Document of
The World Bank

FOR OFFICIAL USE ONLY

Report No. 100436-MG

INTERNATIONAL DEVELOPMENT ASSOCIATION

PROGRAM DOCUMENT

FOR A PROPOSED CREDIT

IN THE AMOUNT OF SDR 39.4 MILLION (US$55.0 MILLION EQUIVALENT)

TO THE REPUBLIC OF MADAGASCAR

FOR A

RESILIENCE DEVELOPMENT POLICY OPERATION

November 11, 2015

Macroeconomics and Fiscal Management Global Practice
Africa Region

THE REPUBLIC OF MADAGASCAR

GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENT

(Exchange Rate Effective as of October 30, 2015)
Currency Unit = Ariary
US$1 = Ariary 3292
US$1 = SDR 0.71588623

ABBREVIATIONS AND ACRONYMS

AfDB	African Development Bank
AGOA	African Growth and Opportunities Act
BCM	Central Bank of Madagascar
BIANCO	Independent Anti-Corruption Bureau
BOP	Balance Of Payments
CPIA	Country Policies and Institutional Assessment
CPF	Country Partnership Framework
DeMPA	Debt Management Performance Assessment
DTIS	Diagnostic Trade Integration Study
DPO	Development Policy Operation
ENSOMD	Millennium Development Goal Surveys
EPM	Household Survey
EPZ	Export Processing Zone
FDI	Foreign Direct Investment
FSAP	Financial Sector Assessment Program
FY	Fiscal Year
GDP	Gross Domestic Product
GRS	Grievance Redress Service
IDA	International Development Association
IEG	Independent Evaluation Group
IFC	International Finance Corporation
IMF	International Monetary Fund
INSTAT	National Institute of Statistics
JIRAMA	State-Owned Electricity and Water Company (Jiro sy Rano Malagasy)
LDP	Letter of Development Policy
LMIL	Large Mining Investments Law
MFB	Ministry of Finance and Budget
MCS	Ministry of Civil Service, Work and Social Laws
NDP	National Development Plan
OGT	*Opération Globale du Trésor* (Monthly Treasury Operations report)
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
PGDI	*Projet de Gouvernance et de Développement Institutionnel*
PPP	Purchasing Power Parity
RCF	Rapid Credit Facility
SADC	Southern African Development Community
SCD	Systematic Country Diagnostic
SDR	Special Drawing Rights

SOE	State-Owned Enterprise
SORT	Systematic Operations Risk-rating Tool
SSA	Sub-Sahara Africa
US$	United States Dollar
VAT	Value Added Tax
WDI	World Development Indicator

Regional Vice President :	Makhtar Diop
Country Director :	Mark Lundell
Global Practice Director :	John Panzer
Practice Manager :	Mark Thomas
Task Team Leader :	Keiko Kubota

THE REPUBLIC OF MADAGASCAR

RESILIENCE DEVELOPMENT POLICY OPERATION

TABLE OF CONTENTS

TABLES

FIGURES

The proposed Resilience Development Policy Operation was prepared by an IDA team consisting of: Keiko Kubota (Lead Economist, Task Team Leader, GMFDR), Faniry Razafimanantsoa and Quentin Gouzien (Economists, GMFDR), Theresa Osborne (Senior Economist, GPVDR), Anne-Lucie Lefebvre and Hajarivony Andriamarofara (Senior Public Sector Specialist, GGODR), Hugues Agossou (Senior Financial Management Specialist, GGODR); Vonjy Miarintsoa Rakotondramanana (Senior Energy Specialist, GEEDR), Eneida Fernandez (Senior Private Sector Development Specialist, GTCDR); Noroarisoa Rabefaniraka (Senior Transport Specialist, GTIDR); Nathalie Munzberg (Senior Counsel, LEGEN), Enagnon Ernest Eric Adda (Senior Financial Management Specialist, GGODR), Aissatou Diallo (Senior Finance Officer, CTRLA), Rondro Rajaobelison (Program Assistant, AFMMG) and Madeleine Chungkong (Senior Program Assistant, GMFDR). Finally, the team benefited of the guidance of Mark Lundell (Country Director, AFCS2), Mark Thomas (Practice Manager, GMFDR), Julio Revilla (Program Leader, GMFDR), and Coralie Gevers (Country Manager, AFMMG). Valuable peer reviewing comments and suggestions were provided by Nancy Benjamin and Enrique Blanco Armas (both GMFDR).

SUMMARY OF PROPOSED CREDIT AND PROGRAM

THE REPUBLIC OF MADAGASCAR

RESILIENCE DEVELOPMENT POLICY OPERATION

Borrower	Republic of Madagascar
Implementation Agency	Ministry of Finance and Budget
Financing Data	Standard IDA credit: SDR 39.4 million (US$55.0 million equivalent). Maturity: 38 years; grace period: 6 years.
Operation Type	Stand alone, single tranche
Pillars of the Operation And Program Development Objective(s)	The proposed operation has a single pillar with the development objective of (i) strengthening reporting and increasing availability of information relevant to assessing the effectiveness of public finance, and (ii) improving payroll management and consolidating accounts in line with the treasury single account principle.
Result Indicators: (Baseline: 2014 unless otherwise noted; Target 2017)	1.i. The number of civil servants with date of birth information not on record at the MFB (Baseline: 30,000. Target: 0); ii. the civil service rosters at MFB and MCS are reconciled every 6 months, (Baseline: not done. Target: within the last 6 months). iii. amount of position-specific benefits paid to those who had already left the "high officer" positions. (Baseline: 3.56 bn Ariary (2015). Target: 0). 2.i Liter of diesel per kwh of thermic generation of electricity by JIRAMA (including the private centers for which JIRAMA is responsible for the fuel supply) (Baseline: 0.16 l/kwh. Target: 0.14 l/kwh). ii. data on diesel consumption and electricity generation publicly available. (Baseline: not available. Target: updated monthly). 3. The audited accounts of Air Madagascar are published within the time allotted by regulations. (Baseline: overdue. Target: Publication is on time). 4. List of enterprises which receive tax expenditures through LMIL, EPZ Law and by Council of Ministers decisions publicly available. (Baseline: not available; Target: annually updated lists are publicly available). 5. The share of dedicated accounts for externally-financed projects held at the Central Bank. (Baseline: 0%; Target: 90%). 6. Length of time needed to submit the audited consolidated final accounts of the State Budget. (Baseline: over 5 years; Target: within 24 months of end year). 7. Timeliness of the publication of the monthly budget execution report by the Treasury (OGT). (Baseline: not publicly available; Target: within 6 weeks of end month).
Overall risk rating	Substantial
Climate and disaster risks *(required for IDA countries)*	Are there short and long term climate and disaster risks relevant to the operation (as identified as part of the SORT environmental and social risk rating)? Yes ☐ No ☒
Operation ID	P153084

IDA PROGRAM DOCUMENT FOR A PROPOSED CREDIT TO THE REPUBLIC OF MADAGASCAR

1. INTRODUCTION AND COUNTRY CONTEXT

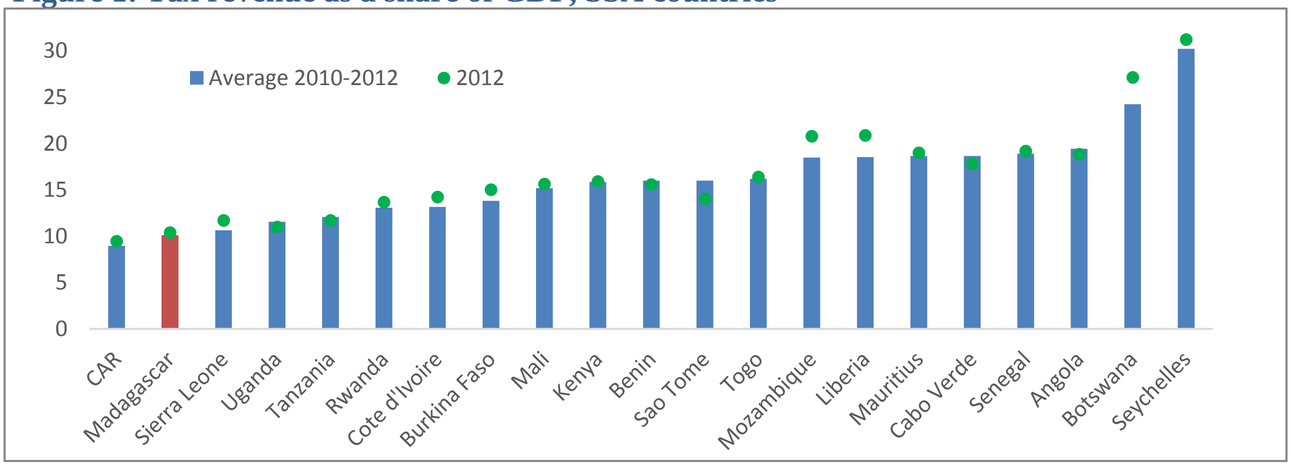
1. **This program document proposes a Resilience Development Policy Operation for the Republic of Madagascar** for the amount of SDR 39.4 million (US$55.0 million equivalent). The Program is the second stand-alone single tranche operation to be presented to the Board of Executive Directors, following the Reengagement DPO approved by the Board on December 18, 2014 after the end of the applicability of OP 7.30 to Madagascar in 2014. It aims to contribute to three of the four areas of reform that the Systematic Country Diagnostic (SCD) identified as potentially having a large impact on poverty in the short to medium term. The reform areas are fully aligned with the Government's efforts to improve budget efficiency and support economic growth by unlocking energy and transport constraints. Those reform efforts are still in their initial stages and have produced few results so far, but will be further advanced by investment projects that are expected to be presented to the Board in late FY16 Q3. For this reason, and because the political stability is still fragile, a second stand-alone single tranche operation, rather than a programmatic series, was prepared with the aim of providing support to the country's resilience as it seeks to consolidate the return to constitutional order.

2. **The political context in Madagascar remains challenging, delaying urgently needed reforms**. Madagascar returned to constitutional order when a duly-elected government took office in 2014, after a five-year long political crisis. The crisis had devastating effects on the economy, poverty and social outcomes. The return to constitutionality was an event welcomed by all, but only the first step towards putting the country back on track for sustainable development. Tangible progress has been made since: a new National Development Plan (NDP) and its implementation strategy were elaborated; efforts are being made to reorient public expenditure towards social spending and public investments in the last two State Budgets adopted by the Parliament (supplemental State Budget for 2014 and State Budget 2015); the constitutionally-mandated local elections were held peacefully in July 2015. The country has, however, encountered difficulties in moving ahead in unison to implement the new development strategy. The executive, legislative and judiciary branches have yet to settle on constructive working arrangements. Intra elite power struggles, which have always been a feature of Malagasy politics, have not abated, distracting the attention and energy of the political leaders, and threatening at times to derail the fragile recovery process. Consequently, most of the urgent reforms have yet to be implemented fully. The speed of the turnaround, while slow, is perhaps to be expected, as the last crisis was particularly long and traumatic, even for a country prone to political instability.

3. **Many of the urgent reforms relate to fiscal policies, on both revenue and expenditure fronts, as a prerequisite for financing public investments and social spending necessary for fighting poverty and pursuing sustainable development**. Madagascar's tax as a share of GDP has historically been among the lowest in the world (Figure 1, for 2010-2012 comparison), and is still hovering below 10 percent in 2015 (see Table 3). This level of revenue is barely enough to fund non-discretionary spending, with very little left for functioning of the State and making necessary investments to achieve development outcomes. The recently completed SCD for Madagascar (2015) has identified increasing fiscal space as the urgent priority among other

pressing reforms. Accordingly, strategies for increasing tax revenue have been drawn up, and efforts are under way, but they have yet to produce concrete results. The government still allocates a significant share of the discretionary spending to unaffordable and poorly-targeted fuel subsidies and transfers to finance the losses of the two troubled state-owned companies, the public utility company (JIRAMA) and Air Madagascar. The limited fiscal space and legacy distortions from the transition period are limiting the administration's margin of maneuver.

Figure 1: Tax revenue as a share of GDP, SSA countries



Source: WDI
Note: 2012 is the last year where comparable data are available

4. **A vast majority of the Malagasy population is poor, and extremely so**. Extreme poverty (per capita consumption under US$1.9 purchasing power parity 2011 – PPP – per day) has increased from 68.7 percent in 2001 to 82.0 percent of the population in 2012 (the latest data available). Over the same timeframe, absolute poverty (US$3.1 PPP per capita per day) rose from an estimated 84.1 in 2001 to 93.0 percent of the population in 2012.

Table 1: World Bank Revised Headcount Poverty Estimates

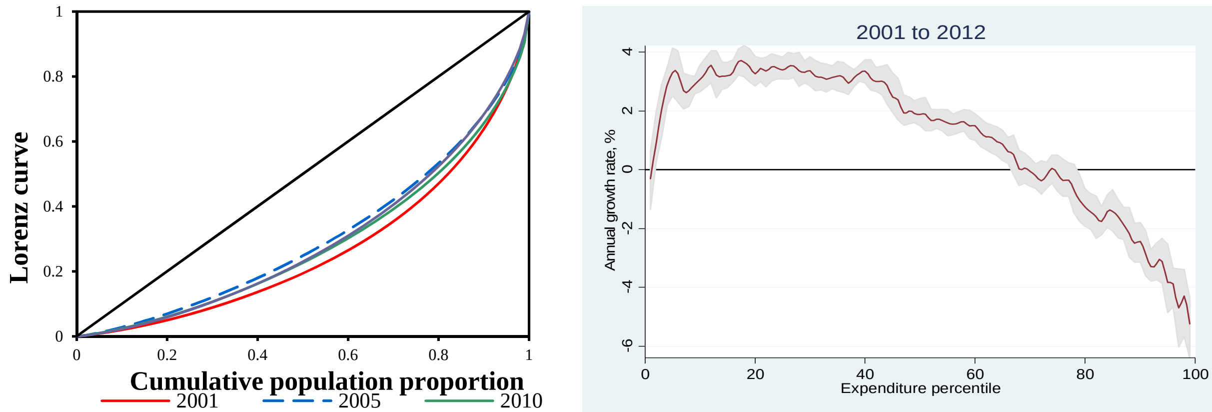
Year	2001	2005	2010	2012
National re-estimated poverty line				
Extreme poverty	60.5	59.8	58.3	58.2
Absolute poverty	70.8	73.2	71.7	70.7
Of which Urban	34.1	40.8	29.8	35.5
Rural	77.7	79.6	80.1	77.9
International poverty line				
Poverty rate at $1.9 PPP	68.7	74.1	81.8	82.0
Poverty rate at $3.1 PPP	84.1	89.9	92.9	93.0

Source: INSTAT, EPM 2001-2010 and ENSOMD 2012 and staff estimates

5. **Inequality in Madagascar is similar to that of other low-income countries, but it diminished strongly between 2001 and 2012**. The Gini coefficient was 0.41 in 2012, similar to the low income average of 0.40 (Source: WDI). The poverty gap, hovering around 40-45 range, is also similar to the low income average, and its evolution mirrors the consumption growth pattern

per period. Madagascar's inequality, however, is not due to a steep welfare increase at the top, but rather to relatively higher inequality among the bottom 90 percent than in other poor countries – that is, different levels of deprivation. Based on an analysis of the incidence of growth, inequality has declined from 2001 to 2012, but only because it declined dramatically in the first half of 2000s when consumption growth accrued disproportionately to the poor (Figure 2). Nonetheless, because growth was negative for households living near the poverty line, and growth did not lift those at the bottom out of poverty, the overall progressive pattern was accompanied by an increase in the headcount poverty rate. Since that time, however, the pattern of growth has been regressive.

Figure 2: Gini coefficient (left) and consumption growth by expenditure percentile (right)



Source: INSTAT, EPM 2001-2010 and ENSOMD 2012

6. **The program development objective of the proposed operation is (i) strengthening reporting and increasing availability of information relevant to assessing the effectiveness of public finance, and (ii) improving payroll management and consolidating accounts in line with the treasury single account principle**. The program seeks to improve the efficiency and effectiveness of public finance primarily through disclosure of relevant information. Such disclosure is important for transparency, enhances accountability, and in the long run, contributes to increasing fiscal space. The proposed program also supports reducing inefficient expenditure. The policy reforms supported by the proposed operation are aimed at enhancing resilience of the country by putting in building blocks to encourage participation of relevant actors and the public at large in informed policy discussions. They are steps towards achieving the longer term goals, and the risk that they may not be followed through exists. On the other hand, the World Bank can strengthen the momentum for the reforms and improve the chances of their success. Not accompanying the reformers who have run into resistance risks letting the non-reformers prevail and possibly tipping the balance for the country to slip back into instability.

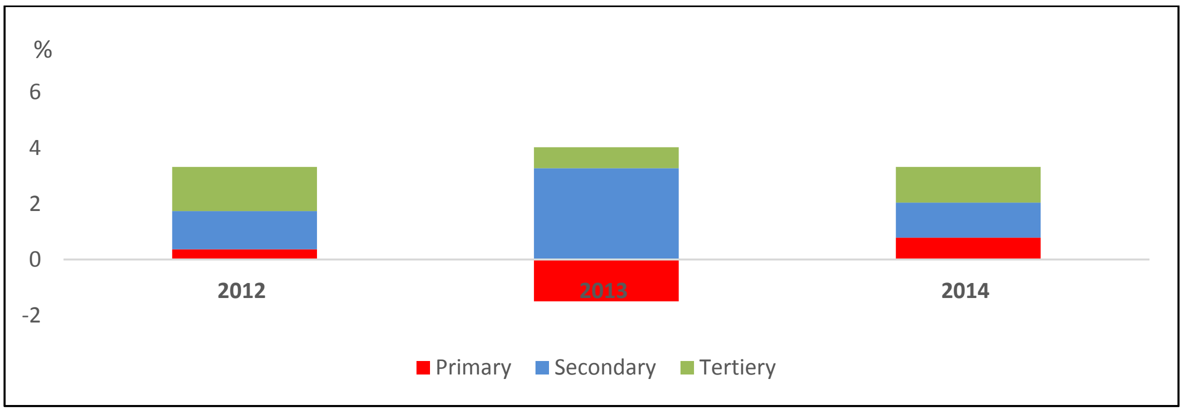
2. MACROECONOMIC POLICY FRAMEWORK

2.1 RECENT ECONOMIC DEVELOPMENTS

Real sector developments

7. **Economic performance improved in 2014 as the economy started to exit the holding pattern that prevailed during the political crisis**. Growth increased to 3.3 percent, up from 2.3 percent in 2013, turning per capita growth positive. The mining sector was the principal engine, recording 26 percent growth as the main nickel processing plant entered its second full year of operation. The volume of nickel exports was 38 percent higher in 2014 than in 2013. The tertiary sector grew by 2.1 percent in 2014 after stagnating in 2013, bolstered by higher public investments and the recovering tourism sector. The primary sector recovered from a disastrous year in 2013 and turned in positive growth in 2014, although its rate and contribution to total growth are lower than other sectors (Figure 3).

Figure 3. Contribution to growth by sectors



Source: INSTAT

8. **Difficult local and international conditions prevented further acceleration of growth in 2015**. The cyclones and droughts at the beginning of the year damaged agricultural crops and infrastructure, causing an estimated loss of around 1.2 percent of GDP. In addition to diminished harvest prospects, the damages fueled inflation, which peaked at 7.9 percent at end-March 2015 (year-on-year), its highest level since October 2011, before decelerating to 7.5 percent in July 2015 with the arrival of the rice harvest period. The lower import price of fuel has not translated into reduced inflation, as pump prices continue to be regulated. The depreciation of Ariary, the local currency, against the US dollar also offset the gains from the declining international prices. On the other hand, the weak commodity prices decreased the country's export earnings: mining products have represented over a third of the total exports in recent quarters.

9. **JIRAMA and Air Madagascar, the two troubled state-owned enterprises, have been experiencing a particularly difficult year in 2015**. Long strikes at Air Madagascar, the national carrier who has a *de facto* monopoly in the domestic market, disrupted the air traffic and hurt sectors that depend on it. Tourism operators suffered cancellation rates of up to 60 percent, and possible loss of markets in the future as well. Air Madagascar is estimated to have lost more than

US$15 million during the strike, making it certain to end another year with operating losses. The company received several million US dollars' worth of cash infusion from the government in 2012, 2014 and 2015. Employees of JIRAMA also staged a long strike this year, while power cuts intensified. The State transfers to JIRAMA are rising, as the company resorts increasingly to expensive diesel-based emergency power generation that it can ill afford. Both companies are developing plans to revamp the business strategy and corporate governance with the assistance from the World Bank.

Table 2: Madagascar: Selected Economic and Financial Indicators

	2013	2014 Est.	2015 Proj.	2016 Proj.	2017 Proj.
Real sector	(annual change, %, except noted otherwise)				
Real GDP growth	2.3	3.3	3.2	3.4	3.6
GDP per capita growth	-0.6	0.5	0.4	0.6	0.8
Consumption (% GDP)	94.6	94.0	93.8	93.3	93.0
Investment (% GDP)	15.7	15.5	15.6	15.6	17.2
Net exports (% GDP)	-10.3	-9.6	-9.5	-8.9	-10.2
Inflation, consumer prices (annual %, end of year)	6.3	6.0	7.9	7.2	7.0
Public Finance	(in percent of GDP)				
Revenues, excluding Grants	9.6	10.1	10.4	10.7	11.3
of which: Tax Revenues	9.3	9.9	9.9	10.4	10.9
Grants	1.3	2.3	1.9	2.0	1.8
Total spending (commitment basis)	14.9	14.7	16.4	15.7	17.2
of which: Capital spending	3.1	3.9	4.5	4.6	6.2
Overall balance (cash basis)	-2.0	-2.4	-5.1	-3.7	-4.7
Gross external financing	1.0	1.7	3.6	1.3	0.8
Total public debt	33.6	36.0	40.6	42.2	43.8
Monetary accounts	(annual change, %)				
Money Supply (M2)	9.0	9.8	12.2	14.6	
Net Foreign Assets	-12.7	13.0	4.0	8.0	
Net Domestic Assets	8.0	12.0			
of which: Credit to the Private Sector	16.7	18.6	17.1	16	
External sector	(in millions of US$)				
Exports of goods	1,952	2,194	2,217	2,222	2,402
Imports of goods	2,773	2,741	2,534	2,659	2,913
Current account balance	-594	-21	-139	-136	-174
Foreign Direct Investment	549	261	235	249	293
Overall Balance	-237	21	-85	-145	-123
Foreign Reserves (months of imports)	2.2	2.5	2.6	2.7	2.8

Source: Ministry of Finance, Central Bank of Madagascar and staff projections.

10. **Private sector remained sluggish in 2015**. Private investments represented 11.6 percent of GDP in 2014, and are projected to remain flat in 2015. The creation of new formal enterprises in the first six months of 2015 was down by 30 percent compared to the same period in 2014. There is anecdotal evidence that the problem of unstable supply of electricity is causing entrepreneurs to postpone or abandon new investments despite new opportunities, and that delays in Value Added Tax (VAT) reimbursements to the export-oriented sectors are offsetting the edge created by depreciation of the local currency. Continued political uncertainties are also causing entrepreneurs to take a wait-and-see approach.

Fiscal policies and developments

11. **The fiscal deficit[1] shrank to 2.3 percent of GDP in 2014, down from 4 percent in 2013, while capital expenditure increased slightly**. Total revenue rose from 10.9 percent of GDP in 2013 to 12.4 percent last year. Budget grants and improved tax collection each accounted for 0.8 percent of GDP. The expenditure remained relatively flat between 2013 and 2014, at around 15 percent of GDP. The wage bill continued to consume an important share of the expenditure (38 percent in 2014), as did transfers to the state-owned enterprises and fuel subsidies. The capital expenditure also rose slightly to 27 percent of total in 2014, up from 21 percent in 2013, mostly financing agriculture infrastructure, road repairs and urgent investments in education and health. External financing accounted for 80 and 70 percent of total capital spending in 2013 and 2014, respectively. Neither revenue collection nor budget execution respected the stipulations of the supplementary State Budget 2014, with expenditure outpacing revenue. The authorities resorted to borrowing, with an increasing reliance on the Central Bank through statutory advances towards the end of the year (although staying within the legal limit).

12. **The fiscal deficit[2] is projected to increase back up to 4.2 percent of GDP in 2015, with expenditure growth outpacing the revenue increase**. Tax revenue in the first half of 2015 was 19 percent higher in nominal terms than in the same period in 2014, although lower than projected at the beginning of the year. The shortfall came mostly from the customs administration as slower than projected growth translated into fewer imports, and the lower prices of both main imports (petroleum-related products) and exports (mining) meant lower import and export values than projected. On the expenditure side, the State Budget 2015 had stipulated a nominal increase of 23.6 percent over the 2014 results, and the execution in the first half of 2015 outpaced this stipulation, in large part because the transfers to JIRAMA and Air Madagascar are higher than planned.

13. **Arrears, which the government started to accumulate during the transition period, compound the government's problem of low revenue, but efforts to clear them are being made**. As of October 2015, Ariary 143 billion (about US$47.7 million) have been cleared, half of which was paid to the fuel and electricity suppliers of JIRAMA, an additional 10 percent of which was paid to the petroleum companies for arrears relating to the pump fuel subsidies, and 16 percent was related to VAT reimbursements. According to the repayment schedule, the remaining payment due to these companies in 2015 amounts to Ariary 160 billion, without counting any new arrears accrued in 2015. The overdue interest payments equivalent to 0.4 percent of GDP have also been paid to the Central Bank this year. On the other hand, the continued difficulties of the Treasury are

[1] Commitment basis.
[2] Commitment basis.

leading to an accumulation of new arrears this year, estimated to be around Ariary 900 billion as of September 2015. In February 2015, the government introduced new medium-term Treasury bonds of 1-3 years as one of the solutions in an effort to regularize the situation. Creditor companies are generally responding favorably to these efforts. The government is receiving technical assistance from the IMF to improve arrears management.

Table 3: Fiscal Operations of the Central Government

	2012	2013	2014 Est.	2015 Proj.	2016 Proj.	2017 Proj.
Total revenues and grants	11.7	10.9	12.4	12.2	12.7	13.1
Tax revenues	10.0	9.3	9.9	9.9	10.4	10.9
Non-tax revenues	0.5	0.3	0.2	0.4	0.2	0.4
Grants	1.2	1.3	2.3	1.9	2.0	1.8
Total expenditure	13.5	14.9	14.7	16.4	15.7	17.2
Current expenditure	10.7	11.8	10.8	11.9	11.1	11.1
Wages	5.4	5.7	5.6	5.8	5.7	5.5
Goods and services	0.8	0.6	0.9	0.6	0.8	0.5
Transfers and subsidies	2.4	4.1	3.2	3.4	3.2	3.2
Interest	0.7	0.7	0.6	0.9	0.9	1.0
Capital expenditures	2.7	3.1	3.9	4.5	4.6	6.2
Domestically financed	0.8	0.6	1.2	0.8	1.1	1.4
Externally financed	2.0	2.5	2.8	3.7	3.5	4.8
Primary balance	-1.1	-3.3	-1.7	-3.3	-2.1	-3.1
Overall balance (commit. Basis)	-1.8	-4.0	-2.3	-4.2	-3.0	-4.1
Arrears variation (- = accumulation)	-0.1	-2.0	0.1	1.0	0.7	0.6
Overall balance (cash basis)	-1.7	-2.0	-2.4	-5.1	-3.7	-4.7
General government financing	1.4	2.0	2.4	4.6	1.6	1.5
External (net)	0.5	1.0	1.2	3.0	0.5	0.1
Domestic (net)	0.9	1.0	1.2	1.6	1.1	1.4

Source: MFB and staff projections

External sector

14. **The balance of payments turned positive in 2014, as the current account deficit continued to narrow**. The current account deficit dropped from 5.6 percent of GDP in 2013 to 0.2 percent in 2014, and continued to narrow in the first half of 2015. A 58 percent increase (in nominal US dollar value) in exports of nickel and cobalt and a 16 percent increase in tourism

receipts contributed to the improvement in 2014. Total export of goods and services increased by 10 percent while imports declined by 4 percent. In addition, there was a large inflow of budget support funds in 2014 and early 2015. These trends masked the deceleration of foreign direct investments, resulting from the end of the construction stage of the large mining operations. Foreign direct investments fell from 5.2 percent of GDP in 2013 to 2.4 percent in 2014, and are estimated to have stayed flat in the first half of 2015. A positive balance of payments contributed to a small accumulation of international reserves in 2014 to US$630 million (2.5 months of import cover). While there was not a significant accumulation in the first half of 2015, reserves are projected to continue the slow increasing trend to end 2015 with 2.6 months of import cover.

15. **The Central Bank has ceased its unorthodox interventions in the exchange rate market** and adopted a new policy for a cleaner float in conformity with good practice. It has terminated interventions of selling and buying foreign exchange in rapid succession towards the end of the day to establish the end-of-the-day exchange rate that made the Ariary seem more appreciated than the market would bear. It also plans to discontinue the temporary foreign exchange surrender requirements, initiated earlier in the year, when they expire in November 2015. These are important steps in adhering to a sound, market-based management of the exchange rate policies. As a consequence, the official exchange rate of the Ariary depreciated rapidly against major currencies, but the impact of the depreciation on the economy is expected to be limited, as most transactions were conducted at parallel rates already.

Table 4: BOP financing requirements and sources (in million USD)

	2013	2014 Est.	2015 Proj.	2016 Proj.	2017 Proj	2018 Proj.
Financing requirements						
Current account deficit (excluding official transfers)	-664	-129	-176	-183	-226	-362
Long term debt amortization (excl. IMF) 1/	-33	-48	-46	-61	-64	-59
Financing sources						
FDI and portfolio investment (net)	549	261	235	249	293	345
Capital grants	135	108	130	134	148	158
Official transfers	67	108	38	48	52	46
Long term debt disbursements (excl. IMF)	-315	-262	-227	-332	-325	-352
Change in reserves	272	-42	-21	-44	-85	-99
IMF credit (net)	-9	22	21	-12	-10	-8
Errors and omissions	-3	-19	0	0	0	0
Financing gap	0	0	-48	-201	-218	-332

Source: Central Bank, IMF and staff projections
Note 1/ Government only

Monetary policies

16. **Monetary policy continued to be passive, dominated by the pressures from the foreign exchange market and fiscal needs, but managed to contain inflation at single digits**. In 2014, annual inflation remained in line with previous year's trend at 6 percent despite increases in the

administered fuel price. In 2015, inflation increased as a result of the poor harvest and difficulties in transporting food and charcoal, as mentioned above, but has peaked by the middle of the year. Money growth was mainly driven by credits to the private sector by commercial banks; their lending to the economy rose by 18.8 percent between end-2013 and end-2014, and at a slightly slower rate of 17 percent in the first half of 2015. New loans were primarily allocated to private companies (60 percent of total variation) while also supporting household consumption and investments. The ratio of total credits to GDP remains structurally low at 13 percent, reflecting low financial intermediation and a high cost of borrowing whereas the banking sector is broadly liquid.[3]

2.2 MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

17. **The pace of economic recovery is expected to accelerate gradually along with the implementation of the National Development Plan**. The growth projection was revised down to 3.2 percent for 2015 from the initial forecast at the beginning of the year due to unfavorable local and international developments during the first half of the year. Investments should start picking up as the infrastructure projects in the pipeline enter the execution phase, and preparations for the Francophonie Summit, which Madagascar will host in 2016, start in earnest. The garment industry is expected to respond to the reinstitution of Madagascar's eligibility for the African Growth and Opportunities Act (AGOA) benefits, and exports to the US market are likely to recover strongly next year.

18. **The outlook for the external sector is balanced, although there are financing gaps corresponding to the fiscal gaps from 2015 onwards**. Continued low commodity prices will hurt mining exports, but will reduce import bills for petroleum-related products. The prospects for AGOA-linked exports are the bright spot in the forecast, while the recovery of the tourism sector will depend in no small part on the success in rehabilitating Air Madagascar. Imports of capital goods are likely to increase when investments pick up, which are expected to be offset by a higher inflow of external financing.

19. **The new Central Bank Law currently under preparation is expected to improve monetary and exchange rate policies**. The newly adopted policy for a cleaner float of the exchange rate will help the balance of payments adjust more smoothly. The Central Bank is receiving technical assistance from the IMF to strengthen its surveillance capacity. A Financial Sector Assessment Program (FSAP) is currently underway.

20. **Financing gaps remain for the government's budget in 2015 and beyond**. The gap for 2015 is estimated to be around US$48 million (approximately 0.5 percent of GDP), and the government is considering a loan[4] to fill it. The size of the gap from 2016 and beyond is larger than that in 2015 partly due to a lack of clarity on the availability of external financing in the form of budget support; if the support continues at a pace similar to 2014-15, the gap would remain manageable, if also accompanied by efforts from the government.

21. **The government is making efforts to expand fiscal space through a combination of**

[3] The banking sector reserves exceeded by 12% on average the monthly minimum requirement in 2014.
[4] The loan is likely to be on non-concessional terms. This loan, even if non-concessional, will not, however, affect the likelihood of debt distress.

economic recovery, increasing tax revenue and reduction in inefficient expenditure. Revenue increasing measures will be introduced in the State Budget 2016, the tax and customs administrations are reviewing the tax expenditures to reduce leakages, and audits of large tax payers aimed at improved compliance are planned (with World Bank assistance). Air Madagascar is revamping its business plan (with World Bank assistance) and seeking a strategic partner once again, having put the idea on hold during the political crisis. JIRAMA, the Ministries of Finance and Energy and BIANCO (independent anti-corruption agency) have formed joint task forces to improve financial operations and reduce nontechnical losses of the company. The government intends to remove the fuel subsidy by end 2015. If achieved, it would constitute a significant step in the right direction. The conditions are favorable for achieving this feat, as the trends in international oil prices suggest that the remaining gap between the administered and cost-based price will remain nil for the rest of the year. The government has started to clean up the civil service roster and plans to overhaul the civil service management system with assistance from the European Union. These efforts will take time to bear fruit, and not all of them will be equally successful. There is, however, a plan and an intention of the administration to move in the right direction.

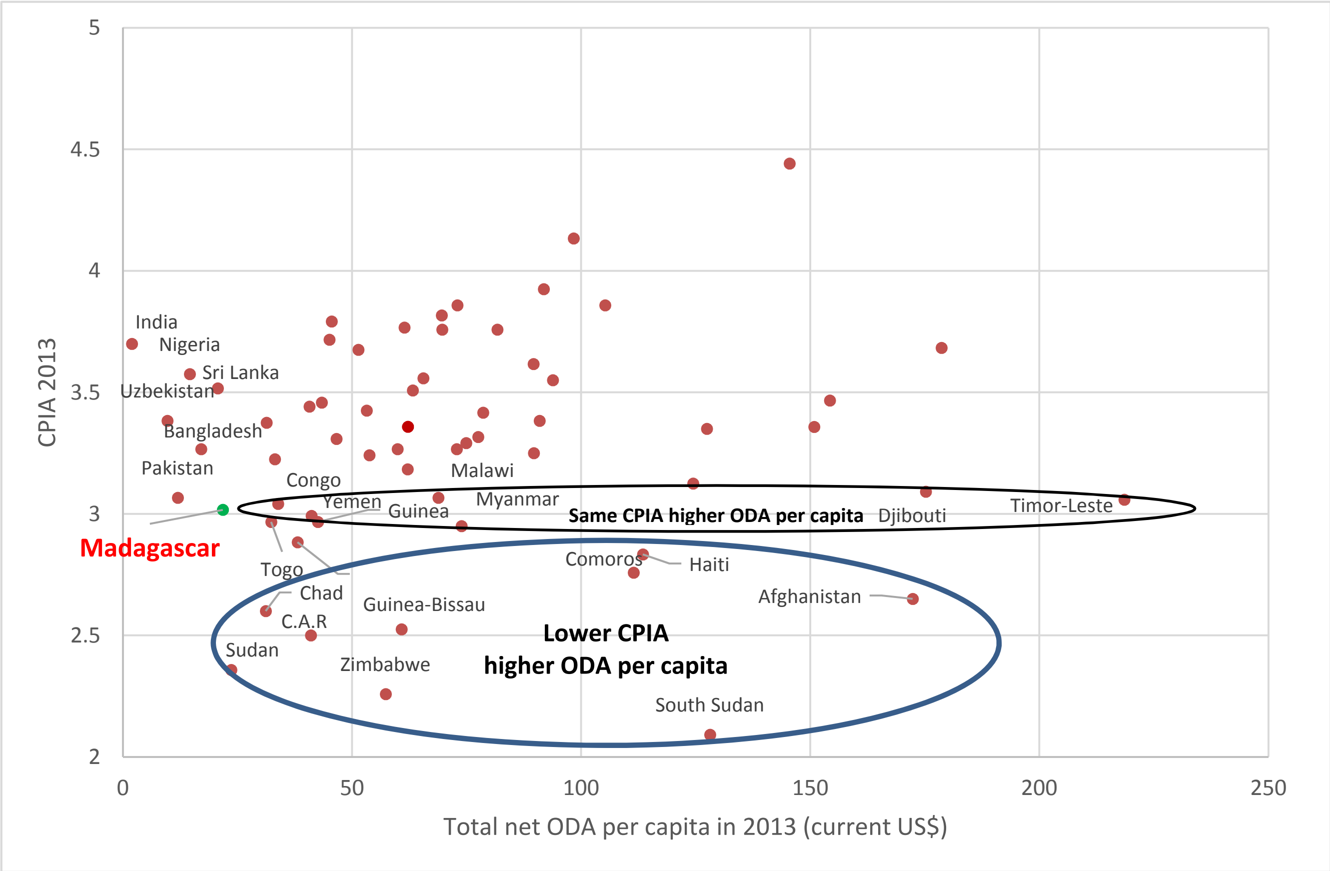
22. **Even so, fiscal sustainability is likely to remain the principal macroeconomic challenge for the authorities in the medium term**. The constraint is not the indebtedness, as Madagascar has maintained prudent debt policies, and its level of public debt to GDP ratio is moderate (see paragraph below). Rather, the country's problem is one of liquidity, as the government does not have adequate resources to make necessary investments to support the rate of growth to lift the country out of poverty and to execute even a minimum of social spending to relieve the most pressing needs of the poor, which is 93 percent of the population (see Table 1). Without robust economic growth and a sizable labor force employed in the formal sector, tax revenue is likely to rise only slowly despite the authorities' efforts. The country's ability to borrow is very limited, as it does not have an established credit record, and hence, lacks credit-worthiness. Madagascar's receipt of official development aid per capita is the second lowest among countries with similar or lower Country Policy and Institutional Assessment (CPIA) scores (Figure 4). There is no easy solution to the country's fiscal problem, and the authorities face challenging years ahead.

23. **Madagascar's risk of debt distress is likely to be elevated to "moderate" during the joint debt sustainability analysis for 2015, principally due to the large exchange rate depreciation** rather than increased borrowing. The public debt to GDP ratio is estimated to have increased to 40.6 percent at end-2015, from 36 percent at end-2014. The debt sustainability becomes a challenge only under most extreme (and unlikely) shocks. Meanwhile, debt management capacity has been enhanced steadily. A law on public debt was enacted in 2014, supported by the Reengagement DPO. Per the stipulation of the law, a medium term debt strategy is currently under preparation, and is expected to be published by end-2015. The implementation decrees of the law are being prepared, one of which is supported by this operation (see section 4.2 below).

24. **In sum, Madagascar's macroeconomic policy framework is adequate for the proposed operation**. It is predicated on the government's ability to define and execute a credible set of development and fiscal policies to serve as a basis for (i) satisfactory performance under the Staff Monitored Program, which will be presented to the IMF Board with the second Rapid Credit Facility (RCF) in November 2015, and (ii) the continued policy-based support needed to close the financing gap. Remaining risks include delays in economic recovery if the government fails to

restore political stability convincingly. Low international reserves are also of concern although this is allayed by the prospects for recovering garment exports and the balanced external outlook.

Figure 4. IDA countries' ODA per capita



Source: WDI, World Bank.

*CPIA covers most of IDA countries (low income and lower-middle income countries). Sao Tome y Principe, Solomon Islands, Kiribati, Samoa and Cabo Verde are out of the graph.

2.3 IMF RELATIONS

25. **The IMF and the government have reached an agreement at the technical level for a second RCF and a Staff Monitored Program**. The first RCF in the amount equivalent to SDR 30.55 million (about US$47.1 million) was approved by the Executive Board of the IMF on June 18, 2014, following the resumption of its relationship with the country after five years of suspension. The financing of the second RCF supports the adoption of the budget law 2016 and ceasing to engage in buy-back operations at non-market rates in the interbank foreign exchange market. A 6-months staff monitored program is aimed at (i) mobilizing fiscal revenue, (ii) improving the composition and quality of fiscal spending, (iii) strengthening fiscal transparency, (iv) strengthening the independence of the Central Bank, and (v) promoting inclusive growth. The staff monitored program is expected to pave the way for a possible agreement under the Extended Credit Facility. The World Bank maintains a close working relationship with the IMF, with regular collaboration across policy issues between the two institutions.

3. THE GOVERNMENT'S PROGRAM

26. **The government's program in the period between 2015 and 2019 is outlined in the National Development Plan** (*Plan National de Devéloppement*) endorsed by the Cabinet at end-2014. In order to reach "development through inclusive and sustainable growth, taking into account the spatial dimension," the document recognizes the need to achieve short term priority actions and structural reforms, in response to the country's fragility and persistent poverty. To respond to urgent needs and to reverse rapidly the decline in the living conditions of the population, the government prepared a Presidential Urgent Program (*Programme d'Urgence Présidentiel*) (2015-2016) which presents the government's selected program for 2015 and 2016.

27. **The National Development Plan has five strategic pillars identified from a country diagnostic and the government's vision defined in the General Policy of the State (*Politique Générale de l'État*)**. The strategic pillars are:

i. Governance, rule of law, security, decentralization, democracy and national solidarity,
ii. Macroeconomic stability preservation and development support,
iii. Inclusive growth and territorial anchorage of development,
iv. Adequate human capital for the development process, and
v. Preserving natural capital and enhancement of disaster risk resilience.

28. **Transparency of public finance is identified as a prerequisite to achieving the stated targets**. Specifically, the objectives for the macroeconomic stability pillar include "economic efficacy and transparent and efficient public finance." To this end, the government will present the audited final accounts of the State Budget (*Loi de Règlement*) from 2007 to 2012, implement the law on public debt, reform the public pension system, revise the legal framework for public procurement, update the legal framework governing trade and revise the legal framework on tax exemptions.

4. THE PROPOSED OPERATION

4.1 LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

29. **The development objective of the program is (i) strengthening reporting and increasing availability of information relevant to assessing the effectiveness of public finance, and (ii) improving payroll management and consolidating accounts in line with the treasury single account principle**. The proposed operation is a stand-alone, single tranche credit to accompany the government's efforts to turn around the country. It supports the "macroeconomic stability" pillar of the government's national development plan most directly, and the "governance and rule of law" pillar indirectly. The two pillars were selected as the natural foundations for overcoming the country's main challenges to reducing poverty. To conduct appropriate pro-poor policies, economic growth and fiscal space for the government are necessary, and improved transparency and better public finance management are steps in this direction. The other three pillars, "inclusive growth," "human capital development" and "natural resources and resilience against catastrophes," are supported by complementary investment and technical assistance operations.

4.2 PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

30. **The proposed operation will support seven prior actions which would help enlarge the fiscal space or improve transparency of public finance as a precondition for improving public service delivery**.

Prior action 1: The Ministry of Finance and Budget of the Recipient has eliminated ineligible persons from its payroll roster of high office holders.

31. **Rationale**. The wage bill represents around 40 percent of the public expenditure in Madagascar. The high share is primarily because public expenditure is low, rather than because the civil service is large; the share of the wage bill in GDP and the number of civil servants per 1,000 population in Madagascar are below the sub-Saharan African region average (see Table 5). The fact remains, however, that the wage bill is the largest item in the State budget, and one that could be managed better to make fiscal space for more development spending. Moreover, it is currently not possible to know the exact number of civil servants due to the inconsistencies in the tools used for managing human resources maintained by the Ministry of Civil Service (MCS) and the payroll maintained by the Ministry of Finance and Budget. To rectify this situation, a civil service census is planned with the financial and technical support of the European Union, but it is a major undertaking that will take a few years to complete. Meanwhile, there are incremental steps that can be taken, which could bring immediate savings and improvement in civil service management.

Table 5: Comparison of salary expenditure

	Ratio salary expenditure			Public servants per 1000 population
	/GDP	/ revenue	/expenditure	
Average SS Africa	6.4%	33.5%	26.1%	10
Madagascar	5.7%	54.5%	42.5%	6

Source: MFB and World Bank, 2013.

32. **Policy**. The Ministry of Finance and Budget has removed from the roster of high office holders (*hauts fonctionnaires*) all those who no longer hold the posts, and is reviewing the identification records of all the civil servants to remove from the payroll those who are past the legal retirement age (without obtaining exception). Once birth dates of all civil servants are on record, the payroll and human resource databases are to be reconciled regularly, as a preliminary step towards moving progressively to an integrated civil service management.

33. **Results**. The ultimate results expected are improved management of the civil service payroll, and a reduction of wasteful expenditure. The immediate result is a reduction of wasteful expenditure by reviewing the high office holder roster. As of October 2015, estimated monthly savings are close to Ariary 300 million (roughly US$90,000). In addition, savings of around Ariary 1.3 billion (roughly US$430,000) are realized from mandatory retirement of those past the legal

age limit.[5] More savings are expected when the birth dates of the remaining 30,000 agents are verified.

Prior action 2: JIRAMA has started to publish monthly statistics on the delivery of diesel to, and generation of electricity at, major diesel-based electricity generation centers

34. **Rationale**. JIRAMA continues to have financial and operational problems, compounded by a long strike during August-September 2015. The use of cost-ineffective diesel at JIRAMA has increased in the first half of 2015, while power outages have worsened in the last months. While overhauling JIRAMA is a major undertaking necessitating significant technical and financial assistance as well as time (the World Bank has an energy project (P151785) under preparation for this purpose), there are a number of immediate measures which could contribute to reducing the losses. Monitoring the use of diesel more closely at JIRAMA is one such measure. Making public the information on the use of expensive diesel is expected to improve transparency and accountability of the use of diesel, inform the public about cost-(in) effectiveness of diesel-based electricity generation, and pave the way for informed decision-making towards a more sustainable energy strategy.

35. **Policy**. The Ministry of Finance and Budget, Ministry of Energy and Hydrocarbon, JIRAMA and BIANCO have established a task force to monitor the use of diesel by JIRAMA. After the first round of inspection missions, the two ministries and JIRAMA have reached an agreement to select major electricity-generating centers, covering more than 80 percent of diesel-based electricity generation in the country, and publish statistics on diesel delivered and electricity generated. In October 2015, the summary statistics for 2014 and monthly statistics for January through August 2015 were published. The monthly statistics will continue to be published within 45 days of closing of the month.

36. **Results**. The ultimate result is to transform JIRAMA into a well-managed company that provides quality service, and the intermediate result expected is a reduction in operational losses of JIRAMA, and a corresponding decline in subsidies from the State. The immediate results expected are improved efficiency of the diesel-based electricity generation, and a shift away from the costly diesel to the less expensive heavy fuel as inputs to thermal electricity generation.

Prior action 3: Air Madagascar has (i) appointed a new general manager through a competitive process, and (ii) published its audited financial accounts for the 2010 to the 2013 calendar year on its website

37. **Rationale**. The continued poor performance of Air Madagascar is a drain on the public Treasury, and a drag on the economy. A protracted strike in 2015 at Air Madagascar at the beginning of the peak tourism season, and its poor handling by the management have led to massive cancelations of flights resulting in losses in tourism revenue and disruptions to private sector activities. While overhauling this underperforming state-owned company is a major undertaking necessitating significant technical and financial assistance (the second Integrated

[5] The savings arising from retirement are partially offset by the corresponding increase in payouts of the State pension, which is funded by the State budget. The World Bank is helping the government to analyze the stream of future liabilities of the State pension fund.

Growth Pole project (P113971) has a component to improve air transport sector. It will provide technical assistance to develop and support implementation of the positioning strategy for Air Madagascar), there are a number of immediate measures which could contribute to reducing the losses. Appointing a qualified person at the helm of the company through a competitive process is one such measure. A professional general manager is accountable for the operational and financial results of the company, and is expected to start complying with the financial disclosure rules within the year of appointment.

38. **Policy**. Air Madagascar, supported by an independent human resources recruiting company, has appointed the new general manager on October 2, 2015 through a competitive selection process. Air Madagascar has also posted its audited financial accounts up to 2013 on its website, and is in the process of finalizing the 2014 accounts, to be posted shortly.

39. **Results**. The ultimate result is to transform Air Madagascar into a well-managed company that provides quality service. The immediate result expected is the compliance of Air Madagascar with financial disclosure rules to make it possible to evaluate the company's performance accurately.

Prior action 4: The Recipient has published, through the Economic Development Board of Madagascar, the list of enterprises that are granted benefits under the Free Zone regime (*Zone franche*).

40. **Rationale**. An IMF study (2015), available data and direct observations have found that one of the main reasons for Madagascar's low revenue collection is the narrowness of its tax base. Among the factors contributing to this narrowness are the size of the informal sector, corruption, fraud and tax expenditures. A large part of Madagascar's tax expenditures comes from special regimes, such as the Large Mining Enterprises Law and Export Processing Zone (EPZ), while it is estimated that ad hoc exemptions and exonerations are also sizable. These last two categories of tax expenditures are granted by the Council of Government. Although such expenditures are often aimed at achieving certain development objectives, their impacts are not assessed, and the ad hoc privileges are not always granted transparently or systematically, when they should in principle be treated like any other expenditures and be subjected to the same level of scrutiny. As a part of the medium term strategy to increase tax revenue, the tax and customs administrations are preparing to review these expenditures (with World Bank assistance) with the aim of introducing more accountability and transparency. The first step is to take an inventory of existing tax expenditures.

41. **Policy**. The list of enterprises that are granted an EPZ license has been published on the website of the Economic Development Board of Madagascar. This action will make it easier to verify the eligibility of the claimants requesting the associated benefits at customs and elsewhere.

42. **Results**. The ultimate result is for the legislative branch and public at large to be advised of the costs and benefits associated with all tax expenditures, and to be able to make informed decisions on which expenditure to maintain and which to discontinue. The immediate result expected is improved transparency in who benefits from tax reductions and exemptions. The main beneficiaries can be classified in three categories, the companies registered under the EPZ regime, those under the Large Mining Investment Law (LMIL), and those who receive ad hoc decision by the Council of Ministers.

Prior action 5: The Recipient has issued an implementing decree for the law on public debt concerning opening dedicated accounts for externally-financed projects at the Central Bank of Madagascar

43. **Rationale**. In 2014, the National Assembly adopted a law on public debt which provides a legal framework to ensure public borrowing is conducted strategically and prudently. The adoption was supported by the Reengagement DPO[6]. The implementation decrees needed to apply the law are under preparation, one of which governs the dedicated accounts used for receiving and managing proceeds of loans and credits for externally-financed projects for which the State is the borrower/recipient. The current practice is to open such accounts at commercial banks, but the debt law stipulates that they should be consolidated in the Treasury account at the Central Bank to improve the efficiency of Treasury management by upholding the principles of the treasury single account.

44. **Policy**. The Ministry of Finance and Budget prepared and the government, through the Council of Ministers, has issued the implementing decree providing details of the modality of the transfer and functioning of the project sub-accounts within the Treasury account at the Central Bank of Madagascar.

45. **Results**. The ultimate result expected is improved efficiency of the Treasury management. The immediate result is the consolidation at the Central Bank of Madagascar of most of the Treasury accounts dedicated to externally-funded projects, as a step towards the ultimate goal.

Prior action 6: **The Recipient has submitted the audited final accounts of the State Budget for the fiscal years 2009, 2010 and 2011 to the Parliament for approval**

46. **Rationale**. Timely and accurate accounting and reporting are an important pillar of sound public financial management. The Organic Law on Budget Acts 2004 (*Loi organique relative aux lois de finances*) stipulates that the annual consolidated and audited public accounts be submitted to the Parliament during the first session of the second year following the fiscal year concerned (approximately 18 months). The government submitted the audited accounts for 2008 and 2009 to the Parliament in June 2015, and those for 2010 and 2011 in October 2015. The Ministry of Finance has established a calendar to catch up with the submission of the audits, and has plans to become compliant by end 2016.

47. **Policy**. The government has submitted the annual consolidated audited public accounts for 2009, 2010 and 2011 to the Parliament in 2015.

48. **Results**. The ultimate result is that the legislative branch is informed of the execution results of the public finance in a timely manner, and is better able to assess their effectiveness and efficiency in achieving the national development objectives. The immediate result is that the government is in compliance with the submission deadline for the audited final accounts, as stipulated in the Organic Law on Budget Acts.

[6] Report No. 90809-MG.

Prior action 7: **Starting May 2015, the Ministry of Finance and Budget is publishing the monthly in-year budget execution results in no later than 60 days of month end**

49. **Rationale**. Timely and accurate accounting and fiscal reporting are an important pillar of sound public financial management. The MFB has been producing monthly budget execution reports in a format that allows for comparison with the initial budget, but these reports were not readily available until May 2015 to analysts and the public at large. As a result, it has been difficult to have informed discussions on public policies such as the merits and costs of fuel subsidies, and the need to prioritize public investments given the available envelope for capital expenditure.

50. **Policy**. The Treasury Department of the MFB has started in May 2015 to publish the monthly in-year budget execution results (*Opération Globale de Trésor*) on the MFB website within 2 months of closing, in a user-friendly format.

51. **Results**. The ultimate results are that the public is informed of the execution results of the public finance in a timely manner, and is better able to assess their effectiveness and efficiency in using public funds. The immediate result expected is that taxpayers and public at large are able to access the execution results of the public finance within 6 weeks of the end of the month.

Table 5: DPO Prior Actions and Analytical Underpinnings

Area	Prior actions	Analytical underpinnings
Expenditure	The Ministry of Finance and Budget of the Recipient has eliminated ineligible persons from its payroll roster of high office holders.	PGDI final report (2009), Reengagement Policy Notes (2014) found civil service management to be weak, and recommended an overhaul.
Expenditure/ SOE	JIRAMA has started to publish monthly statistics on the delivery of diesel to, and generation of electricity at, major diesel-based electricity generation centers	Reengagement Policy Notes (2014), Doing Business surveys and other studies have found access to electricity to be one of the most important constraints to private sector activities.
Expenditure/ SOE	Air Madagascar has (i) appointed a new general manager through a competitive process, and (ii) published its audited financial accounts for the 2010 to the 2013 calendar year on its website	DTIS (2015), Reengagement Policy Notes (2014) Indian Ocean Island Economies: assessing opportunities for regional tourism integration (2013) found underperformance of Air Madagascar as one of the critical constraints to the transportation network and development of the tourism sector.
Tax expenditure	The Recipient has published, through the Economic Development Board of Madagascar, the list of enterprises that are granted benefits under the Free Zone regime (*Zone franche*).	Tax policy diagnostic (IMF 2015) found a sizeable tax expenditure, and recommended a study of their costs and benefits, starting with an inventory.
Increase fiscal space/ treasury management	The Recipient has issued an implementing decree for the law on public debt concerning opening dedicated accounts for externally-financed projects at the Central Bank of Madagascar.	DeMPA (2013), PEFA and other public financial management guidelines agree that the Treasury Single Account is a good practice principle to uphold.

Area	Prior actions	Analytical underpinnings
Transparency /Reporting	The Recipient has submitted the audited final accounts of the State Budget for the fiscal years 2009, 2010 and 2011 to the Parliament for approval	PEFA, CPIA stipulate timely reporting of final public accounts to be good practice.
Transparency /Reporting	Starting May 2015, the Ministry of Finance and Budget is publishing the monthly in-year budget execution results in no later than 60 days of month end	PEFA, CPIA stipulate timely reporting of in-year government budget execution to be good practice.

4.3 LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

52. **A Systematic Country Diagnostic (SCD) presented to the Board in August 2015 emphasized the need to be cognizant of the country's fragility, and working towards improved efficiency and transparency of public service delivery as a way of helping the country to turn around**. As over 80 percent of the Malagasy population lives under extreme poverty, the SCD recommended concentrating on the first of the World Bank Group's twin goals of fighting extreme poverty, and consistent with the Africa Strategy, to work selectively and flexibly. The SCD underscored the importance of enlarging the fiscal space as a prerequisite, so that the government has the means of implementing policies and making public investments. The efforts to enlarge the fiscal space are underway, but they will take a few years to bear significant results. They are also likely to encounter strong resistance from vested interests, who have become accustomed to not complying with the tax obligations during the long political crisis. The authorities had also fallen behind in their reporting obligations concerning how public finance has been executed. Thus, "establishing and reinstituting budget oversight mechanisms to create greater accountability and better performance of public expenditure" was also identified as a priority in the SCD. The proposed operation seeks to put in place building blocks to help create an environment conducive to encouraging compliance with the laws and obligations: transparency is one of the important tools in inducing accountability; making information available on how public resources are used and creating an environment where checks and balance can function are complementary to efforts undertaken by tax authorities to improve revenue mobilization. The proposed operation also contributes to tackling the problem of "access to electricity and transport infrastructure," an area identified by the private sector as the main constraints to doing business, and also selected as a priority challenge in the SCD.

53. **The proposed DPO is an integral part of the World Bank's new Country Partnership Framework (CPF) for Madagascar**, which will operationalize the SCD's findings and recommendations. The CPF will be presented to the Executive Board of Directors in FY16 Q3, after the decision on a possible increased financing package under the exceptional allocation regime for countries facing "Turn-around" situations.[7] The Turn-around facility enhances IDA financing to qualifying countries where fragility and conflict impose severe constraints on development, are confronted with a turn-around situation and are committed to reform. Subject to Management's approval, the IDA team will provide an informal oral briefing to Executive Directors on the case for exceptional support, the parameters for its provision and duration prior to the presentation of the proposed operation or at their convenience. The final eligibility decision

[7] See "Implementation Arrangements for Allocating IDA Resources to Countries Facing "Turn-Around" Situations. IDA, Oct. 2013.

will take into account the guidance received during the consultations with Executive Directors and will be formalized in the CPF. The financing for the proposed operation does not, however, depend on receiving an increased allocation under the Turn-around facility.

54. **This operation builds on the lessons emerging from the past DPOs prepared for the country, especially the most recent Reengagement DPO (Cr. 5582-MG), as well as those prepared for fragile environments**. The Reengagement DPO, approved on December 18, 2014, focused on politically feasible reforms that can build a momentum for future changes, as recommended by *World Development Report (2011), Conflict, Security and Development* and an Independent Evaluation Group (IEG) report on engaging with fragile states.[8] The scope and complexity of the Reengagement DPO were kept modest and in line with a realistic assessment of the political economy constraints. Even so, a preliminary evaluation suggests mixed results, mainly because the political balance has proved to be even more fragile than expected. In some cases, such as for asset declaration, it has been difficult to follow up the first steps supported by the operation with the next ones. In others, such as the reorientation of the State Budget towards development spending, there has been some backtracking when budget pressure mounted. Still, the operation has been under implementation for under a year. The preliminary assessment is that the selected level of complexity and areas of engagement for the Reengagement DPO were broadly adapted to the political reality. The currently proposed operation has an even more streamlined scope, and takes more calibrated steps aimed at consolidating progress and soliciting public support for the reforms being pursued.

55. **The proposed operation is designed to complement the investment and technical assistance projects that are ongoing or under preparation**. Its principal goal of improving the preconditions for increasing inclusive service delivery complements three ongoing projects, the Emergency Support to Critical Education, Health and Nutrition Services Project (P131945), the Emergency Support to Education for All Project (P132616), and the Social Protection Investment Project (P146919). The policy actions to improve governance and restore a culture of respecting the laws and obligations in general, and to increase revenue mobilization in particular, contribute to the objectives pursued in the recently completed Governance and Institutional Development Project (P103950), as well as its successor operation the Public Sector Performance project (P150116), under preparation. The Energy Sector Operations and Governance Improvement project (P151785) under preparation, and a component of the second Integrated Growth Pole Project (P113971) seek to help improve the management and performance of JIRAMA and Air Madagascar, respectively, and transform them into profitable companies that provide quality service to their customers. These projects also complement this operation.

4.4 CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

56. **The authorities have organized consultations with relevant stakeholders in the process of formulating the National Development Plan**. The consultations were held in the capital and

[8] *World Bank Group Assistance to Low-Income Fragile and Conflict-Affected States: An IEG Evaluation* (2013).

regions, inviting sector ministry experts, civil society, academia, private sector representatives as well as development partners.

57. **The *Cadre de Partenariat*, co-chaired by the Ministry of Finance and Budget and the World Bank, provides a forum for collaboration among potential providers of budget support**. The members are the African Development Bank (AfDB), the European Union, France, and the World Bank. All members of the *Cadre* prepared budget support operations in 2014. France and the European Union have floating tranches outstanding that are likely to disburse this year, and the AfDB is considering a new budget support operation. Due to the different procedures and timing that the development partners followed in resuming budget support operations, the members opted not to develop a unified policy action matrix common to all partners for the first operation. However, the reforms supported by these operations and by the IMF overlap to a large extent (identical in the case of AfDB), reflecting the convergence of views on what are the priorities and feasible reforms for the country at this juncture. The *Cadre* aims to move towards a more harmonized approach to policy dialogue to improve alignment with the government's budget cycle, deepen impact and reduce transaction costs for the government.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1 POVERTY AND SOCIAL IMPACT

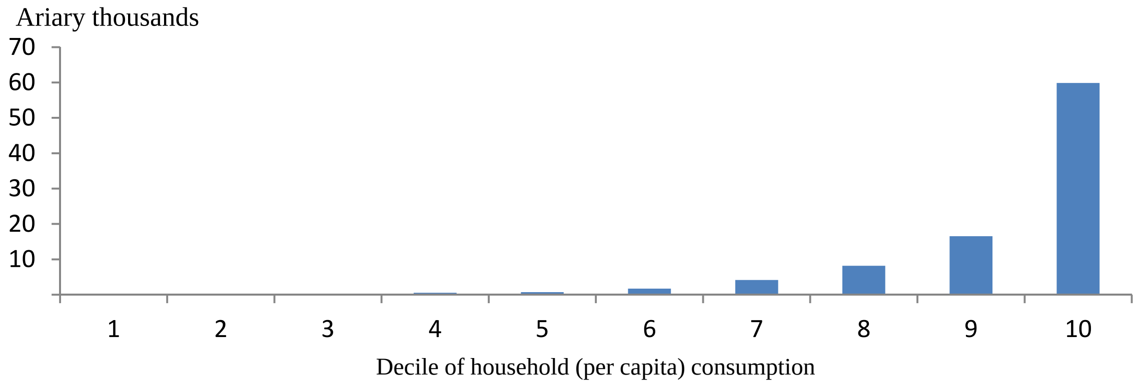
58. **The policies supported by this DPO are likely to contribute to poverty reduction and a positive social impact**. The actions designed to strengthen reporting and increase availability of information relevant to assessing the effectiveness of public finance, and improving efficiency of public finance are expected to contribute indirectly to poverty reduction in the future, as better access to information and improved efficiency of public finance could be used to fund measures to alleviate poverty.

59. **Prior action 1, supporting the elimination of ineligible persons from the payroll roster of high office holders does not entail any job losses.** The action stops paying the position-specific benefits to those who had already left the position. The larger effort, not directly supported by the prior action, enforces compliance with the legal retirement age and eliminates ghost workers from the payroll. While these efforts entail reduction of income by those affected, corresponding to the savings realized by the Ministry of Finance, they are not legally entitled to such income. Moreover, civil servants are generally not poor, and high office holders even less so, even after retirement. To the extent the savings from cleaning up the payroll are allocated to public investments or social spending, as described in the NDP, the prior action is expected to have a positive poverty and social impact.

60. **Prior action 2, intended to improve transparency of JIRAMA, will not have any direct poverty and social impact, and is likely have two broadly progressive distributional impacts indirectly in the long run**. First, the intended impact is a reduction in non-technical losses by JIRAMA, which in turn should improve its finances and allow the State to reduce subsidies to the company. Only 14 percent of the population had access to electricity in 2010, and new connections have been expanding this figure at approximately 1 percentage point per year. The distribution by consumption decile of those who have access to electricity is shown in Figure 5 below. Since

electricity usage, and therefore explicit and implicit subsidies, are highly regressive, improvements to JIRAMA's cost recovery would be progressive. Second, based on international evidence, improved financial soundness of the electricity provider would in the long run result in expansion of service and greater reliability of existing service. Expanded availability of more reliable power would, if achieved, primarily benefit currently un-served populations which tend to be below the top 40 percent of the consumption distribution.[9]

Figure 5. Household Mean Monthly Expenditure (per capita) on Electricity by Consumption Decile in 2012



Source: ENSOMD 2012
Note: Consumption deciles are based on preliminary consumption aggregates.

61. The remaining prior actions supported by the proposed operation are not expected to have any direct poverty and social impacts.

5.2 ENVIRONMENTAL ASPECTS

62. The policy actions supported by this operation are not expected to have any direct environmental impact.

5.3 PFM, DISBURSEMENT AND AUDITING ASPECTS

63. **Addressing the fiduciary concerns and strengthening the government's public financial management has been a subject of an ongoing dialogue and technical assistance** over the last decades. A series of reforms are been implemented in the areas of taxation, budgeting, treasury and cash management. Progress has been made in the area of budget management. The 2014 PEFA self-assessment showed that the country has improved budget credibility regarding revenue forecasting. Annual budget laws are published on the Ministry of Finance's website in a timely manner. In addition, efforts have also been made to improve budget transparency with the regular publication of Quarterly Budget Execution Reports on the MFB's website within a month of the end of the period, an improvement compared to 2008. The annual execution reports are produced, but not made available to the public. The completion of the first Open Budget self-assessment in

[9] If eventual improvements to the governance of the electricity sector are sufficient, this could result in greater productive employment opportunities, which would benefit the general population, including the poor.

July 2014 is an additional step in the right direction. The government has also announced recently its intention to officially join the Open Budget Initiative.

64. **Challenges remain, however, in several areas**. The evaluation of expenditures is showing mismatches between budget provisions and execution, both on the amounts and the composition. Budget information is not exhaustive. Budget preparation has been undermined by a lack of adequate inclusion of sectoral ministries. On the expenditure side, extra-budgetary expenditures are common practice, creating opportunities for abuse. Major shortcomings also exist in the production of annual consolidated accounts as well as in the audits by the independent accounting agency. The proposed operation supports the government's effort in addressing these issues.

65. **An interim Public Financial Management (PFM) Action Plan was developed with technical assistance from the IMF, and is being implemented**. The Action Plan is informed by the 2014 PEFA self-assessment and an extensive PFM diagnosis financed by a World Bank project.[10] The Plan focuses on: (i) change management; (ii) enhanced transparency of public finances; (iii) improved budget credibility and financial sustainability of public policies; (iv) sound public debt management; and (v) enhanced accountability of accounting officers. The interim PFM Action Plan was approved by the Council of Ministers on October 28, 2014. The future PFM Vision and five year action plan under preparation will aim at further improving budget transparency and comprehensiveness, accounting, financial reporting, internal controls, external audit and external scrutiny. Although weaknesses remain in many areas, the country PFM system is deemed adequate to manage the proceeds of the proposed operation.

66. **The IMF conducted a safeguards assessment of the Central Bank in September 2014**, and confirmed that the Central Bank of Madagascar's control, accounting, reporting, and auditing systems are adequate, but need improvements to better strengthen its governance. Publication of the annual reports of the Central Bank was suspended during the crisis but has resumed; the annual reports up to 2013 are posted on the Central Bank's website.[11] The previous operation (Reengagement DPO P150503) was presented to the Board of Executive Directors before the results of the safeguards assessment became available, and hence, IDA required an audit of the dedicated account of the Treasury at the Central Bank of Madagascar. This audit was duly carried out in May 2015, and was deemed satisfactory by IDA.

67. **The proposed credit will be disbursed following the standard IDA procedures for development policy operation**. A credit in the amount of SDR 39.4 million (US$55.0 million equivalent) will be made available upon effectiveness and, provided IDA is satisfied with the implementation of the development policy program and the appropriateness of the Recipient's macroeconomic policy framework, disbursed as a single tranche following the submission of an acceptable withdrawal application by the government. IDA will deposit the proceeds into a dedicated US dollar-denominated account designated by the Recipient that is part of the country's foreign exchange reserves accounts at the Central Bank of Madagascar. The dedicated account will be used exclusively for the DPO credit proceeds. The Recipient shall ensure that upon the deposit of the credit proceeds into said account, an equivalent amount is credited in the Recipient's budget management system, in a manner acceptable to IDA. The Recipient will report to IDA on

[10] The PFM diagnosis was conducted under the Madagascar Second Governance and Institutional Development Project (P103950), which closed on August 31st, 2014.
[11] http://www.banque-centrale.mg/index.php?id=m6_3

the amounts deposited in the foreign-currency account and credited to the budget-management system within 30 days of deposit.

68. **The financial support provided under this operation is not intended to finance goods or services in the standard negative list**. If the proceeds of the credit are used for ineligible purposes as defined in the Financing Agreement, IDA will require the Borrower, promptly upon notice from IDA, to refund an amount equal to the amount of said payment to IDA. Amounts refunded to IDA upon such request shall be cancelled. An audit of the deposit will be carried out within four months of the deposit. A legally registered, private and independent audit company meeting appropriate international standards will be contracted to perform the audit, and in accordance with the Terms of Reference agreed upon with the Government of Madagascar. All audit costs will be borne by the Government of Madagascar.

5.4 MONITORING, EVALUATION AND ACCOUNTABILITY

69. **Progress on the results indicators will be monitored and evaluated jointly by the Recipient and the World Bank**. The Ministry of Finance and Budget has a designated coordinator for budget support operations, and has an adequate capacity. The members of the *Cadre de Partenariat* intend to move towards regular and harmonized monitoring of results, common to all budget support operations in the medium term.

70. **Grievance Redress**. Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the World Bank's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the World Bank's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate GRS, please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

71. **The overall risk rating for the operation is 'substantial,' with two main sources of risk that are inter-connected and that could potentially jeopardize the expected outcomes and benefits of this operation**. The risks are (i) political and governance; and (ii) macroeconomic. Measures to mitigate these risks are outlined below. The potential benefits of the proposed operation outweigh the residual risks and warrant IDA's assistance.

Risk categories	
1. Political and governance	High
2. Macroeconomic	Substantial
3. Sector strategies and policies	Moderate

Risk categories	
4. Technical design of program	Moderate
5. Institutional capacity for implementation and sustainability	Moderate
6. Fiduciary	Moderate
7. Environment and social	Moderate
8. Stakeholders	Moderate
9. Others (i.e. vulnerability to weather-related shocks and natural disasters)	Moderate
Overall	Substantial

72. **The principal risk to the objectives of this operation is that the supported actions are not enough to build the reform momentum**. Because the proposed operation is a single-tranche, stand-alone operation, the actions supported are necessarily steps in the longer reform agenda. If the reform efforts stall, unable to overcome the resistance from stakeholders with vested interests or overwhelmed by political events, the development objectives would not be achieved. This risk is high and cannot be controlled completely, but this operation mitigates it in two ways. First, it seeks to attain the strongest possible actions needed to build the reform momentum without overwhelming the capacity of the post-crisis government. Second, it is complementary to other projects and technical assistance provided by IDA and development partners, which together constitute a more holistic support environment than one operation can offer.

73. **Insufficient tax revenues, growing transfers to the two State-Owned Enterprises (SOEs) and low international reserves constitute a macroeconomic risk, while a delay in economic recovery and resumption of aid inflows will compound it**. Increasing the fiscal space is one of the main goals of the proposed operation and of a new public sector project under preparation; it is also supported by technical assistance from the IMF. Reducing inefficiencies at JIRAMA and Air Madagascar, supported by this operation, would mitigate this risk. The financial contribution provided by this operation will also reduce this risk directly.

74. **In addition, Madagascar's vulnerability to natural disasters and weather-related shocks represents a moderate and indirect risk to this operation.** Madagascar ranks among the countries most exposed to droughts, floods and cyclones. Severe natural hazards present threats to public health, food security, and the government's poverty reduction goals. The immediate necessity of responding to environmental shocks could draw scarce administrative resources away from the reform program and threaten its long-term continuity. This risk is mitigated by the ongoing dialogue on enhancing resilience to natural disasters, and support provided by the World Bank and other development partners to the government. For example, the World Bank is currently supporting the rehabilitation of cyclone and flood early warning systems and hydro meteorological station nationwide. Even though active support from development partners had declined during the transition period, it is expected to revive and contribute to mitigating this risk.

ANNEX 1: POLICY AND RESULTS MATRIX

Prior Actions	Indicator	Baseline (year)	End program Target (2017)
1. The Ministry of Finance and Budget of the Recipient has eliminated ineligible persons from its payroll roster of high office holders.	(i) The number of civil servants with date of birth information not on record at the MFB, (ii) the civil service rosters at MFB and MCS are reconciled every 6 months, and (iii) amount of position-specific benefits paid to those who had already left the "high officer" positions.	(i) 30,000 civil servants (approx. 25% of total) (2015) (ii) reconciliation has not been done (2014) (iii) Approximately 3.56 bn Ariary (2015).	(i) 0; (ii) reconciliation was done within the last 6 months (iii) 0.
2. JIRAMA has started to publish monthly statistics on the delivery of diesel to, and generation of electricity at, major diesel-based electricity generation centers.	(i) Liter of diesel per kwh of thermic generation of electricity by JIRAMA (including the private centers for which JIRAMA is responsible for the fuel supply); (ii) data on diesel consumption and electricity generation publicly available	(i) 0.16 L/kwh; (ii) no information is available (2014)	(i) 0.14 L/kwh; (ii) the database is updated monthly
3. Air Madagascar has (i) appointed a new general manager through a competitive process, and (ii) published its audited financial accounts for the 2010 to the 2013 calendar year on its website.	The audited accounts of Air Madagascar are published within the time allotted by regulations	Publications are overdue (2014)	Publication is on time (in compliance with the Law)
4. The Recipient has published, through Economic Development Board of Madagascar, the list of enterprises that are granted benefits under the Free Zone regime (Zone franche).	List of enterprises which receive tax expenditures through LMIL, EPZ Law and by Council of Ministers decisions publicly available.	No systematic information is available (2014)	The three lists, updated annually, are available publicly
5. The Recipient has issued an implementing decree for the law on public debt concerning opening dedicated accounts for externally-financed projects at the Central Bank of Madagascar.	The share of dedicated accounts for externally-financed projects held at the Central Bank	0% (2014)	90% of the accounts, with explicit deadline for closure of any accounts remaining at commercial banks.
6. The Recipient has submitted the audited final accounts of the State Budget for the fiscal years 2009, 2010 and 2011 to the Parliament for approval.	Length of time needed to submit the audited consolidated final accounts of the State Budget.	Over 5 years (for 2008 accounts) (2014)	Within 24 months of end year
7. Starting May 2015, the Ministry of Finance and Budget is publishing the monthly in-year budget execution results in no later than 60 days of month end.	Timeliness of the publication of the monthly budget execution report by the Treasury (OGT)	OGT is not publicly available (2014)	Within 6 weeks of end month

ANNEX 2: LETTER OF DEVELOPMENT POLICY

Translated from original French, emphasis added

MINISTRY OF FINANCE AND BUDGET

- - - - -

Minister

- - - - -

Antananarivo, November 5, 2015

Minister of Finance and Budget

to

Dr Jim Yong Kim

World Bank

1818 H Street NW, Washington DC

Mr. President,

Madagascar entered a new phase to implement the National Development Plan (PND) with the objective of reducing poverty and pursuing inclusive and sustainable development. This plan expands on the medium term challenges and strategic orientations described in the General Policy of the State (PGE), and develops the vision of "Madagascar: a modern and prosperous nation" for the period between 2015 and 2019.

The PND is articulated around five strategic pillars: (i) governance, the rule of law, decentralization, democracy and national security; (ii) maintaining macroeconomic stability and support to development; (iii) inclusive growth and territorial anchoring of development; (iv) adequate human capital for development process; (v) valuing natural capital and reinforcing resilience against the risks of catastrophes.

This letter testifies the will to meet the challenges to strengthen the performance of the tax and customs administrations for effective recovery of economic growth and to optimize the allocation of resources to sectors that have tangible impact on the population (education, health, and infrastructure).

Since its exit from the crisis, Madagascar has experienced a difficult economic environment. The economic recovery that started in 2014 has not accelerated due to a series of shocks and structural weaknesses. The harmful effects of the socio-political crisis are still evident in the social indicators despite the government's efforts to invest in the mechanisms and systems to improve human capital and social protection. The poverty rate stagnates around 71%. In 2014, 92% of the population lived below $2 a day. Access to quality health services is still limited. In parallel, the problem of under-nutrition is still chronic. In education, primary school enrollment is still low, estimated to be around 69.4% in 2014. The number of out-of-school children is estimated to be around 500,000. The country is ranked 155th out of 187 countries in the 2014 Human Development Report by the United Nations.

The economic and strategic framework of the State has been elaborated as the National Development Plan. Through this plan, the government is determined to tackle the country's urgent economic and social challenges with the support from the development partners. The resumption of cooperation with principal donors through budget support operations in 2014 and 2015 is a testimony to the development partners' commitment to help Madagascar's economic recovery.

In 2015, economic recovery remained fragile with mixed results in all sectors. They are a reflection of the investors' reticence, as well as weak supply-side response. Moreover, the volatility in the international price of nickel and the damages caused by the cyclones in the first half of 2015 contributed to a further degradation of the economic situation. The growth target of 5% for 2015 established in the PND had to be revised down to 3.2%. The secondary sector continue to be the driver of the economy with the growth rate of 8.5% thanks to the mining, energy and soft drink industries. The tertiary sector grew by 2.3% supported by the "banking" and "transport and commerce" activities.

Inflation is estimated to be around 7.6%. It results from an increase in consumer prices, especially for basic household items, due to the damages caused by the cyclones in the first half of the year. The continued depreciation of the local currency also increased the prices of imported goods.

With regard to public finance, revenue collection forecast was revised downwards to 9.9% from 11.5%. Domestic taxes represented 4.8% and customs revenues 5.2%. Customs revenues underperformed projections primarily due to (i) a decline in the prices of hydrocarbon products resulting in lower VAT collections from petroleum products; and (ii) a lower volume of imports. Domestic revenues were affected by the sluggishness of economic activity and the insufficient capacity to reduce tax frauds and evasions. The constraints of information technology is also a challenge in accessing relevant data and information in real time, which is critical in addressing tax arrears and increasing domestic revenues.

Available resources are allocated to projects and programs that have concrete impacts on the daily life of the population, which is implemented by the Supplemental Budget Law 2015. Social sectors (health, education and social protection) as well as rehabilitation and/or reconstruction of basic infrastructure were prioritized. Public expenditures also aimed at supporting economic recovery through the actions described in the National Development Plan and the Implementation Plan. The Implementation Plan is essentially oriented towards increasing the effectiveness and efficiency of the public and territorial administration, and improving the alignment of public investment program with the national priorities.

Growth forecast for 2016 is 4.3%. Investment and exports are expected to sustain such growth to initiate economic recovery. The secondary sector remains the engine of economic growth with a 4.8% rate, driven primarily by the dynamism of the export processing companies (8.0 %). Regarding the primary sector, growth is projected to be 2.5%, resulting from the actions undertaken by the Government to develop the agriculture sector. For the tertiary sector, 5.1% growth is expected, driven by increased activity in public works (9.9%).

Inflation is expected to come down to 7.2% by end-2016, based on the hypothesis of stable prices of petroleum in the international market.

The trade balance is forecast to be around 4.2% of GDP. A larger increase in imports (5.8%) is expected as economic activity picks up. Petroleum products represent 15.8% of imports. Exports are forecast to increase by 2.3%. The mining sector exports are forecast to decline by 1.7% due to the reduced activity at the large mining companies and the fall in the international prices. The rate of export cover is expected to be 85.3% compared to 88.2% the year before.

The outlook for public finance in 2016 remains realistic and will focus on maintaining macroeconomic stability, supporting socio-economic development and good governance practice. The fiscal policy will aim at increasing fiscal space through enlarging tax base and intensifying efforts to improve public expenditure efficiency.

Tax collection in 2016 is expected to achieve 10.4% of GDP. This result will be achieved through legislative and tax measures designed for immediate effects. These measures will be supported by reinforcing the system of monitoring and verification, pursuing those who are noncompliant, implementing a reliable and high-performing risk management system and strengthening monitoring of the products subject to excise taxes.

Public expenditure will be aligned with development priorities defined in the PND. The expenditure in 2016, planned to reach 16.6% of GDP, will target not only the activity which contribute to economic growth, but also those which will have a tangible impact on the life of the population. Thus, the government priorities include: (i) strengthening governance, the rule of law and establishing a fair justice (ii) improving the security of the people and properties, (iii) supporting rural development (iv) developing infrastructure, (v) strengthening food security, (vi) facilitating access to basic social services (health, education); (vii) revitalizing the energy sector and promoting renewable energies; (viii) reestablishing an attractive business climate; and (ix) developing employment generating activities. **A large share (47.3%) of the State budget will be allocated to sectors with strong socio-economic impact (education, health, infrastructure, agriculture/rural development).**

Recovery in total investment is expected. Public investment is projected to increase by 27.7% compared to the Supplementary Budget Law of 2015.

The Government is also committed to avoiding accumulating new domestic arrears and to clearing the existing stock as soon as possible. Given the size of the existing stock, an action plan to repay the existing arrears (VAT, trade payables) has already been established. Repayment has started already in 2014 and will continue until 2019. According to this plan, the arrears in the amount of Ariary 160.9 billion arising from 2014 and 2015 remain to be paid. In addition, the government is taking stock of other arrears. A committee of arrears stock-taking will be put in place. The draft regulation to create an inter-ministerial committee for arrears stock-taking and monitoring arrears clearance is ready to be signed by the relevant authorities. The stock-taking exercise is ongoing; 24 out of 32 ministries and institutions have already responded to the request for information on arrears.

<u>Public financial management reforms improve efficiency of public expenditures. As part of the long-term objective of public finance management recovery and reform, the Government will strengthen its efforts to increase efficiency and transparency in public finance</u>. To meet the identified priorities, the reform action plan will take into account the results of the PEFA self-assessment developed in 2013 and the recommendations by technical and financial partners. Among such measures is the regular publishing of monthly Treasury Operations report in the Public Treasury's website with the aim of pursuing transparence in public finance. The publication started in May 2015.

<u>The government is also committed to catching up over the next two years on the delays in presenting to the National Assembly the Final Accounts of the State Budget for the 2010 exercise onwards.</u> Those for 2009 were already adopted by the first session in 2015, those for 2010 and 2011 are submitted to the second session in 2015, while those for 2012-2014 will be submitted to the National Assembly in 2016. The Final Accounts for 2014 will be submitted to the National Assembly in 2016, in compliance with the stipulation of the Organic Law on Budget Laws.

In the medium term, macroeconomic policy should support efficiency in sectoral measures and actions. It will strive to improve predictability and provide economic actors with stable environment for their activities.

The outlook for economic growth is around 5.0% in 2017-2018, aiming at supporting inclusive and sustainable development. A stable economic environment is necessary to achieve this objective. The agriculture sector, extractive industries, and public works will contribute to this growth.

In the medium term, imports of goods and services are expected to grow at around 7.9% while exports of goods and services will expand at the rate of 5.6%. A trade deficit of 5.6% of GDP and 2.4% overall deficit is expected in 2018.

In order to ensure transparency and effectiveness of public finance, the Government has developed a Medium Term Macro-fiscal Framework 2016-2018, on which the State Budget forecasts will be based. This framework reflects the policy of economic recovery, which will be pursued until 2019.

Attaining these objectives will call for intensified domestic revenue mobilization. Net revenue collection rates will improve by 0.5% of GDP annually to achieve 11.4% in 2018, expenditure will reach 16.1% of GDP, and public investments will reach 6.9%. By allocating public expenditure rationally, tangible results will be achieved in infrastructure, agriculture, education and health to respond to national priorities. The fiscal deficit will decrease progressively to 3.0% of GDP in 2019.

A medium-term debt strategy will be developed to ensure that costs and portfolio risks of the public and external debt remain within debt sustainability limits.

Despite the moderate level of debt distress risk of Madagascar, according to the classification of the IMF and World Bank, the government will implement a mechanism to limit granting of guarantees. A decree governing guarantees is being examined by the Council of Government. Another decree will govern transferring of dedicated project accounts from commercial banks to the Central Bank of Madagascar.

For domestic debt, a new bond instrument was introduced to the domestic market in 2015. Fiary Treasury Bond (BTF) has a low minimum amount for subscribing, and is accessible to all types of lenders (households, individuals, companies, etc.). The efforts will concentrate on developing a domestic market for the future.

The Government will continue reforms to strengthen the performance of the tax and customs administrations to establish an efficient and fair tax system. Fiscal policy will focus on increasing revenues, optimal allocation of resources depending on priorities established in advance, as well as on controlling the deficit. In the short term, the focus will be on increasing tax collection and correcting the dysfunctions that are sources of distortion and imbalance.

A modern customs administration will be implemented to facilitate border crossing and moving the emphasis on *a posteriori* control. To this end, electronic procedures will be introduced to allow (i) acceleration and traceability of activities; (ii) securing the procedure to decrease the risks of fraud and usage of falsified documents; (iii) fight against corruption by reducing direct contacts between users and State agents; and (iv) professionalizing the customs agent corps. The monitoring chain will also be strengthened to improve risk management.

The tax administration plans to put in place innovative actions to optimize internal revenue mobilization. These include (i) conducting a census of potentially taxable activities; (ii) developing a cross-check mechanism, such as creation of a registry of bank accounts by individuals and companies; (iii) intensifying the use of data that have become available through the recent introduction of electronic filing of VAT to fight against possible fraud; and (iv) systematic updating of the user guide for the General Tax Code, with the aim of contributing to increase transparency and intelligibility of tax laws.

Moreover, to improve transparency on the decisions which reduce tax revenues, stock-taking exercises of tax expenditures will be conducted regularly and the list of beneficiaries, granted by the Council of Government, will be published systematically.

As regards to preventing corruption, 77 asset declarations were received by the High Constitutional Court (HCC) in 2015, including 14 members of the government under the leadership of the Prime Minister and

60 members of the Parliament (including the President of the National Assembly). The list of names of those who have filed the declaration is published on the website of the HCC, www.hcc.gov.mg.

As part of the rehabilitation of JIRAMA, the Government has established taskforces with the aim of reducing fuel leakages and improving the billing rate. JIRAMA will be restructured to comply with the law on commercial enterprises. Short term measures include the reforms to improve its management and operation, in particular to eliminate power outages. In the medium term, the Government will enhance oversight to reduce the use of fuel, in terms of both costs and volume, and to decrease the amount of electricity generated but not billed. To this effect, monitoring will be strengthened to ensure coherence between fuel inputs and electricity generated. JIRAMA will publish relevant statistics on the 19 large centers to facilitate the monitoring of the progress. The Committee examines the issues concerning electricity pricing, increasing operations efficiency, and ensuring that the statute of JIRAMA complies with the provisions of the law on commercial enterprises.

Air Madagascar is the principal pillar of tourism and one of the major foreign exchange earners as well as a provider of jobs. An audit of its 2014 financial accounts is ongoing, and the results will be published in the websites of Air Madagascar and of the Public Treasury. The audited financial accounts for 2011 through 2013 are already published in the company's website.

Air Madagascar's Executive Board named Mr. Gilles Filiatreault to the post of General Manager through a competitive process in compliance with the Law 2014-014 of September 4, 2014 on the commercial enterprises with State ownership, and with the decree 2015-849 of May 12, 2015 regarding organization of the supervising ministry and the representation by the State in the management and executive board of the enterprises with State ownership. He will have a mandate of transforming Air Madagascar into a profitable company that provides quality service to its clients.

With the aim of cleaning up the management of public expenditure, a plan to eliminate fuel subsidies at the pump was developed, to be implemented by end-2015. From January 2016, the pump price of fuel would reflect the fluctuations in the international fuel prices and exchange rates. The Government, with the support of the World Bank, is preparing for the transition to this new pricing regime.

To better manage the human resources of the State, the payroll list was reviewed. Irregularities in the payroll were corrected, and proper identification information (birthdates) are being collected for all agents. The objective of this cleaning is to ensure effectiveness of the salary expenditures and to right-size the wage bill to an acceptable level. Moreover, a reform is also ongoing to reduce the size of the deficit at the Civil and Military Pension Fund.

Implementing all the measures envisaged under the General Policy of the State and National Development Plan will enable the Government to reignite economic activity of Madagascar in the coming years. However, taking account of limited resources, the Government is seeking financial support from the World Bank in the form of budget support.

The Minister of Finance and Budget

MINISTERE DES FINANCES ET DU BUDGET

- - - - -

Ministre

- - - - -

Antananarivo, le 05 novembre 2015

Le Ministre des Finances et du Budget

à

Dr Jim Yong Kim

Banque mondiale

1818 H Street NW, Washington DC

Monsieur le Président,

Madagascar entre actuellement dans la phase de mise en œuvre du Plan National de Développement (PND) dans le but de réduire la pauvreté et d'asseoir un développement inclusif et durable. Ce plan constitue la déclinaison à moyen terme des défis et orientations stratégiques de la Politique Générale de l'Etat (PGE) et développe la vision « Madagascar une nation moderne et prospère » pour la période 2015 à 2019.

Le PND s'articule autour de cinq axes stratégiques : (i) Gouvernance, Etat de Droit, Sécurité, Décentralisation, Démocratie, Solidarité nationale, (ii) Préservation de la stabilité macroéconomique et appui au développement, (iii) Croissance inclusive et ancrage territorial du développement, (iv) Capital humain adéquat au processus de développement, (v) Valorisation du Capital naturel et renforcement de la résilience aux risques de catastrophes.

La présente lettre témoigne de la volonté à relever les défis d'une part, d'affermir la performance des administrations fiscales et douanières pour une reprise effective de la croissance économique ; et d'autre part, d'optimiser l'allocation des ressources en faveur des secteurs ayant des impacts tangibles sur la population (éducation, santé, infrastructures).

Depuis sa sortie de crise, le pays a connu un environnement économique difficile. La reprise économique qui a débuté en 2014 n'a pas pu s'accélérer en raison d'une série de chocs et de faiblesses structurelles. Les effets néfastes de la crise sociopolitique se sont encore manifestés au niveau des indicateurs sociaux malgré la volonté du gouvernement à promouvoir les mécanismes et les systèmes de valorisation du capital humain et de protection sociale. Le taux de pauvreté stagne autour de 71%. En 2014, 92% de la population vit en dessous de 2$ par jour. L'accès aux ressources de santé de qualité est encore limité. En parallèle, le problème chronique de sous-nutrition subsiste toujours. Dans le secteur de l'éducation, le taux net de scolarisation dans le primaire reste encore faible, évalué à 69,4% en 2014. Le déficit en termes de nombre d'enfants non scolarisés est estimé environ à un demi-million. Le pays occupe la 155ème place sur 187 pays du Rapport de Développement Humain 2014des Nations Unies.

Les grandes orientations économiques et stratégiques de l'Etat ont été cadrées sur le Plan national de Développement. A travers ce plan, le Gouvernement est déterminé à affronter les défis économiques et sociaux urgents du pays avec l'appui des Partenaires Techniques et Financiers. La reprise de la coopération avec l'extérieur, concrétisée par l'octroi d'aides budgétaires en 2014 et 2015 de la part des principaux Bailleurs, a témoigné la volonté des Partenaires Techniques et Financiers à soutenir Madagascar dans le processus de redressement économique.

En 2015, la reprise des activités économiques reste encore fragile et les performances par branches d'activités demeurent mitigées. Elles traduisent une prudence d'investissement des opérateurs dans les activités économiques ainsi qu'une faiblesse de l'offre. En outre, la volatilité du cours de nickel, les dégâts cycloniques au cours du premier trimestre 2015 ont aggravé la situation économique. L'objectif de croissance de 5% prévu par le PND a été ramené à 3,2% pour 2015.Le secteur secondaire continue de propulser l'économie nationale avec un taux de croissance de 8,5% grâce notamment aux industries extractives, énergie, et des boissons. Le tertiaire entend pour sa part atteindre une croissance de 2,3%, soutenue par le dynamisme affiché des branches « Banque » et « transport des marchandises.

L'inflation est évaluée à 7,9% en fin de période. Il résulte des hausses des prix à la consommation, notamment pour les PPN suite aux dégâts cycloniques du premier trimestre 2015. La dépréciation continue de la monnaie nationale joue aussi un rôle déterminant dans l'évolution des prix des produits importés.

Concernant les Finances Publiques, le taux de pression fiscale net est revu à la baisse, 9,9% contre 11,5% prévu initialement, se répartissant en 4,8% de recettes fiscales intérieures et 5,2% de recettes douanières. Concernant ces dernières, cette chute provient principalement, de (i) la réduction du cours des hydrocarbures entrainant la diminution du montant des TVA sur les produits pétroliers, et (ii) la baisse du volume des importations. Pour les recettes fiscales intérieures, le manque de dynamisme des secteurs d'activités, l'insuffisance de l'accès aux sources de recoupements potentiels pour limiter les fraudes et évasions fiscales ainsi que la limite de la capacité du système d'exploitation informatique actuel, au détriment de l'intégrité et de l'accès en temps réel aux données fiscales dont les déclarations et les arriérés fiscaux sont les principaux obstacles au recouvrement des ressources internes.

Les ressources disponibles sont allouées aux projets/programmes impactant de manière concrète sur le quotidien de la population, ce qui a amené à la mise en place de la Loi de Finances rectificatives 2015.Les secteurs sociaux (santé, éducation et protection sociale) ainsi que la réhabilitation et/ou reconstruction des infrastructures de base ont été priorisés. Les dépenses publiques visent également à appuyer la relance économique à travers la mise en œuvre des actions prioritaires énoncées dans le Plan National de Développement / Plan de Mise en Œuvre (PND/PMO).Ces dernières sont essentiellement axées sur l'augmentation de l'efficacité et de l'efficience de l'Administration publique et territoriale, et l'amélioration de l'alignement du Programme des Investissements Publics avec les priorités nationales.

Le taux de croissance escompté pour l'année 2016 est de 4,3%. L'Investissement et les Exportations devront soutenir cette croissance pour amorcer la relance économique. Le secteur secondaire, en tant que moteur de croissance, affiche un taux de 4,8%, grâce à la prépondérance des zones franches industrielles (8,0%). Pour le secteur primaire, la croissance s'établira à 2,5%. Cette situation résultera des actions entreprises par le Gouvernement en faveur du développement de la branche « Agriculture ». Concernant le secteur tertiaire, une croissance de 5,1 % est attendue, expliquée principalement par la bonne performance de la branche de BTP (9,9%).

L'inflation sera contenue à 7,2% en fin de période. Les hypothèses prennent en compte la relative stabilité du prix de pétrole brut sur le marché international.

Au niveau du commerce extérieur, la balance commerciale connaitra un déficit de 4,2% du PIB. Un accroissement plus important des importations (5,8%) sera attendu avec la reprise des activités économiques. Les produits pétroliers représenteront 15,8% des marchandises importées. L'exportation des marchandises progressera de 2,3%. Les mines connaitront une légère diminution de 1,7% compte tenu de la réduction des activités des grands projets miniers ainsi que la chute des prix sur le marché international. Le taux de couverture des exportations sera de 85,3% contre 88,2% pour l'année précédente.

Les perspectives des Finances Publiques pour 2016 resteront réalistes et se baseront sur la préservation de la stabilité macroéconomique, sur l'appui au développement socio-économique ainsi que sur la pratique de la bonne gouvernance. La politique budgétaire visera à accroître l'espace budgétaire à travers l'élargissement de l'assiette fiscale et l'intensification des efforts axés sur l'efficacité des dépenses publiques.

Le taux de pression fiscale net s'établira à 10,4% en 2016. Ceci résultera de la mise en œuvre des mesures législatives et fiscales à effets immédiats sur les recettes. Ces mesures seront appuyées par la poursuite des défaillants, le renforcement du système de contrôle et de vérification fiscale, en particuliers le renforcement du système de gestion de risques fiable et performant ainsi que le renforcement des contrôles des produits soumis aux Droits d'Accise.

La programmation des dépenses publiques s'aligne avec les priorités de développement définies dans le PND. En 2016, elles sont estimées à 16,6 du PIB et seront axées, non seulement sur les activités contribuant à la croissance économique, mais surtout sur celles qui auront des impacts tangibles sur la vie de la population. Ainsi, parmi les priorités de l'Etat, figurent : (i) le renforcement de la gouvernance, de l'Etat de droit et l'instauration d'une justice équitable ; (ii) le raffermissement de la sécurité des biens et des personnes ; (iii) le soutien au développement rural ; (iv) le développement des infrastructures ; (v) le renforcement de la sécurité alimentaire ; (vi) La facilitation de l'accès aux services sociaux de base (santé, éducation) ; (vii) la revitalisation du secteur énergie et la promotion des énergies renouvelables; (viii) le rétablissement d'un climat des affaires attrayant ; et (ix) le développement des activités favorisant la création d'emploi. Les secteurs à fort impact socio-économique seront privilégiés (éducation, santé, infrastructures, agriculture/développement rural), 47,3% du Budget de l'Etat y sera alloué.

Un redressement des investissements totaux est escompté. Par rapport à la LFR 2015, les dépenses d'investissements publics connaitront une augmentation de 27,7%.

Le Gouvernement s'engage également à éviter l'accumulation des arriérés intérieurs et à apurer le stock existant d'arriérés dans les plus brefs délais. Étant donné le montant du stock existant, un plan d'action assorti d'un calendrier pour rembourser les arriérés existants (TVA, créances fournisseurs) a déjà été établi. Le remboursement a déjà commencé en 2014 et se poursuivra jusqu'en 2019. Suivant ce plan, il reste encore 160,9 Milliards d'arriérés à honorer par le gouvernement au titre de 2014 et 2015. A cela s'ajoutent les arriérés de l'Etat qui sont actuellement en cours de recensement. Un Comité de recensement des Arriérés sera mis en place. Le projet d'Arrêté de création du Comité inter-ministériel de recensement et de suivi des arriérés de paiement est déjà élaboré et reste en attente de signature par les autorités. Par ailleurs, concernant l'état d'avancement des travaux préalables de recensement des arriérés, 24/32 Ministères et Institutions ont répondu à ce jour à la demande d'informations qui leur a été adressée et rempli le tableau de recensement s'y rapportant.

Des réformes de la Gestion des Finances Publiques rehausseraient l'efficience des dépenses publiques. Dans le cadre de l'objectif à long terme, le Gouvernement accentuera son effort pour augmenter l'efficacité et la transparence des Finances Publiques. Le plan d'actions de réforme prendra en compte des recommandations d'une part, de l'autoévaluation PEFA en 2013 et d'autre part des missions d'évaluation des Partenaires Techniques et Financiers. Parmi ces actions, figure la publication périodique de l'Opération Globale du Trésor (OGT) sur le site internet de la Direction Générale du Trésor afin de poursuivre la politique de transparence en matière de deniers publics. La publication a déjà commencé au mois de mai 2015

Le Gouvernement s'est également engagé à présenter à l'Assemblée Nationale les Lois de Règlement depuis l'année 2009 pendant les sessions ordinaires de 2015 et 2016. En effet, suivant la LOLF de 2004, les projets de Lois de Règlement doivent être soumis au Parlement au plus tard deux ans après l'année d'exécution du Budget. Celles de 2009, 2010 et 2011 sont déjà déposées au Parlement pour adoption au cours de la deuxième session 2015. Le Gouvernement prévoit de soumettre les projets de Lois de 2012, 2013, 2014 au cours des sessions parlementaires 2016. Force est de préciser que la soumission au Parlement du projet de loi de règlement 2014, laquelle interviendra en 2016, est conforme aux délais légaux prescrits par la LOLF.

A moyen terme, la politique macroéconomique devrait soutenir l'efficacité des mesures et actions sectorielles. Elle devrait tendre vers l'amélioration de la prévisibilité en offrant aux opérateurs économiques un cadre d'interventions stable.

Les perspectives de croissance économique s'établissent à une moyenne de 5,0% sur la période de 2017 à 2018, visant à soutenir le processus de développement inclusif et durable. L'atteinte de cet objectif préconise un environnement économique stable. Le secteur agricole, les industries extractives, les Bâtiments et Travaux Publics (BTP) contribuent à cette croissance.

A moyen terme, les importations de biens et services tendront à progresser avec une croissance moyenne de 7,9%. Quant aux exportations de biens et services, elles s'amélioreront à un rythme de croissance annuelle de 5,6%. Un déficit de 5,6% du PIB sera ainsi enregistré en 2018, ce qui induira au déficit de la balance globale de 2,4% pour la même période.

En vue d'assurer la transparence et l'efficacité et la transparence des Finances publiques, l'Administration Publique a établi un Cadre Macro-Budgétaire à Moyen Terme (CMBMT) 2016-2018 sur lequel se basent les prévisions du Budget de l'Etat sur la période. Ce cadre reflète la politique de relance économique qui se poursuivra jusqu'en 2019.

L'atteinte de ces objectifs nécessite la mobilisation intensive des ressources intérieures. Le taux de pression fiscale net progressera de 0,5 point en pourcentage du PIB par année pour atteindre 11,4% en 2018, les dépenses publiques atteindront 16,1% du PIB et le taux d'investissement public atteindra 6,9%.Avec une allocation rationnelle des dépenses publiques, des résultats tangibles en matière d'infrastructure, agriculture, éducation et santé sont ainsi escomptés pour répondre aux priorités nationales. Le déficit public devra diminuer d'année en année pour atteindre un objectif de 3,0% du PIB en 2019.

Une stratégie de la gestion de la dette sera élaborée afin de tenir compte des coûts et risques du portefeuille de la dette du Gouvernement Central dans les contractions d'emprunts extérieurs et intérieurs.

Malgré le niveau modéré de la soutenabilité de la dette de Madagascar, selon le classement du Fonds Monétaire International et de la Banque Mondiale, le Gouvernement mettra en place un dispositif pour règlementer l'octroi, par le Gouvernement Central, de garanties sur emprunt. A cet effet, les modalités et procédures d'octroi de ces garanties seront fixées par un décret du Conseil de Gouvernement. En outre, les modalités de gestion et de régularisation des opérations sur les comptes des projets ouverts au niveau de la Banque centrale de Madagascar devront également être arrêtées par un décret.

Pour le cas des emprunts intérieurs, un nouveau titre a été mis en place sur le marché intérieur en 2015. Il s'agit des Bons de Trésor Fihary (BTF) dont le montant minimum de souscription est accessible à tout agent économique (ménages, particuliers, sociétés, etc.). Les efforts seront concentrés sur le développement du marché intérieur pour les années à venir.

Le Gouvernement continuera les réformes pour renforcer la performance des administrations fiscales et douanières en vue de mettre en place un système fiscal efficace et équitable tout en tablant sur l'amélioration et la sécurisation des recettes fiscales. La politique budgétaire sera axée sur l'augmentation des recettes, l'allocation optimale des ressources en fonction des priorités préalablement établies, ainsi que sur la maîtrise du déficit. A court terme, l'accent sera mis sur l'augmentation des recouvrements fiscaux et la correction des dysfonctionnements, sources de distorsion et de déséquilibre.

Un système douanier moderne sera mis en place par la facilitation au niveau des frontières et plus de contrôle a posteriori. A cet effet, la dématérialisation des procédures sera renforcée pour permettre (i) l'accélération et la traçabilité des opérations, (ii) la sécurisation de la procédure pour diminuer les risques de fraude et l'utilisation de faux documents, (iii) la lutte contre la corruption pour amoindrir le contact direct entre les usagers et les agents de l'administration, (iv) la professionnalisation du métier des commissionnaires agrées en douane. Les circuits de contrôle seront également améliorés en vue d'une meilleure gestion de risque à la douane.

L'Administration Fiscale prévoit de mettre en œuvre un certain nombre d'actions innovantes pour mobiliser à l'optimum les ressources internes. Il s'agira notamment de (i)procéder au recensement général des activités potentiellement imposables, (ii) au développement des recoupements multi sources notamment la constitution de registres des comptes bancaires ouverts par les particuliers et sociétés auprès des établissements bancaires, (iii)à l'intensification de l'exploitation des données issues de la dématérialisation récente de la déclaration des annexes TVA afin de lutter contre les fraudes éventuelles ainsi que (iv)à la mise à jour systématique du guide d'application du Code Général des Impôts ,ce dernier étant afin de pouvoir contribuer à plus de transparence et l'intelligibilité des textes fiscaux.

Par ailleurs, pour assurer une meilleure transparence budgétaire des mesures fiscales dérogatoires, un inventaire des dépenses fiscales sera régulièrement effectué avec publication systématique de la liste des bénéficiaires, approuvée en Conseil de gouvernement.

Concernant la prévention de corruption, 77 déclarations de patrimoine ont été reçues au niveau de la Haute Cour Constitutionnelle en 2015 dont 14 membres du gouvernement sous le leadership du Premier Ministre et 60 députés (y compris le Président de l'Assemblée Nationale). La Liste nominative de ces déclarants est déjà publiée sur le site de HCC, www.hcc.gov.mg.

Dans le cadre des actions de redressement de la JIRAMA, le Gouvernement a mis en place des tasks forces dans l'objectif de réduire les fuites de carburants et d'améliorer le taux de facturation. La restructuration organisationnelle de la JIRAMA sera faite pour qu'elle soit conforme à la loi sur les sociétés commerciales. Les mesures à court terme incluent la réforme de la gestion et de l'exploitation, notamment pour éradiquer les délestages. A moyen terme, le Gouvernement prévoira de prendre des mesures qui tendent vers la maîtrise des charges de carburant en termes de prix et de volume, et vers la réduction de la quantité d'électricité produite et non vendue. A cet effet, les contrôles seront renforcés pour assurer la cohérence entre l'utilisation des intrants de carburant et de l'électricité produite. La JIRAMA publiera les statistiques y afférentes sur les 19 grands centres pour suivre la progression. Le comité examine, par ailleurs, les questions liées à la tarification de l'électricité, à l'augmentation de l'efficacité des opérations et à l'orientation des statuts de la JIRAMA pour être conformes aux dispositions de la Loi sur les Sociétés Commerciales.

Concernant la société Air Madagascar qui est le principal pilier du tourisme et l'un des premiers secteurs pourvoyeurs de devises et d'emplois, un audit de comptes de 2014 est actuellement en cours. Le résultat de cet audit sera publié sur le site du Trésor Public et d'AIR MADAGASCAR. Les états financiers 2011 à 2013 de la société sont consultables sur son site web.

Le Conseil d'Administration a nommé M. Gilles Filiatreault au poste de Directeur Général, à travers un processus concurrentiel conformément à la Loi n°2014-014 du 04 septembre 2014 sur les sociétés commerciales à participation Publique et au décret n°2015-849 du 12 mai 2015 portant organisation de la tutelle et de la représentation de l'Etat dans les organes de gestion et d'administration des sociétés à participation de l'Etat. Il aura comme mandat de rentabiliser les activités de la compagnie en fournissant des services de qualité aux clients.

Dans le but de renforcer l'assainissement de la gestion des dépenses publiques, un plan de réduction des subventions pétrolières a été établi avec l'objectif de l'achever avant fin 2015. A partir de janvier 2016, les prix à la pompe devraient ainsi inclure la variation des cours mondiaux et des taux de change. Le gouvernement, avec l'appui de la Banque mondiale, prépare la transition à ce nouveau régime.

Dans le domaine de la gestion des ressources humaines de l'Etat, un assainissement a été effectué pour assurer l'effectivité des dépenses de solde. La solde des agents de l'Etat en situation irrégulière a été annulée et la mise à jour des dates de naissance de tous les agents est en cours. L'objectif de cet assainissement est d'assurer l'effectivité des dépenses de solde et de ramener la masse salariale à un niveau acceptable. De plus, une réforme est également en cours afin de résorber le déficit de la Caisse de Retraite Civile et Militaire.

La mise en œuvre de toutes les actions envisagées dans le cadre de la Politique Générale de l'Etat et du Plan National de Développement permettra au Gouvernement de relancer les activités économiques de Madagascar dans les prochaines années. Toutefois, compte tenu des ressources limitées, le Gouvernement sollicite l'appui financier de la Banque Mondiale dans le cadre d'un appui budgétaire.

Le Ministre des Finances et du Budget

ANNEX 3: FUND RELATIONS ANNEX

Madagascar and IMF Mission Reach Staff-Level Agreement on Financial Assistance Under the Rapid Credit Facility and a Staff-Monitored Program

Press Release No. 15/431
September 22, 2015

End-of-Mission press releases include statements of IMF staff teams that convey preliminary findings after a visit to a country. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF's Executive Board. Based on the preliminary findings of this mission, staff will prepare a report that, subject to management approval, will be presented to the IMF's Executive Board for discussion and decision.

An International Monetary Fund (IMF) team, headed by Marshall Mills, visited Antananarivo, Madagascar, from September 9–23, 2015 and reached staff-level agreement with the Malagasy authorities on a reform program that could be supported by the IMF's Rapid Credit Facility (RCF)[1], coupled with a 6-month Staff-Monitored Program[2]. Subject to IMF management approval, the staff-level agreement on the RCF disbursement is expected to be submitted to the IMF Executive Board for its consideration in November 2015. Under the RCF arrangement, Madagascar would be able to access up to SDR 30.55 million (about US$47.4 million).

The team met with President Hery Rajaonarimampianina, Prime Minister Jean Ravelonarivo, Minister of Finance and Budget Gervais Rakotoarimanana, Minister of Economy and Planning Herilanto Raveloharison, Central Bank of Madagascar Governor Alain Rasolofondraibe, the Economic Advisor to the President Léon Rajaobelina, and other senior government officials as well as private sector representatives and development partners.

At the end of the mission, Mr. Mills issued the following statement:

"The Malagasy authorities and the IMF mission have reached staff-level agreement on a set of economic and structural policies to reinforce the progress made since the previous RCF, which was approved by the IMF Executive Board in June 2014. These policies aim to maintain macroeconomic stability, enhance fiscal and external sustainability, and strengthen the capacity of the government. Over the medium term, the key challenge remains to secure strong, sustainable, pro-poor growth to help reverse the deterioration in development indicators. This requires scaling up essential infrastructure, reforms to improve governance and the business climate, and enhanced social development policies, as reflected in the National Development Program, the National Social Protection Strategy, and the National Anti-Corruption Strategy.

"The economic environment remains challenging. The economic recovery that began in 2014 has failed to gain further momentum due to a series of shocks and deep-rooted structural weaknesses; growth is expected to reach 3.2 percent in 2015, with end-year inflation remaining contained at 7.9 percent. Sharply falling commodity prices are holding back mining revenues, while private investment remains weak in the context of the poor business climate. Tourism has been hampered by difficulties at Air Madagascar, while recurring power cuts at JIRAMA, the public utility, continue to constrain economic activity.

“To support a medium-term development program, two key objectives of the authorities’ program are to increase domestic revenue collection and enhance spending quality. These objectives are reflected in the broad outlines of the 2016 budget discussed with the authorities. New measures to improve tax administration focus on increasing compliance, deterring fraud, eliminating some exemptions, and tackling the large informal sector. To enhance the quality of expenditures, the authorities intend to, *inter alia*, eliminate fuel subsidies and continue to clean up the government’s payroll. To control transfers to state-owned enterprises, the authorities, with the support of the World Bank, will continue to tackle the problems encountered by JIRAMA and Air Madagascar. With IMF technical assistance, the authorities are also developing a framework to monitor and continue repaying arrears.

“The Central Bank of Madagascar has recently taken measures to ensure the smooth and transparent functioning of the foreign exchange market. In particular, it has discontinued buy-back operations, eliminating the wedge between the official interbank market exchange rate and the private sector market rate used for most transactions (which was 8 percent at the beginning of September). The private sector market rate has remained roughly stable. The forthcoming new draft Central Bank law will enhance the governance and independence of the Central Bank.

“In addition, based on these macroeconomic and structural policies, the Malagasy authorities and IMF staff agreed on a SMP covering the period up to the end of March 2016. Successful implementation of this program will strengthen economic stability and sustainability, provide a framework that boosts confidence and assists in catalyzing external assistance, and help lay the groundwork for a future request for an ECF arrangement.

“The mission takes this opportunity to thank the Malagasy authorities for their strong cooperation and the constructive discussions that took place.”

---

[1] The RCF (http://www.imf.org/external/np/exr/facts/rcf.htm) is a lending arrangement that provides rapid financial support in a single, up-front payout for low-income countries facing urgent financing needs.

[2] An SMP is an informal agreement between country authorities and Fund staff to monitor the implementation of the authorities’ economic program. SMPs do not entail financial assistance or endorsement by the IMF Executive Board.

IMF COMMUNICATIONS DEPARTMENT

Media Relations
E-mail: media@imf.org
Phone: 202-623-7100


MADAGASCAR
SELECTED CITIES AND TOWNS
REGION CAPITALS
NATIONAL CAPITAL
RIVERS
MAIN ROADS
RAILROADS
REGION BOUNDARIES
0 40 80 120 160 200 Kilometers
0 40 80 120 Miles
This map was produced by the Map Design Unit of The World Bank. The boundaries, colors, denominations and any other information shown on this map do not imply, on the part of The World Bank Group, any judgment on the legal status of any territory, or any endorsement or acceptance of such boundaries.
Mozambique Channel
INDIAN OCEAN
Mayotte (France)
45°E
50°E
15°S
20°S
25°S
ANTANANARIVO
DIANA
SAVA
SOFIA
BOÉNY
ANALANJIROFO
MELAKY
BETSIBOKA
ALAOTRA MANGORO
ANALAMANGA
BONGOLAVA
ITASY
ATSINANANA
VAKINANKARATRA
AMORON'I MANIA
MENABE
HAUTE-MATSIATRA
VATOVAVY-FITOVINANY
ATSIMO-ANDREFANA
IHOROMBE
ATSIMO-ATSINANANA
ANOSY
ANDROY
Antsiranana
Ambilobe
Vohimarina
Ambanja
Maromokotro (2,876 m)
Massif Tsaratanana
Bealanana
Sambava
Antalaha
Antsohihy
Befandriana
Maroantsetra
Mahajanga
Mandritsara
Mampikony
Soalala
Mananara
Besalampy
Maevatanana
Andilamena
Soanierana-Ivongo
Kandreho
Andriamena
Fenoarivo-Atsinanana
Ambatondrazaka
Andilanatoby
Maintirano
Ankazobe
Toamasina
Antsalova
Tsiroanomandidy
Miarinarivo
Moramanga
Tsiafajovona (2,642 m)
Vatomandry
Antanifotsy
Miandrivazo
Belo Tsiribihina
Antsirabe
Mahanoro
Morondava
Malaimbandy
Ambatofinandrahana
Ambositra
Vavika
Mandabe
Ambohimahasoa
Manja
Mananjary
Fianarantsoa
Morombe
Beroroha
Ankazoabo
Pic Boby (2,658 m)
Manakara
Ihosy
Farafangana
Sakaraha
Toliara
Betroka
Betioky
Midongy-Atsimo
Tsivory
Berakete
Ampanihy
Amboasary
Androka
Beloha
Ambovombe
Tolanaro
Cliff of Bongolava
Cliff of Angavo
Ankaratra
Androy Plateau
Sofia
Bemarivo
Mahavavy
Mahajamba
Betsiboka
Manambolo
Lake Alaotra
Tsiribihina
Mania
Mangoro
Mangoky
Fiherenana
Onilahy
Mananara
Mandrare
Menarandra

Press Release No. 15/528
FOR IMMEDIATE RELEASE
November 18, 2015

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$42.1 Million Disbursement Under the Rapid Credit Facility for Madagascar

On November 18, 2015, the Executive Board of the International Monetary Fund (IMF) approved a SDR 30.55 million (about US$42.1million) disbursement in financial assistance for Madagascar under the Rapid Credit Facility (RCF)[1]. This is intended to assist the authorities to meet urgent balance of payments needs. The authorities' request follows a first RCF disbursement of an equivalent amount—SDR30.55 million (about US$42.1million)—approved by the Executive Board on June 18, 2014 (see Press Release No. 14/287).

The Executive Board was also informed about the Managing Director's approval of a six-month Staff-Monitored Program (SMP) covering the period up to the end of March 2016. The SMP is intended to guide policy implementation, further develop local capacity, and build a stronger track record. A demonstrated capability to sustain reforms is a prerequisite for a future request for an arrangement under the Extended Credit Facility (ECF). The SMP in combination with the RCF disbursement are also expected to catalyze external financial assistance in 2015 and 2016.

The economic environment remains challenging. The recovery that began in 2014 has failed to gain further momentum due to falling commodity prices, weather-related shocks, and deep-rooted structural weaknesses. Against this background, private investment has also remained weak. Growth is expected to reach 3.2 percent in 2015, with end-year inflation contained at 7.9 percent.

Despite the challenges facing Madagascar, macroeconomic policies have generally succeeded in maintaining economic stability and sustainability in 2015. Going forward, the authorities have begun implementing significant measures aiming to further strengthen macroeconomic stability, particularly to improve revenue generation, enhance the quality of fiscal spending, strengthen central bank operations, and improve the functioning of the foreign exchange market. The ultimate policy objective is to scale up spending on essential

[1] The RCF (http://www.imf.org/external/np/exr/facts/rcf.htm) provides immediate financial assistance with limited conditionality to low-income countries with an urgent balance of payments need. In this context, the economic policies of a member receiving RCF financing are expected to address the underlying balance of payments difficulties and support policy objectives including macroeconomic stability and poverty reduction. Financing under the RCF carries a zero interest rate, has a grace period of 5.5 years, and a final maturity of 10 years. The Fund reviews the level of interest rates for all concessional facilities every two years.

infrastructure and social development to secure strong, sustainable, pro-poor growth that reverses the deterioration in development indicators. The government has also adopted a new strategy to fight corruption and improve governance.

New measures to improve tax administration focus on increasing compliance, deterring fraud, eliminating some exemptions, and tackling the large informal sector. To enhance the quality of expenditures, the authorities will eliminate inefficient fuel subsidies and reduce the need for transfers to loss-making state-owned enterprises, including the energy company JIRAMA and Air Madagascar. The authorities will also take actions to avoid the build-up of new domestic arrears and settle the existing stock expeditiously. The ongoing recapitalization of the central bank, revision of its legal framework, and more active bank liquidity management will reinforce the capacity to safeguard price and financial sector stability.

Following the Executive Board discussion on Madagascar's new RCF request, Mr. Furusawa, Deputy Managing Director and Acting Chair stated:

"Madagascar's economic recovery has been slower than expected as a result of falling world prices for commodity exports, weather-related shocks, and deep-rooted structural problems. Against this background, financing and balance of payments needs have grown. Nonetheless, the authorities' policies over the past six months have succeeded in broadly preserving macroeconomic stability and debt sustainability. The disbursement under the Fund's Rapid Credit Facility should help catalyze donor support.

"The government aims to raise growth and reduce poverty on a sustained basis. This will require higher public investment in physical, human, and institutional capital. Efforts to create the necessary fiscal space focus on raising the currently low level of revenue collection, combined with better spending prioritization. Stronger economic governance, including a strategy against corruption, is needed to enhance the efficiency of the public sector and improve the business climate, thereby promoting private sector-led growth. The authorities are committed to avoiding a build-up of new domestic arrears and to clearing the existing stock expeditiously. The draft 2016 budget includes welcome policy initiatives in these directions. Sustained reform efforts will be necessary to support medium-term development and mobilize additional external financing.

"The Malagasy authorities have taken steps to enhance the functioning of the foreign exchange market, maintain a flexible exchange rate, and strengthen the central bank's capacity and independence. Additional measures, including more active liquidity management, should aim to deepen the financial sector and strengthen price and financial sector stability."