify but they appear to be rising sharply as transmission of the disease has increased. It has certainly heightened downside risks to the economy, imposed great hardship on people and will retard economic growth. The latter will also be impacted by the prospects for a pickup in industrial production in China and economic growth prospects in Europe and the U.S. and the direct link to commodity prices. Conflicts in the Middle East and former Soviet Union states will impact on imported petroleum prices and regional stability. Iron ore prices have been particularly volatile in 2012-14 and would appear to be on a significant declining trend. The increase in world supply of iron ore from the low cost majors is also likely to maintain depressed prices for a number of years. Gold, bauxite and mineral sands' prices also appear to be on declining trends. This has rendered forecasts of production and government revenue receipts from mining particularly difficult. The earlier optimism of large second phase iron ore developments is fading and the viability of the projects increasingly questioned. The Ebola epidemic may reduce the urgency of the domestic structural policy reform agenda where commitment was already finely balanced.

2.31 Risks from domestic economic management relate to: (a) shortfalls in domestic revenue collections mainly due to weakness in tax compliance; (b) the continuation of strong political pressures to increase recurrent and infrastructure spending, the productivity of which could be questionable, in the absence of robust public expenditure, public investment and cash forecasting processes and accountabilities in place, and without first ensuring adequate domestic financing; (c) implicit contingent liabilities materializing from the financial sector relating to potential state bank rehabilitation costs and potential underfunding and weak governance of the public pension scheme; (d) the continuation of the poor performance of state owned enterprises, particularly the utilities; and (e) lasting social impact from Ebola.

2.32 **A debt sustainability analysis (DSA) conducted jointly with the IMF in October 2013 was updated in September 2014 and concluded that Sierra Leone's risk of debt distress continues to remain moderate**. The update took account of the initial impact of Ebola and concluded that in addition to the unchanged debt distress risk, that stress tests point to vulnerability to adverse shocks affecting key macroeconomic variables, particularly exports, commodity prices, FDI inflows, government revenue and borrowing conditions. Debt prospects over the medium term horizon are consistent with the previous DSA, especially with respect to external debt which rises modestly from present levels of around 23 percent by 1-2 percentage points. Notably, however, domestic debt is on a rising trajectory.

2.33 **The macroeconomic policy framework set out above provides an adequate basis for the proposed operation, although with an unusually high degree of risk associated with it as noted above**. The costs of the Ebola outbreak have been assessed by the IMF and a financing plan agreed for 2014 involving an augmented ECF. Financing for the expected lagged costs of the program for 2015 have not been confirmed to date. Whilst there was some fiscal slippage over the first half of 2014 and despite Ebola being the main focus of Government attention over the second half, the Government remains committed to rectifying the structural elements underlying the fiscal slippages of the first half of 2014. In this respect the Government remains committed to greater revenue efforts, tighter expenditure controls and mitigation of fiscal risk, including a more coherent wage policy and improved frameworks for public investment and financial risk management. If the Government undertakes its reform commitments, as expected, and the costs of the Ebola epidemic are financed externally, the macroeconomic framework should be sustainable over the medium term. The IMF is conducting close program monitoring, particularly with respect to Ebola-related spending, financing limits and fiscal transparency, and

Government has re-affirmed its commitment to adhere closely to the agreed macro-fiscal program.

C. IMF RELATIONS

2.34 **Government entered into a new three-year ECF arrangement for SDR 62.22 million (US$95 million equivalent) with the IMF in October 2013, following cancelation of the previous ECF-supported arrangement earlier in 2013**. Policies under the program are to entrench macroeconomic stability, build fiscal and external buffers and improve prospects for inclusive growth, in the context of the new *Agenda for Prosperity.* Structural reforms continue to focus on strengthening the fiscal position through enhanced revenue mobilization and public financial management reforms. Structural benchmarks under the IMF program include legislation for an Extractive Industries Revenue Act, a new Tax Administration Act, a new Public Finance Act that includes a Natural Resource Revenue Fund and an associated fiscal rule, establishment of a natural resource revenue unit in the National Revenue Authority, establishment of a Treasury Single Account, establishment of a Public Investment Management Unit in MOFED, publication of a Public Investment Program for 2015-18, and a road map to guide the transition to a risk-based prudential supervisory system for the banking sector. The program is anchored on a ceiling of 2 percent of non-iron ore GDP for domestic bank and non-bank financing.

2.35 **The IMF completed its first review under the extended ECF arrangement in June 2014 and noted compliance with all performance criteria, all but one indicative targets and all structural reform measures**. The review noted, however, that the balance of risks was to the downside reflecting the decline in international mineral prices, uncertainties over external budget support, and a fragile fiscal position because of the low revenue base and expenditure pressures. The staff cautioned the Government on the financial implications of large scale investment projects.

2.36 **Responding to the Ebola outbreak, in September 2014, the IMF Board approved a request for augmentation of access under the ECF, of 25 percent of quota for SDR 25.93 million (US$39.8 million equivalent) through an ad hoc review.** End-December 2014 performance criteria on net domestic bank credit to the central government and on net domestic bank assets of the central bank were also modified to allow the use of IMF financing for budget support in order to meet the financing requirements of the adjusted program. In effect the central bank will lend the leone equivalent to the Government and use foreign exchange sales to mop up liquidity as government spending occurs. This should also reduce some of the pressures in the domestic securities market.

3. THE GOVERNMENT'S PROGRAM

3.1 **The *Agenda for Prosperity* covers the period 2013-18 and sets out Sierra Leone's vision to be an inclusive, green, middle-income country by 2035**. This strategy follows the *Agenda for Change,* the second PRSP that covered the period 2008-12. The proposed operation is fully consistent with the *Agenda for Prosperity* and the Government's program. *The Agenda for Prosperity* is based on wide consultation, underpinned by an economic growth diagnostic analysis, and takes account of the lessons learned from implementation of the second PRSP. The strategy maintains the main thrust and areas of focus of the second PRSP and includes pillars covering: Diversified Economic Growth; Managing Natural Resources; Accelerating Human Development; International Competitiveness; Labor and Employment; Social Protection; Governance and Public Sector Reform; and Gender and Women's Empowerment. Efforts to improve implementation of PRSP-3, include targets that cascade down to the district level, where most of the collection and reporting of information takes place. The Strategy and Policy Unit in the Office of the President has responsibility for quarterly reviews of the Performance Management Contracts of Ministries, Departments and Agencies (MDAs).

3.2 **Positive developments in the mineral and hydrocarbon sectors over the past four years generated high expectations about economic opportunities which now need to give way to greater realism**. Implementation of PRSP-3 will need to address several key challenges facing Sierra Leone, including appropriate extractives sector development and management of any wealth that this may generate (less of a factor during PRSP-2). Principal among these challenges are poverty reduction, addressing the infrastructure deficit, improving public sector performance and governance; all consistent with the progress achieved during the *Agenda for Change*. Accordingly, the PRSP-3 places emphasis on a re-prioritization of inclusive growth, youth employment, natural resource management, gender empowerment and greater effort directed at poverty reduction. Ongoing World Bank operations in Sierra Leone are consistent with such pronouncements and aim to support the country in identification of additional drivers of growth, especially in key sectors such as tourism, fisheries, trade facilitation and cash-crops.

3.3 **Adherence to sound fiscal and monetary policies to support macroeconomic stability is an important PRSP-3 priority.** Underpinning the maintenance of this stability will be government efforts, supported by this operation, to respond as effectively as possible to curb the spread of Ebola by, (i) strengthening public financial management to ensure scarce resources are used as efficiently as possible; and (ii) enhancing transparency and accountability.

3.4 **Government's National Ebola Response Plan was revised in early October 2014, with the goal to address and reverse the spread of disease within a ninety day period.** Accordingly the plan has four specific strategic objectives: (a) achieve isolation of at least 40 percent of infected people in a period of 30 days, from the present rates of 17-25 percent; (b) increase isolation of infected persons to 75 percent of cases and achieve 75 percent safe burial within a period of 60 days; (c) achieve 100 percent isolation of both cases of infected persons and safe burial within 90 days; and (d) achieve areas clear of Ebola, including the capital Freetown and a declining case rate within 90 days.

3.5 **The plan has components covering case management, surveillance, social mobilization, child protection, communications and public relations, operational and logistical support for field teams and accountability and gender and psychosocial support**. The goal of the latter component is to provide psychosocial services, (interim care, social mobilization, family tracing and reunification assistance) for EVD-affected individuals and families, including children, women, men and disabled persons. This is being overseen by the Ministry of Social Welfare, Gender, and Children's Affairs working in concert with international partners.

4. THE PROPOSED OPERATION

A. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

4.1 **The policy actions in the proposed EEFSO are consistent with the Government's Ebola response plan and national development program as defined in the PRSP-3 and reflected in the Letter of Development Policy. They will directly contribute to closing the fiscal gap in 2014**. They are also aligned with previous PRSPs and the Bank's previous support through programmatic development policy operations. Indeed prior to the onset of Ebola a new three year programmatic series of development policy operations was under preparation and discussion with the government was advanced. A number of the policies and prior actions identified remain valid for the purposes of this emergency stand-alone operation.

B. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

4.2 **The EEFSO is organized around two broad pillars that contribute directly to supporting and strengthening Government's management of public resources in response to the social and economic crisis spawned by Ebola**, and the macroeconomic and fiscal demands resulting from the same. The first pillar relates directly to the Ebola response and aims to strengthen budget management and reduce fiscal risks that have been heightened by Ebola. The second pillar is concerned with actions to improve transparency and accountability for use of public resources through disclosure and fostering accountability. Improving overall public sector governance is imbued in both pillars.

Background

4.3 **The Ebola outbreak which began in May 2014 spread from neighboring Guinea into Kailahun then Kenema district, the former considered Sierra Leone's breadbasket. To date it has spread to all 13 districts and the capital**. Resultant quarantines imposed to try to stem the spread of the Ebola virus in these and subsequently three other productive agricultural districts have led to widespread disruption of agriculture, coming close to the planting season. Hence the full effect on agricultural production is likely to be evident only in 2015. Closure of markets, has for the same reasons, led to sporadic localized shortages and food price spikes. The World Food Program, normally an active player in Sierra Leone—on account of 2.5 million persons annually considered at risk of having insufficient food—is carrying out an expanded program of food delivery in response to the Ebola epidemic.

PRIOR ACTIONS AND RESULTS

Strengthen Budget Management and Reduce Fiscal Risks Heightened by Ebola

Prior Action #1: *The Recipient's Ministry of Finance and Economic Development has established a formal hazard payment system for clinical and non-clinical workers responding to the Ebola crisis.*

4.4 **A large number of clinical and non-clinical personnel are engaged in precarious work, to contain the spread of the Ebola virus, diagnose the afflicted, care for the sick and bury the dead.** Some of these are already public sector employees while many are casuals and volunteers from society at large. The Government has instituted a system of hazard pay for those involved in the frontlines of this perilous work. The World Bank together with the African Development Bank and other partners is financing this through the Ebola Emergency Response project and the proposed Additional Financing for the same. The number of people engaged in this task has swelled to more than 3,000 presently and is expected to rise further. Payments to these clinical and non-clinical workers have been difficult to effect because of the *ad-hoc* nature of their employment; payments were initially made in cash and distributed to District Officers in each district, sometimes directly and at other times through further intermediaries, depending on the location of the recipient. Government has subsequently recognized that such an *ad-ho*c system is not consistent with good principles of financial management and could also invite abuse and result in wasted resources. Moreover, it is now also clear that the crisis will not be a short term one with temporary mobilization of workers and that these payments may need to be maintained for longer than initially expected. MOFED therefore pledged to take the necessary actions to establish a system to ensure that all eligible clinical and non-clinical workers receive hazard payments through a formal payments system such as a bank account or a mobile payment system, with respect to their responsibilities in responding to the Ebola Virus Disease crisis.[11] This action has been met.

Prior Action #2: *The Recipient's Ministry of Finance and Economic Development has appointed a fiduciary agent to ensure that the clinical and non-clinical workers receiving hazard payments are entitled to receive said hazard payments and are providing appropriate services.*

4.5 In parallel with the efforts to formalize all payments through a verifiable electronic payment system, a fiduciary agent has been appointed to put in place a financial management system that includes complying with hazard pay guidelines to ensure that rightful beneficiaries are paid. Additional measures that will complement the work of the fiduciary agent include the internal auditors providing oversight to oversee payments, to ensure that they are being made correctly to the intended beneficiaries who are indeed providing the requisite service in the fight against Ebola. To enhance transparency and support accountability the system also provides for periodic public disclosure of the payments made for this purpose as well as for all Ebola related expenditures; it also provides for the establishment of a complaints mechanism. A key action for the system to function effectively, to which Government committed, was the appointment on November 18, 2014 of a fiduciary agent to oversee this process. This action has been met.

[11] This covers six categories of personnel including those working at Ebola Treatment Centers, Ebola Care Centers, Ebola Holding Centers, laboratory workers, screening workers and burial teams.

4.6 ***Results.* The expected result of these measures will be to establish a robust and accountable temporary payment system which could be rapidly re-mobilized in the event of future national emergency.**

Prior Action #3: *The Recipient's Ministry of Finance and Economic Development has executed a Loans and Fiscal Agency Agreement with the Bank of Sierra Leone as part of the implementation of phase one of the Treasury Single Account.*

4.7 The establishment of a robust cash management system supported through the design and implementation of a Treasury Single Account (TSA) is critical for credible budget implementation. The creation of a TSA could lead to significant reductions in domestic bank financing costs, rationalize the build-up of expenditure arrears, and improve the predictability of resource flows to service delivery agencies. Government's weak budget credibility and the inherent weaknesses in fiscal forecasting of both revenues and expenditures result in a lack of predictability in resource flows to MDAs for service delivery whose obligations are not often met on a timely basis. The orderly but progressive implementation of a TSA would need to be conducted within the confines of a robust cash management system, coordinated under the auspices of the Cash Management Committee. The Office of the Accountant General is gearing itself to implementing a robust TSA, grounded on a strong cash management arrangement.

4.8 Implementation of the TSA will support compliance with the requirements of the Bank of Sierra Leone (BSL) Act on borrowing, including linking all government bank accounts (exclusive of privatization receipts but inclusive of cleared balances from NRA transit bank accounts held with commercial banks). Government has already carried out an inventory of its bank accounts, for official bank accounts held in the BSL and commercial banks (Table 4.1). TSA implementation is expected to be in three phases. The first phase which included completing an inventory of government bank accounts concluded with the signing of a Loans and Fiscal Agency Agreement between the MOFED and the BSL governing the TSA. <u>This action has been met</u>.

Table 4.1: Inventory of Official Government Bank Accounts

Type of Account	**Number of Bank Accounts**		
	Total	*In BSL*	*In Commercial Banks*
Sub-vented Agencies	461	38	423
Transit	117	0	117
Projects	279	34	245
Treasury	57	57	0
Departmental	475	118	357
Local Councils	183	0	183
Govt. Business Entities	223	2	221
Total	**1,795**	**249**	**1,546**

4.9 ***Results.* The expected result of these measures will be to secure a much higher level of budget control, execution and accountability and thus enhance the predictability of .resource flows to service delivery agencies.**

Prior Action #4: *The Recipient's Ministry of Finance and Economic Development has received audited financial statements for year ended 2013 for Sierra Leone Commercial Bank Limited and Rokel Commercial Bank (Sierra Leone) Limited, respectively, with a view to assessing the contingent liability implications for said Sierra Leone Commercial Bank Limited and Rokel Commercial Bank (Sierra Leone) Limited.*

4.10 Sierra Leone Commercial Bank Limited (SLCB) is fully state owned and Rokel Commercial Bank (Sierra Leone) Limited (RCB) is part state-owned with the National Commission for Privatisation, the largest shareholder. These two state banks (accounting for 30 percent of private sector system lending) have had their private sector lending programs effectively halted in 2014 because of serious prudential concerns regarding their loan books necessitating large provisioning amounts. Both have had their management heads replaced over the past year. Implementation of more rigorous prudential lending standards being applied by the BSL in early 2014 has also placed more pressure on the financial position of these two institutions. The new limits on large exposures and greater disclosure of poorly performing loans and consequent higher provisioning levels for bad and doubtful debts may have resulted in both having negative regulatory capital with bad debt provisions being increased from Le 44 billion at end-March 2014 to Le 155 billion at end-June 2014. While some loan recoveries were achieved over the first half of 2014, these are unlikely to be sufficient to restore bank capital ratios and profitability concerns will remain.

4.11 These two institutions are thus a source of significant fiscal risk to the Government. Given the considerable difficulties that SLCB and RCB are facing as detailed above, the resolution of these issues will require as a starting point a clear understanding of their underlying financial situation that would emerge from audited financial statements. This action aims to support this process through completion of such audits for the 2013 financial year and issuance of the audited reports to the Government so that it can properly assess the attendant fiscal risk in terms of the contingent liability implications and design and prepare an appropriate risk management framework governing all debt and debt related operations. This action has been met.

4.12 ***Results.*** **The expected result of these measures will be to progressively identify the contingent liabilities and to manage the fiscal risks therefrom**.

Improve Transparency and Accountability for use of Public Resources

Prior Action #5: *The Recipient's Ministry of Finance and Economic Development has submitted a Supplementary Budget for extra-budgetary expenditure in Fiscal Year 2014 to Parliament.*

4.13 Budgetary over expenditure such as that in the first half of 2014 needs to be sanctioned by the appropriate legislative body or oversight entity in order to ensure appropriate accountability. This is particularly important in Sierra Leone with its cash accounting system as over spending in one year that leads to a fiscal overhang in the following year, needs to be adequately accounted for and accommodated in the absence of which it will undermine budget execution in the subsequent year. It is not expected that utilization of supplementary budgets will encourage persistent over-spending rather, the increase in accountability and transparency within a rigorous IMF program should ensure the adherence of fiscal targets. In Sierra Leone both the Constitution and the Government Budgeting and Accountability Act (GBAA) require that Parliament sanction higher than budgeted expenditures, either through a supplemental appropriation or supplementary budget. On July 10, 2014, Government submitted a Supplementary Appropriation Act and accompanying Budget to Parliament for 2014. This action has been met.

Prior Action #6: *The Recipient's Ministry of Mines and Minerals has published all signed Mineral Lease Agreements with a view to increasing transparency and accountability in the mineral sector.*

4.14 **These two prior actions relate to revenue transparency and strengthened accountability in the minerals sector through public disclosure**. They are concerned with fostering increased accountability through observance of good practice and compliance with legislative requirements. Under this prior action, Government committed to publish all (6) signed Mineral Lease Agreements on-line. This was duly completed in first half 2014. This action has been met.

Prior Action #7: *The Recipient's Ministry of Finance and Economic Development has published in Fiscal Year 2014, data on revenue collected in Fiscal Year 2013 from top extractive industries consistent with §159 of the Mines and Minerals Act.*

4.15 Under the Mines and Minerals Act, (2009) the Minister is required to annually disclose and disseminate detailed information on revenues from the sector to the public. Compliance to date has been difficult due to fragmentation of the required data across agencies and recording systems, but is being addressed through a pilot data integration project. In the interim Government committed to disclose publicly in 2014, a statement of the revenue collected in 2013 from the top 10 extractive industries, by revenue type, in accordance with §159 of the Mines and Minerals Act, 2009, and consistent with Government commitments under the Extractive Industries Transparency Initiative. A statement of revenues collected was prepared by the NRA and disclosed on the MOFED website in June 2014 covering the ten largest firms.[12] This action has been met.

4.16 ***Results.*** **The expected result of these measures will be increased budget execution, enhanced transparency and increased accountability in the minerals sector**.

ANALYTICAL UNDERPINNINGS

4.17 The Bank, together with other partners, has undertaken analytical work and provided technical assistance complemented by a policy dialogue in the policy areas relating to the prior actions supported under the proposed operation. These cover the period 2010-12 and are summarized below (Table 4.2).

[12] http://mofed.gov.sl/publications/2013%20Mines%20Revenue%20i.pdf; accessed on October 28, 2014.

Table 4.2: Prior Actions and Analytical Underpinnings

Action	Analytical Underpinnings
Strengthen Budget Management and Reduce Fiscal Risks Heightened by Ebola	
1. The Recipient's Ministry of Finance and Economic Development has established a formal hazard payment system for clinical and non-clinical workers responding to the Ebola crisis.	*(a) Sierra Leone National Ebola Response Plan (2014); (b Government Budgeting and Accountability Act, (2005); (c) Auditor General's Report on the Public Accounts (2011 & 2012).*
2. The Recipient's Ministry of Finance and Economic Development has appointed a fiduciary agent to ensure that the clinical and non-clinical workers receiving hazard payments are entitled to receive said hazard payments and are providing appropriate services.	*(a) Sierra Leone National Ebola Response Plan (2014); (b) Government Budgeting and Accountability Act, (2005); (c) Auditor General's Report on the Public Accounts (2011 & 2012).*
3. The Recipient's Ministry of Finance and Economic Development has executed a Loans and Fiscal Agency Agreement with the Bank of Sierra Leone as part of the implementation of phase one of the Treasury Single Account.	*(a) Public Expenditure Review (2010); (b) Auditor General's Report on the Public Accounts (2012). (c) 2012 PEFA Report (published in 2014); (d) Sierra Leone: Treasury Single Account, Crown Agents, October 2013.*
4. The Recipient's Ministry of Finance and Economic Development has received audited financial statements for year ended 2013 for Sierra Leone Commercial Bank Limited and Rokel Commercial Bank (Sierra Leone) Limited, respectively, with a view to assessing the contingent liability implications for said Sierra Leone Commercial Bank Limited and Rokel Commercial Bank (Sierra Leone) Limited..	*(a) Sierra Leone: Diagnostic and Policy Note, Fiscal Risk Assessment, 2013; (b) Auditor General's Report on the Public Accounts (2012).*
Improve Transparency and Accountability for Public Resources	
5. The Recipient's Ministry of Finance and Economic Development has submitted a Supplementary Budget for extra-budgetary expenditure in Fiscal Year 2014 to Parliament.	*(a) Public Expenditure Review (2010); (b) Auditor General's Report on the Public Accounts (2012); (c) Constitution of Sierra Leone, (1991); (d) Government Budgeting and Accountability Act, (2005).*
6. The Recipient's Ministry of Mines and Minerals has published all signed Mineral Lease Agreements, with a view to increasing transparency and accountability in the mineral sector.	*Sierra Leone Mines and Minerals Act, (2009).*
7. The Recipient's Ministry of Finance and Economic Development has published in Fiscal Year 2014, data on revenue collected in Fiscal Year 2013 from top extractive industries consistent with §159 of the Mines and Minerals Act.	*Sierra Leone Mines and Minerals Act, (2009).*

C. LINK TO CAS AND OTHER BANK OPERATIONS

4.18 The proposed EEFS is fully consistent with the Joint Assistance Strategy (JAS) prepared in collaboration with the AfDB and the International Finance Corporation and discussed by the Board on April 6, 2010. The JAS established the Bank's support to the PRSP-2 covering the period FY10-13 through its two pillars on Human Development and Promoting Inclusive Growth. A successor Country Partnership Framework is under preparation to support the newly launched PRSP-3. A CAS Progress Report prepared in 2012 emphasizes the centrality of Development Policy Operations (DPOs) to the Bank's continued engagement in Sierra Leone and introduces a third pillar on Managing the Extractives Boom in recognition of the changing country context. Other Bank operations in the health sector, public financial management, and the minerals sector are linked to the proposed operation and also provide valuable support through Technical Assistance.

4.19 **In the health sector, the ongoing IDA-financed Ebola Emergency Response Project will provide critical support to Sierra Leone in managing the Ebola epidemic and bringing it under control** through financing of essential personal protective equipment for health care workers, medical supplies and equipment, and hazard pay for health care workers and others on the front-lines of this growing international health emergency. The recently approved Additional Financing to this project will also finance pre-investment rapid assessment and planning of new Ebola therapies, diagnostics and potential vaccine candidates and the international health worker response as well as a scaling-up of community based care and community-led activities.

D. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

4.20 Sierra Leone has an established system of undertaking consultations with relevant stakeholders where legislative reforms are to be undertaken. These are largely confined to the government sphere but are nevertheless important in ensuring consistency and ownership. Consultation on the reforms supported under DPOs has been uneven and more limited.

4.21 The Bank collaborates closely with the IMF and the MDBS partners comprising the AfDB, DFID, and the European Union. This extends to a close discussion and collaboration on macro-fiscal and financial sector issues and structural reforms with the IMF. Close collaboration with the MDBS partners encompasses program design and implementation. The IMF and MDBS partners have been providing financial support to Sierra Leone since the end of the civil war in 2002. This normal collaboration has been vastly expanded since the start of the Ebola crisis and extends to all the main actors that are involved in the fight to contain the spread of Ebola, including the UN Mission for Ebola Emergency Response, the World Health Organization, Médecins Sans Frontières and the U.S. Centers for Disease Control

5. OTHER DESIGN AND APPRAISAL ISSUES

A. POVERTY AND SOCIAL IMPACT

5.1 **Measures supported by the proposed EEFSO are expected to have a positive and direct impact on poverty reduction**. The EEFSO is designed to support Sierra Leone's efforts to bring the Ebola epidemic under control. In this regard it focuses on fiscal support to the overall budget and the Ebola response and on strengthening public financial management. To the extent that the poor are more vulnerable to Ebola, having little recourse in terms of financial resources or mobility to mitigate it, they would benefit more from this operation. Moreover, the prior actions which are concerned with improved transparency and disclosure should strengthen governance and lead to reduced rent-seeking, and allow for more resources to be available in support of the poor and vulnerable. The direct beneficiaries of the proposed EEFSO include those in Ebola-affected areas, which are presently widespread in Sierra Leone covering both rural areas and urban centers including the capital. *No significant adverse social or poverty impacts are expected from the prior actions supported by the operation.*

B. ENVIRONMENTAL ASPECTS

5.2 **The reforms supported by the proposed EEFSO are not likely to have any positive or negative effects on the environment, natural resources and forests as they do not entail any environmental effect**. By providing for better resourcing of the fight against the Ebola virus, it is possible that there may be some positive environmental effects through improved disposal of medical and other waste. Moreover the ending of the Ebola epidemic will likely have positive environmental benefits associated with it.

C. PUBLIC FINANCIAL MANAGEMENT, DISBURSEMENT AND AUDITING ASPECTS

Public Financial Management Systems

5.3 **While weaknesses continue to manifest themselves within the overall PFM environment in Sierra Leone, there have been progressive improvements in key areas since the emergence of earlier *governance reform and growth* policy-based operations**. Weaknesses remain due to delays in eliminating inconsistencies in the enabling legal framework (GBAA, 2005), as well as inherent capacity constraints of PFM actors, resulting from the over-spills from the country's historical fragility. Measurable progress has been achieved in critical areas of reform, partly due to the concerted efforts of development partners in support of the Government program of reforms, and partly as a result of government's own demonstrated commitment to raise the profile of PFM within its menu of governance reforms. With the closure of the joint donor-supported project, the Integrated Public Financial Management Project (IPFMRP), which had served as a primary vehicle and essential thrust for implementing PFM reforms, a follow-on joint donor financed PFM operation—PFM Improvement and Consolidation Project (PFMCIP)—has been designed and is currently in its initial stages of implementation. The new reform project which aims to build on the achievements of the IPFMRP, was in response to the Government's own priority reform requirements as contained in its PFM reforms strategy (2014-2017). In effect, the continuing commitment of the government to address weaknesses in PFM remains unflinching. The expected outcome of the new reform platform is to improve budget planning and credibility, financial control, accountability and oversight in government finances.

5.4 **Considerable analytical work in the area of PFM has been conducted with the support of development partners in Sierra Leone during the past several years**. Key amongst these were PEFA assessments in 2007, 2010 and 2012; a Country Procurement Assessment Review (using the OECD bench-marking tool) in 2011; IMF Fiscal Affairs Department PFM Review in March 2008; IMF Fiscal Affairs Department Report on

Determination and Implementation of Fiscal Rules in 2012; Tax Administration Reforms for Successful VAT Implementation published in March 2008; and a 2010 Review of the GBAA and Financial Management Regulations.

5.5 **A comparison of PEFA scores in 2010 vis-à-vis 2012 has shown that the overall PFM performance improvement has been uneven, with a number of key performance indicators having registered poorer ratings largely due to systemic weaknesses in budget credibility.** Evidence since 2012 though, points to a slight comparative improvement in fiscal discipline, resulting in improved budget credibility at both central and local government levels. In summary, the 2012 PEFA does reflect that the overall domestic conditions supporting macroeconomic and fiscal stability remain fragile and fraught with issues due essentially to marginal progress in structural reforms that continue to endanger fiscal discipline. These issues include (a) the delay in amending the PFM laws to take cognizance of improved fiscal control mechanisms; (b) the need to restructure MOFED to increase its effectiveness and efficiency; (c) budget management and control processes which show variances between a priori and de factor practices and well as the lack of comprehensiveness; (d) shortcomings in fiscal reporting for compliance with international standards; (e) the impact of legislative scrutiny of both the annual budget law *(ex-ante)* and the ex post review of budget implementation.

5.6 **Concrete PFM improvements as reported by the 2012 PEFA can be found in a number of important areas.** These include: (a) improvements in the control and management of expenditure arrears; (b) enhanced comprehensiveness of and transparency in budget documentation, and publication of the budget document; (c) improved collection and monitoring of tax payments; (d) improvements in cash management, notwithstanding the short-termism focus in the arrangements in the absence of a well-functioning Treasury Single Account; (e) improvements in account reconciliations and timeliness in, and quality of, financial reporting; (f) improved effectiveness of internal audit across MDAs; and (g) significant improvements in external audit oversight and audit quality.

5.7 **With the establishment of a Procurement Regulatory Authority and procurement units in MDAs under the 2004 Public Procurement Act and the procurement regulations, the institutional basis for strong value for money procurement arrangements across government is established.** Nevertheless, there is scope to strengthen not only the capacity of the regulatory authority to monitor performance and compliance, but also the capacity of the procurement staff assigned to MDAs at the central and sub-national governments. In addition, strengthening the complaints mechanisms and appeals processes will scale up the contribution of public procurement to the overall expenditure management outcomes in Sierra Leone. These and other reforms are being considered for inclusion in the amendment of the 2004 Public Procurement Act with a view to improving value for money and transparency in the use of public funds.

5.8 **The IMF conducted Safeguards Assessments of the Bank of Sierra Leone (BSL) in 2002, 2006, 2010, and as recently as February 2014.** The BSL has consistently implemented virtually all the recommendations in all the pre-2014 assessment reports. The safeguards framework of the Bank has been strengthened since 2010 in the areas of internal audit and legal, and the accountability framework has also remained adequate. The 2014 assessment report however highlighted further recommendations in the following key areas: (a) appointment of

Directors to avoid gaps in the governance structure of the Bank; (b) strengthening the role of the Audit Committee over the external audit oversight function; and (c) strengthening the Bank's financial autonomy through its re-capitalization, consistent with the BSL Act, 2011. The BSL and the Government of Sierra Leone have begun the process of addressing the identified weaknesses.

5.9 **Overall, based on the improvements already made as well as the demonstrated commitment of the Government to implement wide ranging reforms in the area of PFM**, including public procurement, and with the results of the 2014 IMF Safeguards Assessment of the Bank of Sierra Leone, the fiduciary risk of the operation is rated 'moderate'. In essence, no additional fiduciary arrangements are considered necessary for this operation.

Disbursement and auditing issues

5.10 **Recipient and Financing Agreement:** The proposed operation is a one-tranche IDA grant of SDR 20.6 million (US$30 million equivalent). The grant disbursement will follow the standard Bank procedures for Development Policy Lending. The administration of this grant will be the responsibility of the Ministry of Finance and Economic Development.

5.11 **Funds flow arrangements**: The Government of Sierra Leone shall identify a Foreign Exchange Account with the Bank of Sierra Leone, and which forms part of the country's official foreign exchange reserves, into which the proceeds of the grant will be disbursed upon grant effectiveness, subject to meeting the agreed prior actions. The Sierra Leone 'Leones' equivalent of the funds in the account will, within two working days, be transferred into the Consolidated Fund of the Government of Sierra Leone, and the amount recorded appropriately in the budget management system of the Government.

5.12 **Disbursements from the Consolidated Fund by the Government of Sierra Leone shall not be tied to any specific purchases and no special procurement requirement shall be needed**. The proceeds of the grant shall, however, not be applied to finance expenditures on the negative list as defined in Schedule 1 of the Financing Agreement. If any portion of the grant is used to finance ineligible expenditures as so defined in Schedule 1 of the Financing Agreement, IDA shall require the Government to promptly, upon notice from IDA, refund an amount equal to the amount of the said payment to IDA. Amounts refunded to IDA upon such request shall be cancelled from the grant.

5.13 **Assurance Requirements**: Based on the moderate fiduciary risk associated with the operation, there will be no special or additional fiduciary arrangements established for the grant in terms of a requirement for an audit, in as much as an audit remains an option. Within 30 days of the disbursement of the grant by IDA, however, the Financial Secretary of the MOFED of Sierra Leone shall provide written confirmation to IDA, certifying the receipt of the 'Leones' equivalent of the grant into the Consolidated Fund Account of the Government of Sierra Leone, the number of the account, the date of the receipt, and the exchange rate applied to translate the grant currency into *Leones.* In addition, as the Auditor General is required by law to submit its annual report and the audited accounts on the public consolidated fund to Parliament within 12 months of the end of the fiscal year, a copy of the said reports and accounts shall be provided to IDA within one month after the lapse of the 12-month period. The Government shall equally ensure that the annual entity financial statements of the Bank of Sierra Leone, audited in accordance with international standards on auditing as promulgated by the International Federation of Accountants, are publicly available.

5.14 The expected closing date of the operation is December 31, 2015.

D. MONITORING AND EVALUATION

5.15 **The MOFED will be responsible for the overall execution of measures implemented under this program**. MOFED has the requisite experience including technical skills and coordination experience for this task, some elements of which it will undertake in conjunction with BSL. Additionally there is a small, well-coordinated group of development partners also providing close support to the government. The Results Framework in Annex 1 provides the list of result indicators which will be used to monitor the progress over the proposed operation.

6. SUMMARY OF RISKS AND MITIGATION

6.1 **The overall risk rating for the operation is 'substantial', with five main sources of risk that could potentially jeopardize the expected outcomes and benefits of this operation**. These are: (i) political and governance risks; (ii) macroeconomic risks; (iii);risks from institutional capacity for implementation and sustainability; (iv) fiduciary risk; and (v) epidemiological risk (Table 6.1). Risk mitigation measures, should they be warranted, are outlined below. The potential benefits of the proposed operation, however, outweigh the residual risks and warrant IDA's assistance to provide critical financial support at this difficult time for Sierra Leone and for implementing reforms and policy actions in coordination with other development partners.

Table 6.1: Risk Rating

Risk Categories	**Rating (H, S, M or L)**
1. Political and governance	M
2. Macroeconomic	S
3. Sector strategies and policies	L
4. Technical design of project or program	L
5. Institutional capacity for implementation and sustainability	M
6. Fiduciary	M
7. Environment and social	L
8. Stakeholders	L
9. Other: Epidemiological	H
Overall	S

Political and Governance Risks

6.2 **Political and governance risk are judged to be moderate in terms of their effect on the project development objectives**. Political risk in particular is considered low as the government is completely committed to the operation which is an important element in its fight against Ebola. Governance risks remain a concern especially when it comes to fraud and corruption though the present emergency situation and direct international response and spotlight is an important mitigating factor.

Macroeconomic Risk

6.3 **Macroeconomic risks are judged to be substantial with three components—aversion behavior as a result of Ebola, exogenous shocks from international commodity prices and domestic policy risk.** These have to some extent already materialized**.** Ebola has led to a large behavioral response through aversion. This has resulted from closure of markets and quarantines to contain the spread of the virus and other restrictions on public gatherings, including closure of restaurants, bars and the like. Other measures such as internal travel restrictions have also played a part. Equally the sharp reduction in commercial flights, restrictions by shipping lines and increased costs are posing a challenge to macroeconomic stability and prospects as the effects on the hospitality sector and services more broadly has been devastating. Additionally, some deferred FDI is adding to the macroeconomic weaknesses, which if maintained over time, could cloud future growth prospects. Efforts by prominent international leaders to speak out against isolation and to maintain ties to the Ebola affected countries at this point offer the only mitigating measures.

6.4 **External exogenous shocks such as those from global commodity prices have already materialized in the case of iron ore.** The two iron ore mines in Sierra Leone have been loss making in 2014. One has gone into voluntary administration in October 2014, mainly on account of falling international prices. The second stopped production to reduce its losses as it seeks to restructure its debt. Other sources of further shock could be a slowdown in China or regional conflicts affecting oil prices. The most appropriate mitigation measure is to accelerate structural reforms to accelerate economic diversification and resiliency. Maintenance of a satisfactory macroeconomic framework, bolstered by continuous dialogue with the community of multilateral and bilateral development partners (including the IMF, World Bank and the MDBS partners) should also mitigate this risk somewhat.

6.5 **Domestic policy risks relating to a number of sources including rollover risk from domestic debt, implicit contingent liabilities relating to recapitalization and continued structural deterioration in non-iron ore revenues--could materialize and be difficult to address if the government is pre-occupied with the need to respond to the Ebola threat or if it is unable to muster the requisite fiscal resolve.** This risk remains a principal source of concern though it is to some extent mitigated by the close and intensive engagement between the Government and international partners that has been occasioned by the Ebola epidemic.

Institutional capacity for implementation and sustainability

6.6 **Weak institutional capacity for implementation and sustainability is judged a moderate risk.** While institutional capacity in Sierra Leone remains inadequate in most areas, the requirements in this area from this operation are quite modest. Sustainability, however, could be more of a concern. The deployment of an external fiduciary agent and the intensive international monitoring presently underway—both in terms of technical support and the media—mitigates against this.

Fiduciary Risk

6.7 **Fiduciary Risk due to weak institutional capacity and poor governance is considered to be moderate**. Weak institutional capacity and corruption generally hampers reform implementation. On the institutional side, weaknesses include a lack of skills and training with respect to procurement procedures and limited accounting skills, especially at the sub-national level. These risks are mitigated by robust PFM measures calibrated to existing capacity, including the provision of extensive technical assistance and capacity building through ongoing or planned projects, and the growing involvement of civil society in oversight activities.

Epidemiological Risk

6.8 **The epidemiological risk is high and growing as Ebola continues to spread in Sierra Leone.** Recent work by the World Health Organization and the U.S. Centers for Disease Control suggest that 0.5-1.5 million persons could be infected in all three countries—Liberia, Sierra Leone and Guinea—by the end of January 2015. Applying the 70 percent mortality rate of the current epidemic yields 0.35-1.05 million casualties across the three countries. Such an outcome could spell disaster for the country's future by significantly increasing poverty and constraining future growth severely. Moreover, since mid-November 2014, transmission of the disease has intensified sharply in Sierra Leone. An important mitigating factor is the increased response and support of the international community which is providing financial, technical and human resources to bring this unfolding catastrophe, under control.

Annex 1: Policy and Results Matrix

Prior Action	*Results Indicator*	*Baseline (2014)*	*Target (2015)*
Pillar A: Strengthen Budget Management and Reduce Fiscal Risks Heightened by Ebola			
The Recipient's Ministry of Finance and Economic Development has established a formal hazard payment system for clinical and non-clinical workers responding to the Ebola crisis.	Clinical and non-clinical workers paid through the formal hazard payment system, disaggregated by gender (%).	Zero (No system in place)	At least 80% of clinical and non-clinical workers paid through the system
The Recipient's Ministry of Finance and Economic Development has appointed a fiduciary agent to ensure that the clinical and non-clinical workers receiving hazard payments are entitled to receive said hazard payments and are providing appropriate services.	Audits of hazard payments by the Internal Audit Department of MOFED (Number)	No audit of hazard payments.	Quarterly audits.
The Recipient's Ministry of Finance and Economic Development has executed a Loans and Fiscal Agency Agreement with the Bank of Sierra Leone as part of the implementation of phase one of the Treasury Single Account.	Aggregate report from banks including opening and closing balances and summary of receipts and payments (Monthly)	No or irregular reporting	Regular bi-annual reports logged by the Accountant General.
The Recipient's Ministry of Finance and Economic Development has received audited financial statements for year ended 2013 for Sierra Leone Commercial Bank Limited and Rokel Commercial Bank (Sierra Leone) Limited, respectively, with a view to assessing the contingent liability implications for said Sierra Leone Commercial Bank Limited and Rokel Commercial Bank (Sierra Leone) Limited.	Estimate of fiscal contingent liability (Yes/No)	No	Yes
Pillar B: Improve Transparency and Accountability for Public Resources			
The Recipient's Ministry of Finance and Economic Development has submitted a Supplementary Budget for extra-budgetary expenditure in Fiscal Year 2014 to Parliament.	• Supplementary Budget for 2014 sanctioned by Legislature (Yes/No) • Budget execution rate (% of appropriation)	• No • 75.4% (end September)	• Yes • Greater than 90%
The Recipient's Ministry of Mines and Minerals has published all the signed Mineral Lease Agreements with a view to increasing transparency and accountability in the mineral sector.	Mineral Lease Agreements published on the internet or otherwise (Percentage of total Lease Agreements on record).	0%	At least 90%
The Recipient's Ministry of Finance and Economic Development has published in Fiscal Year 2014, data on revenue collected in Fiscal Year 2013 from top extractive industries consistent with §159 of the Mines and Minerals Act.	Coverage of 2013 revenues from extractive industries publicly reported (%)	0%	At least 90%

Annex 2: Letter of Development Policy

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December 3, 2014

Dr. Jim Yong Kim
President
The World Bank
Washington D.C.
U.S.A.

THE EMERGENCY ECONOMIC AND FISCAL SUPPORT OPERATION

LETTER OF DEVELOPMENT POLICY

I am writing on behalf of the Government of Sierra Leone to request the approval of the Emergency Economic and Fiscal Support Operation in the sum of US$30 million to support Government's efforts to respond to the challenges posed by the Ebola virus disease Epidemic and thereby mitigate the negative economic and fiscal impact of the Ebola virus disease on the implementation of the Agenda for Prosperity.

Progress in the Implementation of the Agenda for Prosperity

1. Mr. President, you would recall that Sierra Leone Growth and Poverty Reduction Strategy- *Agenda for Prosperity (AfP), 2013-2018,* was launched in July 2013. The AfP aims to consolidate the gains made under the Agenda for Change (2008-12) and addresses other immediate development challenges. The overarching objective of the AfP is to promote sustainable inclusive green growth and poverty reduction.

2. The AfP is anchored on eight sectoral pillars: (i) economic diversification to promote inclusive green growth; ii) managing natural resources; (iii) accelerating human development; (iv) international competitiveness; (v) labour and employment; (vi) strengthening social protection systems; vii) governance and public sector reforms; and (viii) gender equality and women's empowerment.

3. The 2014 financial year marks the beginning of the effective implementation of the Agenda for Prosperity. Thus, the 2014 budgetary allocations to Ministries, Departments and Agencies (MDAs) were closely aligned to the pillars of the Agenda for Prosperity. The implementation of the AfP remained on track during the first half of 2014 as leading indicators pointed towards strong economic growth and a stable

macroeconomic environment. Economic activities were increasing in the midst of declining inflation, lower domestic Treasury bill interest rates and a stable exchange rate.

4. In agriculture, Government continued to provide agricultural inputs and equipment to farmers to enhance agricultural productivity. In the fisheries sub-sector, efforts were underway to operationalise the fish landing jetties. Political stability, combined with improvements in basic infrastructure, attracted foreign investment in the tourism sector.

5. The mining sector continued to expand as the two major iron ore mining projects completed the investment phase of their business plans. Output for the first half of the year indicated that the mining operations were on course to meet their annual production and export targets.

6. In the health Sector, Government continued to strengthen the implementation of the Free Health Care Initiative while providing medical equipment and essential drugs to health facilities. In **the education sector**, Government sharply increased grants to tertiary educational institutions partly to subsidize tuition fees, thereby enhancing access to higher education. The rehabilitation of **water supply systems** in the three provincial districts of Bo, Kenema and Makeni under the ADB funded Three Towns Water Supply Project was progressing satisfactorily. To build social protection systems in the country, Government established the Social Protection Secretariat under the National Commission for Social Action to coordinate all social protection interventions and stakeholders in the country.

7. The construction of **trunk roads and city streets** throughout the country remained on track. The **energy** sector has been reformed with the establishment and operationalization of the Electricity Generation and Transmission Company and the Electricity Distribution and Supply Authority. Major repairs were undertaken on the Bumbuna Hydro Electric Dam as well as thermal plants in Freetown and Bo.

8. In furtherance of **good governance**, Government continued to implement public sector and public financial management reforms, including anti-corruption strategies to improve public service delivery. Civil service reforms, including a medium-term pay strategy were developed and adopted by Government. The National Public Procurement Act 2004 and the Government Budgeting and Accountability Act 2005 were also reviewed during the period.

9. To promote **gender equality and women's empowerment**, Government, with support from partners, developed a web portal to monitor progress in addressing gender inequality in Sierra Leone.

10. Unfortunately, the outbreak of the Ebola virus disease and its rapid spread to all 13 districts in the country derailed the implementation of the A4P. Resources, both human and financial, are now being diverted towards fighting the spread of the disease. The epidemic is reversing the gains made in economic and social progress in recent years and poses a significant threat to macroeconomic stability, human development and poverty reduction in the medium-term.

Recent Economic Performance, 2011-13

11. Mr. President, substantial progress was made in stabilizing the economy while sustaining economic growth. Efforts continued to address the challenges in service delivery in recent years. Economic growth accelerated to 15.2 percent in 2012 and further to 20.1 percent in 2013, from 6.0 percent in 2011, owing to expansion in the mining sector, especially iron ore production and exports. Growth of the non-iron ore economy also remained strong averaging 5.5 percent during the review period underpinned by increased activities in agriculture, fisheries, construction, and services sectors and supported by increased public investment in infrastructure.

12. Inflationary pressures receded in 2012. Year-on-year national inflation returned to single digits in the fourth quarter of 2013. This is due to a combination of pro-active monetary policy, stable exchange rates, stable world food prices and increased domestic food production. National inflation declined from 16.7 percent at end 2011 to 11.4 percent at end 2012 and further to 8.2 percent at end 2013.

13. Fiscal performance improved markedly in 2013 following weak performance during 2010-2012. With budget deficits, excluding grants, averaging 10 percent of GDP during the period, the budget deficit, including grants, narrowed to 4.9 percent of GDP in 2013 as domestic revenues were higher-than projected while expenditures remained broadly within budgeted limits. The lower deficit also followed fiscal consolidation measures adopted by Government, supported by the weekly meetings of the Cash Management Committee.

14. The external position also strengthened in 2013 on account of the substantial increase in iron ore exports and the moderation of mining related imports of machinery and transport equipment. The current account deficit, including official grants, improved from 45 percent of GDP in 2011 to 12.4 percent of GDP in 2013. Gross foreign reserves increased from US$382 million in 2010 (2.4 months of import cover) to US$473 million (3.4 months of import cover) in 2013. The exchange rate remained relatively stable.

15. Total public debt at end 2013 is estimated at US$ 1.49 billion equivalent. External debt which accounted for 70 percent of this figure is estimated at US$ 1.04 billion as at end 2013. Domestic debt amounted to Le1.97 trillion as at end 2013. The debt situation remained sustainable with moderate risk of debt distress.

Annex 2: Letter of Development Policy

Economic Performance, January – June 2014

16. Economic activities remained buoyant in the first half of 2014 with increased activities in agriculture, mining, construction, tourism and the other service sectors. The level of output in the various sectors during the period indicated that the economy was on track to achieve the projected growth rate of 11.3 percent for 2014.

17. Inflation continued the downward trend reaching almost a five year low of 6.4 percent in April 2014. The drop in inflation followed hawkish monetary policy, a stable exchange rate with domestic food supplies uninterrupted and world food prices continued to decline.

18. The expansion in exports combined with the moderation in imports resulted in an improvement in the trade balance. It recorded a surplus of US$97.7 million in the first half of the year compared to a deficit of US$143 million for the corresponding period in 2013. Gross foreign exchange reserves increased to US499.3 million at end June 2014 from US$434.6 million in June 2013.

19. Fiscal performance was weaker than expected during the first half of 2014. Domestic revenue collected was Le73.1 billion lower than projected as all the revenue categories recorded shortfalls. Recurrent and domestic funded capital expenditures were higher than budgeted. The higher than programmed budget deficit was financed mostly by borrowing from the domestic banking sector as the non-bank sector disinvested its holdings of Government bonds. Domestic interest rates continued to decline with the 91 day Treasury bill rate falling to 1.66 percent as at end June 2014.

Economic and Fiscal Impact of the Spread of the Ebola Virus Disease in 2014

Economic Impact

20. The unprecedented outbreak of the Ebola virus disease in May 2014 and its rapid spread to all 13 districts with higher infection rates since July has created a devastating humanitarian and social crisis with severe negative impact on economic activities in the second half of the year.

21. The outbreak of the Ebola virus disease and measures adopted to contain the spread of the disease is disrupting activities in the key sectors of the economy including agriculture, mining, manufacturing, construction, transportation, domestic and international trade and tourism. Preliminary estimates by Government and the International Monetary Fund indicate that economic growth will slow down to 4.0

percent in 2014 compared to the projected growth rate of 11.3 percent due to disruptions and reduced activity in these key sectors.

22. The closure of periodic markets and national borders, internal travel restrictions has led to disruptions in the supply of food and other basic necessities. These factors, combined with the depreciation of the exchange rate heightened by the Ebola virus disease, resulted in the spikes in the prices of basic goods. Inflation, which had fallen to 6.4 percent at end-April 2014 rose to 7.5 percent in September 2014. Accordingly, the end-December target for inflation has been revised from 7.5 percent to 10 percent.

23. Even though complete trade data is not yet available for the second half of 2014, anecdotal evidence indicate that exports will fall in line with the reduced domestic production while imports will increase to cover additional needs for medical and emergency food supplies, fuel, and capital equipment for new health centers. Consequently, the current account deficit is expected to be larger than earlier projected in 2014. The IMF projects that the overall balance of payments (BOP) will shift from a surplus of US$38 million to a deficit of US$216 million with a financing gap of US$110 million. The official exchange rate depreciated by 9.2 percent between end May and end October due to excess demand pressures for foreign exchange.

Fiscal Impact

24. Domestic revenue collection is being adversely affected by reduced economic activity, lower mining revenue, and weaker taxpayer compliance. Ebola virus disease-related revenue shortfall is estimated at US$90 million or 1.6 percent of non-iron ore GDP in 2014 and US$215 million (3.6 percent of GDP) in 2015.

25. At the same time, the epidemic has engendered tremendous expenditure pressures. The revised estimates by Government and the IMF indicate that total expenditure will increase by US$41 million in 2014, of which US$38 million are due to the Ebola virus disease. Thus, the total impact of the epidemic on the Government budget is about US$130 million (2.4 percent of GDP) in 2014. The revenue loss combined with the additional expenditures resulted in the widening of the financing gap to US$128 million. Higher domestic borrowing, and a scale back of capital spending, combined with additional budget support provided by the African Development Bank and the World Bank, the augmentation of access to IMF resources under the existing Extended Credit Facility, covered the gap by a total of almost US$100 million. The uncovered financing gap remains at US$28 million.

Annex 2: Letter of Development Policy

Medium Term Impact and Economic Outlook

26. The medium-term outlook of the economy is yet uncertain. Lower economic growth, low revenue collection and expected higher spending may pose serious risks on the economic and fiscal outlook in the foreseeable future. The full impact of the disease on the economy will only be assessed following its containment.

27. The medium-term outlook of the economy is therefore anchored on two possible scenarios: low (optimistic) Ebola virus disease scenario and high (pessimistic) Ebola virus disease scenario. The low Ebola virus disease scenario is based on the assumption that the Ebola virus disease outbreak will be contained by early 2015. Under this scenario, economic activities will rebound led by agriculture, manufacturing, tourism and construction. This will result in overall GDP growth of 2.5 percent in 2015 compared to the 8.9 percent originally projected. Non-iron-ore GDP growth will be 4.5 percent compared to the initial projection 6.3 percent.

28. Thus, lower than anticipated economic growth will have a dramatic effect on Government revenue. Domestic revenue is projected to drop to 11.7 percent of GDP. Expenditure pressures are likely to continue in 2015, particularly for higher social spending and cost of incentives for health workers and farmers. The estimated total impact of the Ebola virus disease for 2015 is estimated at US$224 million (3.8 percent of non-iron ore GDP) comprising 3.6 percent of revenue loss and 0.2 percent of additional expenditure. The uncovered financing gap for 2015 is estimated at US$72 million.

29. Inflation is projected to increase to 12 percent at end 2015 compared to an earlier projection of 6 percent. The current account deficit is projected to widen to 15.7 percent of GDP in 2015

30. A more pessimistic slow Ebola virus disease containment scenario (high Ebola) is also envisaged, with the assumption that efforts to end the crisis will not bear fruit until around the third quarter of 2015. In this scenario, agricultural output falls dramatically due to large scale abandonment of farms by farmers and the services sector, especially the hospitality sector.. Only government spending buoys the economy. As a consequence, overall GDP will contract by 2.0 percent in 2015 while the non-iron ore economy shrinks by 3.2 percent. The lower growth projection implies lower domestic revenues as Income Tax and Good and Services Tax collections decline significantly and the domestic revenue to GDP ratio drops significantly to 10.6 percent. Ebola virus disease related expenditures will be higher than under the low scenario, resulting in a higher budget deficit.

31. Inflation will remain elevated under this scenario reaching 14 percent at the end of 2015. Exports will contract by 7 percent as imports increase by 1.3 percent.

32. In both scenarios, gross foreign exchange reserves will remain above 3 months of import cover in 2015 on account of the projected increase in Ebola virus disease related foreign inflows and inflation will return to single digit in 2016. External public debt will be stable at between 25 percent and 27 percent during 2015 and 2016 as Government remains committed to prioritize highly concessional loans and grants.

Structural Reforms

Public Financial Management Reforms

33. With support from development partners, Government carried out a number of Public Financial Management (PFM) reforms at both the central and local levels. These contributed to improving public budgeting and expenditure management, public procurement, public sector accounting and reporting, internal auditing and external oversight of public finances in recent years. Despite these improvements, challenges remain in some specific PFM areas.

34. To address these, Government developed a medium-term PFM Reform Strategy for the period 2014-2017 that seeks to consolidate and improve on the reforms achieved under the Integrated Public Financial Management Reform Project. To this end, Government remains committed to improving fiscal discipline, strengthening budget credibility and ensuring value for money as agreed under the Multi-Donor Budget Support Performance Assessment Framework (MDBS-PAF) supported under the new Public Financial Management Improvement and Consolidation Project funded jointly by the Multi-Donor Budget Support Partners.

35. Government will complete the regulations for effective implementation of the new Public Financial Management Bill, soon to be submitted to Parliament. The new PFM Bill presents clear and comprehensive definitions of Government entities; introduces fiscal responsibility principles; improves macro-fiscal planning; and management of fiscal risks; strengthens budget discipline to enhance budget credibility; improves cash management; and strengthens accounting, reporting and auditing.

36. Progress in the establishment of the Treasury Single Account (TSA) is also far advanced. The TSA was scheduled to be completed in September this year but technical assistance support was delayed because of the Ebola virus disease outbreak. Meanwhile, a Loans and Fiscal Agency Agreement between the Ministry of Finance and Economic Development and the Bank of Sierra Leone has been agreed that defines the roles and responsibilities of stakeholders with regard to the implementation of the TSA.

Public Sector Reforms

37. Government is also implementing public sector reforms under the World Bank funded Pay and Performance project. This includes public sector pay reform; right-sizing the civil service with a focus on the recruitment of technical personnel to fill the 'missing middle' as well as the integration of performance management.

Financial Sector Reforms

38. The Bank of Sierra Leone (BSL) has prepared a roadmap for developing and implementing risk-based supervision to support financial sector stability. The Bank also prepared a Primary Dealer agreement to facilitate the development of the interbank foreign exchange market. The BSL is moving towards a wholesale Foreign Exchange Auction with Technical Assistance from the IMF.

39. Going forward, the BSL will prepare an internal Contingent Manual to guide identification and supervisory actions in the event of specific or systemic bank distress. The BSL will also draw up a detailed risk-based supervisory framework for on-sight supervision of the largest banks in the country. Furthermore, the BSL will develop and issue to commercial banks, Internal Risks Management guidelines to forestall credit, market, and technology risks.

THE EMERGENCY ECONOMIC AND FISCAL SUPPORT OPERATION

40. Mr. President, the main objective of the operation is to ensure Government's Ebola Response Plan is executed through adequate budgeting and transparent use of resources, consistent with strengthening longer-term fiscal management and transparency. The operation is, therefore, organized around two broad pillars that contribute directly to supporting and strengthening Government's management of public resources in response to the social and economic crisis created by the Ebola virus disease epidemic. The first pillar aims to strengthen budget management and reduce fiscal risks heightened by Ebola. The second pillar is concerned with actions to improve transparency and accountability in the use of public resources.

(i) Strengthen Budget Management and Reduce Fiscal Risks Heightened by Ebola

41. As part of efforts to contain the rapid spread of the Ebola virus disease, Government recruited health and non-health workers to assist in contact tracing, providing care and support to Ebola virus disease victims and burying the dead. Given the risks faced by these personnel, incentive in the form of hazard pay is being provided by Government with financial support from the African Development Bank and the World Bank. This is important to encourage these staff to continue providing medical care and support to Ebola virus disease victims.

42. To ensure transparency and accountability in the payment of these incentives the Ministry of Finance and Economic Development (MOFED) established a system to ensure that all eligible clinical and non-clinical staff receive hazard pay through a formal payments system, including bank accounts or use of a mobile payment system. As a first step in formalizing the hazard payment system, the Ministry of Finance and Economic Development agreed to produce a validated list of eligible beneficiaries.

43. To this end, the Internal Audit Department recently conducted a nationwide verification of eligible health and non health workers receiving the health hazard incentive. The names, designation, Pin Code / Reference number, banker, bank account number and mobile phone number were captured. The audit team compiled the list of all eligible clinical and non-clinical personnel that are actually entitled to receive the hazard pay at district level.

44. In the meantime, a team comprising staff of the Audit Service Sierra Leone (ASSL), the National Emergency Response Centre (NERC), the Police and some members of the Republic of Sierra Leone Armed Forces was established to pay hazard incentives to the eligible clinical and non-clinical personnel using the validated list provided by the Internal Audit Department of MOFED for two weeks. Staffs of the Internal Audit Department of MOFED were involved in this exercise. During the exercise, the Internal Audit validated the data of eligible clinical and non-clinical personnel who were initially verified and verified new payees.

45. In tandem with efforts to formalize all payments through a verifiable electronic payment system, a validation system is being established to provide comfort about the use of public funds. In this regard, Government has awarded a contract to BDO Private Sector Services, formerly PKF, on 18th November to provide fiduciary agency services to ensure that only eligible clinical and non-clinical personnel receive the hazard payments. The contract was initially awarded, to Price Waterhouse Coopers (Ghana) Limited but was nullified due to failure on the part of the firm to sign a contract. BDO has a physical presence at NERC and started providing fiduciary services on Monday 21st November 2014.

46. The multiplicity of Government accounts with idle cash balances in commercial banks outside the control of the office of Accountant General is posing significant challenges to cash management and budget execution. To address this, a Treasury Single Account (TSA) will be established that links all Government bank accounts to improve budget control, execution and accountability while enhancing the predictability of resource flows to service delivery agencies. This is expected to reduce domestic borrowing costs and the accumulation of payments arrears.

47. Progress in the implementation of the TSA is far advanced with technical assistance provided by the Commonwealth Secretariat. The TSA was scheduled to be completed in September 2014 but technical assistance related to the installation of the technical infrastructure as well as training of staff was delayed because of the Ebola virus disease outbreak in the country including restrictions in travel. In the meantime, the Ministry of Finance and Economic Development and the Bank of Sierra Leone have signed a Loans and Fiscal Agency Agreement that defines the roles and responsibilities of stakeholders with respect to the implementation of the TSA.

48. The two large state commercial banks (accounting for 30 percent of private sector system lending) are a significant source of fiscal risk to Government. A combination of poor corporate governance, weak management and, reckless lending practices resulted in high levels of non-performing loans in these banks. As part of remedial measures, Government replaced the Managing Directors of the two institutions.

49. The application of strict prudential regulations to the commercial banking sector warranted huge provisioning for bad loans, which in turn eroded the capital of these banks. The banks cannot meet the minimum paid up capital requirement of the Bank of Sierra Leone.

50. In order to better identify and manage the associated fiscal risks, the banks have provided through the National Commission for Privatisation their respective 2013 audited financial statements. This will allow for an assessment of the contingent risk posed by these entities to be made and to plan accordingly.

(ii) Improve Transparency and Accountability for Public Resources

51. A key challenge to budget execution in recent years that contributes to undermining budget credibility is the high level of extra-budgetary expenditures. This often results in overspending above the budgeted limits in a given year. Nonetheless, both the Constitution and the Government Budgeting and Accountability Act (GBAA), 2005 require that Parliament sanction higher than budgeted expenditures through a supplemental appropriation bill.

52. Following six months of implementation of the 2014 budget, the underlying assumptions on which domestic revenue projections were based were no longer valid, including recent falls in the international price of rutile and bauxite. Furthermore, several compelling expenditure requirements emerged during the course of the year, including resources to fight the Ebola virus disease not foreseen during the preparation of the 2014 budget. In view of the foregoing and consistent with the requirements under the Constitution and GBAA, 2005, Government submitted a Supplementary Appropriation

Bill to Parliament for 2014 on July 10, 2014. This was subsequently ratified by the House.

53. In accordance with Section 159 of the Mines and Minerals Act, 2009, and consistent with Government commitments under the Extractive Industries Transparency Initiative, Government remains committed to enhancing transparency and accountability in the extractive sector.

54. In this regard, Government has published all the six (6) signed Mining Lease Agreements on the website of the Ministry of Finance and Economic Development. Furthermore, Government has published on the MOFED website a statement of revenue collected in fiscal year 2013 from the ten largest mining companies covering at least 90 percent of the total collection by revenue type.

CONCLUSION

55. Mr. President, the Ebola virus disease crisis has exposed the country's vulnerability to external shocks and exacerbated the country's fragility. The negative impact, in terms of slowing economic growth, lower domestic revenues and higher spending, poses serious risks on the economic and fiscal outlook of the country.

56. In the absence of external budget support, the Government will have to significantly reduce much needed capital spending in order to mitigate part of the shortfall and or excessively borrow from the domestic economy with attendant consequences on macroeconomic stability and economic growth.

57. Your approval of this disbursement request, therefore, will enable Government to address the emerging challenges and mitigate the negative impact of the Ebola virus disease on the population of Sierra Leone.

Yours Sincerely,

Kaifala Marah (Dr.)
Minister of Finance and Economic Development

Annex 3: Fund Relations Note

IMF Executive Board Approves US$130 Million in Immediate Assistance to Guinea, Liberia, and Sierra Leone in Response to the Ebola Outbreak

Press Release No. 14/441
September 26, 2014

The Executive Board of the International Monetary Fund (IMF) today approved—in an expedited decision supported by a joint statement of all Directors—emergency financial assistance to Guinea, Liberia, and Sierra Leone totaling US$130 million to help respond to the Ebola outbreak. The IMF financing will be made available to the three countries immediately, in the amounts of US$41 million for Guinea, US$49 million for Liberia and US$40 million for Sierra Leone. This emergency financing comes in addition to the assistance provided under existing programs for these countries. It will help cover part of the immediate balance of payments and fiscal needs currently estimated at about US$100 million for each country.

"The Ebola outbreak in Guinea, Liberia, and Sierra Leone has already cost too many lives," said IMF Managing Director Christine Lagarde. "This humanitarian crisis could also have deep economic consequences. The governments of Guinea, Liberia and Sierra Leone requested IMF support to enhance their efforts to contain this unprecedented epidemic that is disproportionately affecting the most vulnerable in their populations. The IMF is working hard with the authorities of the affected countries and their development partners to ensure that the outbreak is quickly brought under control and to assist the economic rebuilding effort that must follow."

The Ebola Outbreak affecting the three countries has created a significant social and humanitarian crisis, and has so far proven difficult to contain despite efforts by the respective governments and their development partners. It is also having an acute macroeconomic and social impact on the three already-fragile countries. The crisis is still unfolding, but preliminary IMF estimates indicate that growth could decline by at least 3-3½ percent in Liberia and Sierra Leone and by about 1½ percent in Guinea in 2014. Inflationary pressures have flared up in the affected countries, and significant fiscal financing needs have emerged as the outbreak has caused sharp declines in tax revenues and Ebola-related spending had to be increased substantially. Additional and sizeable budget support from bilateral and multilateral development partners is urgently needed to avoid painful domestic adjustment measures and help eradicate the disease.

The Executive Board of the IMF today approved an augmentation of access of 25 percent of quota under the current Extended Credit Facility[1] (ECF) arrangements for Liberia and for Sierra Leone, resulting in an increase of almost 50 percent in financing under their existing arrangements; and a 25 percent of quota financing under the Rapid Credit Facility[2] (RCF) arrangement for Guinea.

Following the Executive Board's discussion, Ms. Christine Lagarde, Managing Director and Chair, made the following statement:

"The Ebola outbreak is taking a very high human toll in Guinea, Liberia, and Sierra Leone. Unless brought under control, the epidemic will reverse the advances that these countries have made in recent years under Fund-supported programs toward mending their still fragile economies. Large-scale and well-coordinated assistance by the international community is urgently needed to support the national authorities' efforts to contain the devastating impact of the disease. Against this background, the Fund's Executive Board strongly and expeditiously supported the authorities' request for financial assistance.

"The outbreak is affecting Guinea, Liberia, and Sierra Leone in different ways, but in all cases it is expected to reduce economic growth significantly and fuel inflationary pressures. The poorest and most vulnerable segments of the population are being disproportionately affected by disruptions in commerce and the higher prices of food and basic commodities. Fiscal deficits are projected to widen due to lower revenues as economic activity slows as well as higher additional outlays on emergency programs. Current account balances are also projected to worsen owing to the decline in exports and the increase in food and other critical imports. Preliminary staff estimates put the combined financing gap at about US$300 million, provided that contagion is stopped early next year.

"The Fund resources made available today will cover almost half of this financing need. Additional balance of payments and budget support from multilateral and bilateral donors is needed to avoid painful adjustment measures and safeguard macroeconomic stability. The rapidly deteriorating health situation underscores the urgency of this support.

"The Fund is closely monitoring the situation and stands ready to provide further assistance through this challenging period."

Background:

Liberia: The ECF arrangement for Liberia of about US$79.9 million was approved by the IMF's Executive Board on November 19, 2012 (see Press Release No. 12/449). The additional and immediate financing of US$49 million increases the funds available under the ECF to US$130 million.

Sierra Leone: The ECF arrangement for Sierra Leone of about US$ 95.84 million was approved by the IMF Executive Board on October 21, 2013 (see Press Release No. 13/410). The additional and immediate financing of US$40 million brings the funds available under the ECF to US$136 million.

Guinea: The ECF arrangement for Guinea of about US$198.9 million was approved by the IMF's Executive Board on February 24, 2012 (see Press Release No. 12/57). Guinea is making satisfactory progress under this existing ECF arrangement, but will receive emergency funding of US$41 million under the RCF due to a pending ECF review.

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[1] The ECF is a lending arrangement that provides sustained program engagement over the medium to long term in case of protracted balance of payments problems.

[2] The RCF is a lending arrangement that provides rapid financial support in a single, up-front payout for low-income countries facing urgent financing needs.

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