



**AFRICAN DEVELOPMENT  
BANK GROUP**

## **ECONOMIC GOVERNANCE REFORM PROGRAM II (EGRP II)**

**COUNTRY: SIERRA LEONE**

**Date: July 2011**

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### **APPRAISAL REPORT**

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**Currency Equivalents  
As of May 2011**

**Sierra Leone Currency Unit = Leone (Le)**

1 Unit of Account (UA)	=	Le 6718.43
1 Unit of Account (UA)	=	USD 1.57305
1 Unit of Account (UA)	=	EUR 1.09082
1 Unit of Account (UA)	=	GBP 0.972496

**Fiscal Year  
January 1-December 31**

**WEIGHTS & MEASUREMENTS**

1 metric tonne	=	2204 pounds (lbs)
1 kilogramme (kg)	=	2.200 lbs
1 metre (m)	=	3.28 feet (ft)
1 millimetre (mm)	=	0.03937 inch (“)
1 kilometre (km)	=	0.62 mile
1 hectare (ha)	=	2.471 acres

## ACRONYMS AND ABBREVIATIONS

ACC	Anti-Corruption Commission
ADB	African Development Bank
ADF	African Development Fund
AGD	Accountant General Department
AFROSAI	African Organisation of Supreme Audit Institutions
APRM	African Peer Review Mechanism
ASSL	Audit Service Sierra Leone
ATAF	African Tax Administration Forum
BSL	Bank of Sierra Leone
CPIA	Country Policies and Institutions Assessment
DBSL	Development Budget Support Loan
DFID	Department for International Development
DRMS	Debt Recording and Management System
EC	European Commission
ECF	Extended Credit Facility
EGRP	Economic Governance Reform Program
EIA	Environmental Impact Assessment
EITI	Extractive Industry Transparency Initiative
FSF	Fragile States Facility
GBS	General Budget Support
GDP	Gross Domestic Product
GoSL	Government of Sierra Leone
GST	Goods and Services Tax
HDI	Human Development Index
HIPC	Heavily Indebted Poor Countries
IMF	International Monetary Fund
IPFMRP	Integrated Public Finance Management Reform Program
JAS	Joint Assistance Strategy
MDAs	Ministries, Departments and Agencies
MDBS	Multilateral Development Budget Support
MDG	Millennium Development Goal
MDRI	Multilateral Debt Relief Initiative
MOFED	Ministry of Finance and Economic Development
MoU	Memorandum of Understanding
MTDS	Medium-Term Debt Management Strategy
MTEF	Medium Term Expenditure Framework
PAC	Public Accounts Commission
PAF	Performance Assessment Framework
PETS	Public Expenditure Tracking Surveys
PFM	Public Finance Management
PCR	Project Completion Report
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PRSP	Poverty Reduction Strategy Paper
SLFO	Sierra Leone Field Office
WAMI	West African Monetary Institute

## GRANT INFORMATION

### Client's information

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**GRANT RECIPIENT:** Republic of Sierra Leone  
**EXECUTING AGENCY:** Ministry of Finance and Economic Development

### Financing Plan for 2011-2012

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Source	Amount in UA	Instrument
FSF	10.0 million	Grant
WB	6.2 million (USD 10.0 million)	Credit
EC	22.5 million (EUR 24.5 million)	Grant
DFID	25.7 million (GBP 25.0 million)	Grant
<b>TOTAL COST</b>	<b>58.2 million</b> <b>6.2 million</b>	<b>Grant</b> <b>Credit</b>

### FSF key financing information

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Grant currency	USD
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### Program Timeframe - Main stepping stones (expected)

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Concept Note approval	May 2011
Appraisal	May 2011
Board approval	September 2011
Effectiveness	October 2011
First Tranche Disbursement	October 2011
Government/Donors Review	April/May 2012
Second Tranche Disbursement	June 2012
Completion	June 2013

## Program Executive Summary

Paragraph	Topics to cover
Program Overview	<p><u>Program Name</u>: Sierra Leone – Economic Governance Reform Program II  <u>Geographic Scope</u>: Entire Nation  <u>Overall Timeframe</u>: 2011-2012  <u>Expected Outputs</u>: verification of teachers’ records established; system for stocktaking of recommendations of Auditor General’s report developed; EITI annual reconciliation report published; electricity tariff study completed; and a cost-driven electricity tariff formula adopted by Cabinet.</p>
Program Outcomes	<p>The program objective is to improve PFM transparency and accountability essential for inclusive economic growth and poverty reduction. The expected outcomes of the program are (i) improved fiscal discipline and efficiency/effectiveness of public expenditures; and (ii) improved revenue transparency and accountability in the energy and extractive sectors. Thus, EGRP II will contribute to improved PFM system and a robust fiduciary arrangement that ensure transparency and accountability in the use of public resources. The direct beneficiaries are Sierra Leone’s key PFM institutions; while the indirect beneficiaries are the population of Sierra Leone in general, who will benefit from better PFM system creating enhanced fiscal space for social service delivery.</p>
Needs Assessment	<p>The proposed budget support operation under the Fragile State Facility (FSF) pillar 1 for ADF-12 period is premised on the fragility of Sierra Leone’s economy and socio-political systems as a post-conflict country. Like other fragile states, the country is struggling to pay for basic state functions due to macroeconomic vulnerability and inability to raise significant revenue from domestic taxes. Budget support plays a key role in supporting macro-budgetary stability and maintaining the gains made by the successful peace process. It also minimizes otherwise constant cash pressures, which often lead to poor budget planning and execution, and enables government to deliver basic social services, including payment of staff salaries. As Sierra Leone enters into a new phase of gradual improvement, the AfDB/WB Joint Assistance Strategy (JAS, 2009-2012) for the country justified the need for budget support for governance reform programs so as to provide the basis for creating a competitive and diversified economy necessary for longer term sustainable economic growth and poverty reduction.</p>
Bank’s Added Value	<p>The proposed operation will allow continuation of reform initiated under the EGPR I and will be complemented by the institutional support project and targeted technical assistance. The Bank comparative advantage in supporting the program derives from a number of factors including: (i) the Bank being an African premier multilateral development institution with a deep knowledge of the African socio-economic setting; (ii) scaling up of the Bank’s engagement and the reorientation of its policy and institutional actions to respond to challenges in economic governance in Africa; and (iii) the Bank’s experience working with African and regional institutions such as AFROSAI, ATAF, and WAMI will serve as impetus to guide financial and governance reform. In terms of added value, the Bank’s sponsored study on the local government PEFA assessment and strengthened field presence positions it to make effective contribution to policy dialogue and implementation of PFM reforms. The Bank’s strategic support to the APRM process in Sierra Leone also provides a unique opportunity to promote country-led governance assessment.</p>
Institutional development and Knowledge building	<p>The program will contribute to institutional development and knowledge building in the areas of public financial management reform. The Bank will capture and disseminate lessons learned and good development practice through careful monitoring and evaluation of program implementation, joint PAF reviews, and Project Completion Report to inform dialogue and programming going forward.</p>

## VII. Results Based Logical Framework

**Country and project name:** Economic Governance Reform Program II (EGRP II)

**Purpose of the project:** To promote inclusive economic growth and poverty reduction through public financial management (PFM) reforms.

RESULTS CHAIN	PERFORMANCE INDICATORS			MEANS OF VERIFICATION	RISKS/MITIGATION MEASURES	
	Indicator (including CSI)	Baseline	Target			
IMPACT	<b>Impact:</b> Inclusive and sustainable economic growth and poverty reduction	GDP annual growth rate	5% GDP growth 2010.	>6.0% GDP growth	IMF ECF review reports; and PRS and MDG progress reports.	<b>Macroeconomic Risk #1:</b> Sierra Leone's vulnerability to external shocks due to its dependence on imported food and fuel as well as on primary exports. This has impacted negatively on the economy and poverty outcomes and compounded by its fragility situation. <b>Mitigation:</b> Continued implementation of fiscal and monetary policy supported by IMF program. The multi-donor budget support operations and domestic revenue reform would create the fiscal space to enable government to implement pro-poor projects that will help mitigate the pains of external shock.
		Domestic revenue/GDP ratio  Population below poverty line.  <ul style="list-style-type: none"> <li>Access to improved drinking water sources</li> <li>Under-five child mortality</li> <li>Infant mortality rate</li> <li>Net enrollment ratio primary education (Boys and girls ratio).</li> </ul>	13.3% in 2010  60% in 2008.  <ul style="list-style-type: none"> <li>50% access by 2009</li> <li>140 per 1000 births</li> <li>89 per 1000 in 2009</li> <li>Primary school enrollment: 61.7% in 2009 (1:1 girls to boys ratio)</li> </ul>	14.2% in 2013  55% in 2013  <ul style="list-style-type: none"> <li>63% access in 2013</li> <li>120 per 1000 births in 2013</li> <li>65 per 1000 in 2013</li> <li>Primary school enrollment 74% (1:1 girls to boys ratio in 2013)</li> </ul>		
OUTCOMES	<b>Outcome 1:</b> Improved fiscal discipline and efficiency/effectiveness of public expenditures.	PEFA (PI-18) Effectiveness of payroll control	PEFA (PI-18) score (D) 2010	PEFA score C by 2013 Ghost teachers eliminated	PFM reform progress report MDBS review aide memoire EITI report PCR	<b>Election risk #2.</b> As the 2012 elections approaches, there is the risk that substantial "spending" could lead to a large fiscal deficit. Election related tension could also undermine revenue performance. <b>Mitigation:</b> Donors support to election through the trust fund will help to reduce election expenses from the government budget and enhance the chances of democratic and peaceful election. The on-going dialogue on the budget, increased role of civil society organizations in budget monitoring and oversight, and budget support disbursement conditions would strengthen fiscal discipline and mitigate the potential risks of fiscal slippages during the election period.
		PI-28 Legislative scrutiny of external audit reports Scope, nature & follow-up of external audit	PEFA (PI-28) score score D+ (2010)	PEFA (PI-18) score improved to C by 2013. ASSL financial independence strengthened		
	<b>Outcome 2</b> Improved revenue transparency and accountability in the mining and energy sectors	<ul style="list-style-type: none"> <li>EITI status</li> <li>NPA financial position</li> </ul>	<ul style="list-style-type: none"> <li>EITI candidate country</li> <li>Revenue collection ratio 69% in 2010</li> </ul>	<ul style="list-style-type: none"> <li>EITI compliant by 2012</li> <li>NPA financial position improved % collection ratio increased to 98%</li> </ul>		
OUTPUTS	<b>Component 1: strengthening public expenditure management</b>					
	Output 1.1: Verification and automation of teachers records established	Number of (%) teachers files created and reconciled with master file in HRMO	35,505 teachers' files created in 2010.	50% of teachers on the payroll should have the key data on their records verified by a physical interview by December 2011 and 100% by June 2012.	PFM reform progress report HRMO file MDBS review aide memoire Supervision reports	<b>Fiduciary and implementation Risk #3:</b> Government could back slide in implementing PFM reform and

RESULTS CHAIN	PERFORMANCE INDICATORS			MEANS OF VERIFICATION	RISKS/MITIGATION MEASURES
	Indicator (including CSI)	Baseline	Target		
Output 1.2: System for stock taking of recommendations of Auditor General's report developed, and training for PAC provided	Number (%) of Auditor General's recommendation implemented	2009 audit reports finalized and submitted to PAC	2010 audit report finalized and system of stock taking of recommendations put in place.		address weaknesses in the fiduciary control environment. This can also be aggravated by the weak institutional capacity which could undermine the implementation of PFM reform program aimed at reducing the level of fiduciary risk. Mitigation: Progress against PFM reform is central to conditionality and features strongly in the PAF. Government led reform plan jointly backed by the MDBSG provides strong platform to encourage and monitor change. On-going and planned institutional capacity projects by donors will help strengthen government capacity to implement PFM reforms.
	Budget for ASSL approved by Parliament	Budget of ASSL submitted to MOED	Audit act amendment submitted to Parliament		
	Number (%) of payment vouchers presented to ASSL	Reaches 80% for 2009 audit	Payment voucher reaches 90% for 2010 audit		
<b>Component 2: Strengthening revenue governance in the mining and the energy sectors</b>					
Output 2.1: EITI implementation plan for (2011-2012) and EITI reconciliation report prepared	EITI status	EITI candidate country (2008)	EITI Compliant in 2012	EITI report MDBS aide memoire NPA financial statement	
	Report on mining revenues	2010 report on mining revenue published	Report on mining revenues collected from the 10 largest mining enterprises published		
	Draft NMA bill	N/A	NMA act approved		
Output 2.2: Tariff study completed and a cost-driven tariff formula adopted by Cabinet.	Implementation of cost driven electricity tariff	Tariff study consultant hired	Adoption and implementation of an electricity tariff formula by June 2012		
	Energy sector reform	Draft electricity and regulatory bills	Electricity and regulatory bill submitted to Parliament		
	NPA financial statement and audit report	NPA 2008 audit report published	2009 and 2010 NPA audit report published by Dec. 2011, AND 2012.		
<b>KEY ACTIVITIES</b>	<b>ACTIVITIES</b>		<b>INPUTS</b>		
	<ul style="list-style-type: none"> <li>Physical verification and automation of teachers/personnel record</li> <li>Stock taking of recommendation of the auditor general's reports</li> <li>Follow-up audit recommendations and management responses</li> <li>Prepare a 2-year EITI implementation plan, capacity building and implement community outreach activities</li> <li>Prepare and submit reconciliation report</li> <li>Finalize the preparation of the draft bills related to energy sector</li> </ul>		<ul style="list-style-type: none"> <li>Budget support - FSF Grant = UA 10 million</li> <li>Other donors/MDBS members = UA 54.4 million</li> <li>MDBS missions: supervision and policy dialogue</li> <li>Complementary capacity building project for PFM (\$2m) and FSF targeted technical assistance to teachers record (\$2m)</li> <li>Multi-donor support to Integrated Public Financial Management Reform Program (US\$ 20 million from 2009 – 2012)</li> </ul>		

## **I THE PROPOSAL**

**1.1 Management submits the following Report and Recommendation on a proposed grant to the Republic of Sierra Leone for UA 10 million from pillar I of the Fragile States Facility (FSF) to finance the second Economic Governance Reform Program (EGRP II).** The program is aligned with Sierra Leone’s Agenda for Change (PRSP II), and the AfDB/World Bank Joint Assistance Strategy (JAS) for Sierra Leone. The JAS Cover Note conceptualized Bank Group support to Sierra Leone during the period (2009-2012), and recommended the renewal of Sierra Leone’s eligibility under the Fragile States Facility (FSF) and justified the use of budget support instrument for governance reform.

**1.2 The purpose of the operation is to assist the Government in promoting inclusive economic growth and poverty reduction through PFM reforms.** The operational policy objective is to improve PFM transparency and accountability essential for inclusive economic growth and poverty reduction. It consists of two reform components: (i) strengthening public expenditure management and (ii) strengthening revenue governance in the mining and energy sectors. The expected outcomes of the program are improved fiscal discipline and efficiency/effectiveness of public expenditures, and improved revenue transparency and accountability in the mining and the energy sectors.

## **II COUNTRY AND PROGRAM CONTEXT**

### **2.1 Government overall development strategy and medium-term reform priorities**

**2.1.1 Sierra Leone’s development priorities are laid out in the PRSP-II, known as the “Agenda for Change”, whose objective is to reduce poverty through sustained economic growth.** The PRSP has four key priorities: (i) enhancing national electricity; (ii) developing the national transportation network; (iii) enhancing productivity in agriculture and fisheries; and (iv) ensuring sustainable human development. The strategy is anchored on four preconditions and principles namely, good governance, macroeconomic stability, private sector development, and management of natural resources. These preconditions and principles were designed to drive growth in the various sectors. The Government has also been implementing an Integrated Public Financial Management Reform Program (IPFMRP, 2009-2012) to promote fiscal discipline, efficient allocation and use of funds, value for money and probity in the use of public resources.

### **2.2 Recent socio-economic developments, perspectives, constraints and challenges**

#### Recent macroeconomic performance and medium term outlook

**2.2.1 Sierra Leone’s post conflict economic performance has been strong.** Post-conflict recovery continued for an eight year unbroken period, with GDP growth reaching 5.5% in 2008. Growth dipped to 3.2% in 2009 (Table 1), due to the impact of the global financial and economic crisis, which resulted in a decline in global demand for Sierra Leone’s exports and falling foreign inflows from remittances. Economic activity has started to rebound after the crisis. Real GDP growth reached 5% in 2010, driven by the growth in mining, manufacturing and agriculture outputs. Growth of mining output was led by increased diamond output (9.3%), on account of the resumption of full operation by Koidu Holdings Limited; increased bauxite output (64.2%); and increased gold output (52.6%). Growth in manufacturing output was driven by improved electricity supply to Freetown, following the commissioning of

Bumbuna hydropower station at the end of 2009; while increased output of coffee (7.2%), partly in response to the 9% rise in average world coffee prices, enhanced growth performance of the agriculture sector.

**2.2.2 Despite a strong economic performance, Sierra Leone has been facing serious economic challenges since the second half of 2010.** Though lower fuel and domestic food prices eased inflationary pressures during most of 2009, inflation jumped to 18.4% by end-2010 compared with 10.8% in 2009. This development was due to the spill-over effect of the huge depreciation of the Leone in 2009, one-off effect of the introduction of the Goods and Services Tax (GST) in January 2010, and rising fuel and food prices<sup>1</sup>. Overall fiscal deficit rose to 6.9% of GDP in 2010 from 4.7% in 2009. While budgetary expenditures were broadly on track through June 2010, fiscal policy became expansionary in the second half of the year. Spending allocations exceeded the program for the year as a whole by 2.7% of GDP, despite revenue over performance. As Government stepped up spending on infrastructure, domestically financed capital expenditure (through ways and means credit from the central bank) exceeded the budget by 1.8% of GDP. Reflecting the increase in central bank financing, broad money grew by 29% while reserve money grew much faster than anticipated (35% compared with 8% programmed). Private sector credit rose by 31% and interest rate short up to over 30%. On the external front, current account deficit (including official grants) worsened to 9.0% of GDP compared with 8.4% in 2009. Gross international reserves, which was 6.4 months of import cover in 2009 (due to IMF allocation of the equivalent of US\$128 million) fell to 5.2 months in 2010.

**2.2.3 Government has moved strongly to take corrective measures to strengthen budget discipline and bring the economic situation back on track.** In view of the expansionary fiscal and monetary policy in the second half of 2010, some key quantitative performance criteria for end-year 2010 under the IMF extended credit facility (ECF) were missed. Notably, the ceiling for net domestic bank credit to government was exceeded by 2.4% of GDP, while the target for domestic assets of the central bank was exceeded by 0.9% of GDP. The structural benchmark relating to full pass through of international fuel prices was also missed. Consequently, the IMF second review of the ECF could not be concluded as planned. Important corrective measures have since been taken including tight fiscal and monetary policy, putting less critical capital expenditure on hold, increase in fuel pump price by 30%, adoption of automatic domestic fuel pricing framework to ensure full pass through of fuel prices, and amendment of the Bank of Sierra Leone's (BSL) Act, to cap annual direct credit from the BSL to the government to 5% of previous year's domestic revenue. These measures would facilitate the satisfactory conclusion of the IMF review and bring the program back on track.

**2.2.4 The Medium term outlook for the Sierra Leonean economy is positive.** Real GDP is projected at 5.1% in 2011 and 6% in 2012 (Table 1). This projection does not however reflect the anticipated impact of the scaling up of iron-ore and diamond production on economic activities in the medium term, which the IMF estimates, could raise economic growth to around 12% in 2012 and beyond. This development will also impact positively on Sierra Leone's employment, social welfare and poverty situation. Also, growth is expected to be driven by the recent completion of the Bumbuna hydropower, investment in basic infrastructure, improved agricultural output, and initiatives directed at improving the business

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<sup>1</sup> Fuel and food price increase is likely to have both direct and indirect negative effects on the population. To mitigate the impact of the significant increase in fuel prices, especially on the urban poor, the Government plans to increase financial resources for safety net programs (e.g. cash-for-work), and the size of the public bus fleet.

climate. Demands for minerals and agricultural exports are projected to improve as global economic recovery accelerates. Expanded domestic food production and a more restrictive monetary and fiscal policy are expected to ease inflation to 8% and fiscal deficit to 4.5% of GDP by end-2012. As imports expand to cater for the investments critical to spur growth, external current account deficit would increase to 11.4% of GDP and gross foreign exchange reserves would decline to 4.5 months of import cover in 2012.

Table 1: Selected Macroeconomic Indicators, 2008-2012

Indicators	2008 Act.	2009 Act.	2010 Prel.	2011 Proj.	2012 Proj.
Real GDP (%)	5.5	3.2	5.0	5.1	6.0
Consumer Price Index - end period (%)	12.2	10.8	18.4	13.1	8.0
Overall Budget balance (% of GDP)	-4.7	-3.2	-6.9	-4.0	-4.5
Revenue (% of GDP)	11.5	11.7	13.3	13.6	13.6
Grants (% of GDP)	4.5	7.8	7.2	7.5	6.2
Total expenditure and net lending (% of GDP)	20.7	22.7	25.1	25.1	24.4
Current Account balance - incl. grants (% of GDP)	-11.7	-8.4	-9.7	-11.9	-11.4
Gross official reserves (months of import cover)*	4.4	6.4	5.2	4.7	4.5
External public debt – incl. IMF (% of GDP)	31.2	29.7	34.1	23.0	24.3

*Sources:* Sierra Leonean authorities; and IMF staff estimates and projections; November 2010.

**2.2.5 Sierra Leone reached HIPC completion point in December 2006 and subsequently benefitted from both HIPC and Multilateral Debt Relief Initiatives.** Consequently, the country's external debt was significantly reduced from about 142% of GDP at end-2005 to 32% at end-2007. Estimates for end-2010 (34.1% of GDP) and projections for 2011 (23%) and 2012 (24.3%) indicate a sustainable external debt profile. Public domestic debt, estimated at 20% of GDP at end-2010, is also quite low. Thus, Sierra Leone does not have the problem of debt distress. The GoSL is committed to debt sustainability and in this regard, intends to keep domestic financing below 2% of GDP, while external borrowing will be limited to highly concessional terms. To improve debt management, the country is in the process of developing a comprehensive Medium-Term Debt Management Strategy in line with its debt management act. It is also working to improve the quality of debt data and reporting so as to better monitor commitments, disbursements and debt service obligations.

#### Recent Developments in Poverty and Social Indicators

**2.2.6 Sierra Leone remains one of the poorest countries in the world and is unlikely to meet any of the Millennium Development Goals (MDGs) by 2015<sup>2</sup>.** Per capita income is estimated at US\$ 260 and over 60% of the population live below the poverty line in 2008. Income inequality remains relatively high with Gini coefficient estimated at 0.425 (World Bank, 2010). This calls for inclusive growth, which should be reflected in substantial pro-poor budget allocation and reduction in youth unemployment (currently estimated at about 40%), which constitutes a serious element of the poverty situation. The comparative social indicators prepared by the AfDB (Annex 1 and summarized in Table 2), show that Sierra Leone's social indicators lag behind Africa's averages in a number of cases. However, Government is making effort to improve the social indicators. In this regard, the PRSP progress reports have shown a significant shift towards pro-poor expenditures. Gender

<sup>2</sup> Only the MDG relating to HIV/AIDS, malaria and other diseases is likely to be achieved, but only with respect to HIV/AIDS since malaria and TB are still huge problems. The MDG relating to education is inconclusive due to limited information.

budgeting has also provided funds from the national budget for school feeding programs, girl-child education, as well as child and maternal health. In the area of child and maternal health, a Free Health Care Initiative has recently been introduced for children under five years, and pregnant and lactating women.

Table 2: Social indicators – Sierra Leone compared with Africa’s average

Indicator	Year	Sierra Leone	Africa
1. Population living below US\$1 per day (% of population)	2008	60.0	42.3
2. Life expectancy at birth			
Total (Years)	2010	48.2	56.0
Female (Years)	2010	43.4	57.1
3. Gross primary school enrolment			
Total (%)	2008	157.7	102.8
Female (%)	2008	148.0	99.0
4. Infant mortality rate (per 1000 live births)	2010	101.5	78.6
5. Child mortality rate (per 1000)	2010	142.6	127.2
6. Maternal mortality rate (per 100,000)	2008	970.0	530.2
7. Access to sanitation (% of population)	2008	13.0	41.0
8. Access to safe water (% of population)	2008	49.0	64.9
9. HIV/AIDS incidence (% of pop. 15-49 years)	2007	1.7	4.6

Source: AfDB – Comparative social indicators, 2010

### Recent Development in Governance

**2.2.7 Sierra Leone has made a steady progress in the area of governance.** Two general and presidential elections as well as two local government elections (in 2005 and 2007) have been successfully conducted and judged to be free and fair by international observers. Improvement in governance has also been highlighted in key governance reports, for example, the Mo Ibrahim Index, Corruption Perception Index (CPI), Voice and Accountability, and the Bank’s Country Policy and Institutional Assessment (Annex 2). However, corruption remains high as revealed by the country’s low CPI score and ranking. The fight against corruption has thus become a central thrust of government policy. In this regard, the power of the Anti-Corruption Commission (ACC) has been strengthened. The 2008 ACC Act devolves prosecutorial powers to the Commission without recourse to the Attorney General, and this effort has started to bear fruits. In 2010 alone, the Commission handled 117 cases, eight (8) of which led to convictions, including two government ministers and about Le 1.73 billion was recovered as settlement from corruption related cases. Despite the delay, the APRM and EITI implementation are underway with the aim to complete the APRM peer review and achieve the EITI compliant status in 2011 and 2012 respectively. Doing business indicators have also improved. Sierra Leone ranked 143 out of 183 countries in 2011, higher than its Mano River Union neighbors: Liberia (149), Cote D’Ivoire (168) and Guinea (173), as the country intensifies doing business reforms (Annex 3).

### Fiduciary Environment

**2.2.8 The fiduciary risk assessment (FRA) conducted by the Bank in May 2011 rates the risk as ‘substantial’ with a positive trajectory of change since 2007 (annex 4).** The FRA was based on the 2010 PEFA Assessment of the central and local governments. It concluded that the regulatory framework for PFM has been positively transformed. The biggest improvements have been in the quality and timeliness of in-year budget reports, timeliness and regularity of accounts reconciliation, and quality and timeliness of annual

financial statements. In addition, procedural innovations have been put in place for budget planning and monitoring such as the Integrated Financial Management and Information System (IFMIS), Medium-term Expenditure Framework (MTEF), District Budget Oversight Committees, and Public Expenditure Tracking Surveys.

**2.2.9 In line with the government PFM reform program, the Bank is providing a significant support to further improve transparency and accountability of the PFM system,** including targeted support to strengthen the Parliament, Audit Service Sierra Leone (ASSL), Anti-Corruption Commission (ACC), Local Councils PFM capacity strengthening, and PFM reform through the multi-donor funded IPFMRP. Government's commitment to, and ownership of, reforms are high, and emphasis has been placed on building internal capacity to continue reforms. Risk mitigation strategies are in place and a credible PFM reform plan and donor supported programs are addressing areas of weaknesses. The main mechanisms for monitoring performance of PFM improvements are: IPFMRP action plan bi-annual reviews, MDBS bi-annual reviews, ISP supervision missions, and public expenditure tracking survey. All of these mechanisms will continue to be used to monitor and mitigate risks. In line with the Guidelines for the utilisation of resources from the Fragile State Facility, further fiduciary safeguard includes the use of the budget support compliance audit by an independent audit firm.

#### Key Medium-Term Constraints and Challenges

**2.2.10 As a fragile state, Sierra Leone's development challenges are enormous.** The 2010 PEFA assessment indicate weaknesses in the PFM system. Expenditure control is constrained by ineffective payroll system, delays in follow-up on audit recommendations, and weak external scrutiny. Revenue transparency and accountability, especially in the mining and energy sectors also remain weak. Although Sierra Leone became an EITI candidate since 2008, it has to date failed to attain compliance status aimed to promote revenue transparency in the extractive sector. A non-cost reflective energy tariff, a billing system perceived to be non-transparent by consumers, and limited use of pre-paid meters constrain revenue collection. Strengthening revenue mobilization will create the fiscal space for pro-poor expenditure and enhance Sierra Leone's chances of achieving the MDGs. Poor infrastructure, especially inadequate electricity supply and poor transport system also pose significant challenges. Only 8% of roads are paved while national electricity generation capacity and electricity consumption are about the lowest in Africa. Government plans to accelerate public investments in infrastructure (roads, water, and energy), as well as reform the mining and energy sectors to enhance domestic revenue generation and transparency. The recent confirmation of offshore oil reserves presents opportunities, but may also exacerbate governance of the extractive sector. This makes improved extractive industries governance imperative, to avoid the resource curse that plagued diamond exploration in the past.

### **2.3 Bank Group Portfolio Status**

**2.3.1 The performance of the Bank Group portfolio in Sierra Leone is broadly satisfactory.** There are currently eight (8) on-going operations in the portfolio amounting to UA 98.41 million. Infrastructure accounts for 68%, Social Sector for 17%, and Agriculture for 15%. The April 2011 Country Portfolio Performance Review (based on 2010 ratings) showed improved overall rating of 2.25 (satisfactory) compared with 1.97 in 2009; Implementation Progress rating of 2.02; and Development Objective rating of 2.47. Fifty per cent (50%) of the portfolio was at risk, which though high, was an improvement over the figures in the last three years (54% in 2009, 75% in 2008 and 83.3% in 2007). There was no

outstanding PCR as at end June 2011 except the Social Action Support Project due by end June 2011. The improved portfolio performance was driven by enhanced project supervision and monitoring by SLFO. Table 3 presents portfolio performance indicators and comparison with Bank-wide average.

Table 3: Comparison of Portfolio Performance

	Sierra Leone 2009	Sierra Leone 2010	Bank-wide 2009
Disbursement ratio	27.7	37.6%	28% (18%)*
Average size of portfolio	UA 8.71 m	UA12.01m	UA24.8m (UA18.9m)*
Average supervision mission per year	1.6	2.0	1.5
Portfolio at Risk rate	54%	50%	7% (47%)*
Commitment at Risk rate	63.9%	39.9%	39%
Problematic Projects	18%	16.7%	6%
Time between approval and 1 <sup>st</sup> . Disbursement	19.6 months	13.6 months	11 months
Ageing projects	18%	0%	12%
Operations supervised twice/year	75%	78%	33%
Average age of portfolio	4.5 yrs.	3.2 yrs.	4.2 yrs.

\*ADF only.

Source: Sierra Leone: Country Portfolio Performance Review Report – An Update of 2009 Review, 4 April 2011

### **III RATIONALE, KEY DESIGN ELEMENTS AND SUSTAINABILITY**

#### **3.1 Link with the Country Strategy Paper (CSP), country readiness assessment, and analytical works underpinnings**

##### Link with the CSP

**3.1.1 The proposed operation is aligned with the AfDB/World Bank Joint Assistance Strategy (JAS) for Sierra Leone (2009-2012).** The JAS has two pillars namely: (i) Promoting Inclusive Growth (infrastructure and agribusiness); and (ii) Providing Basic Services (health, education, and social protection); with governance and private sector as cross-cutting themes. The JAS Cover Note identified governance as a key area of AfDB's support to Sierra Leone and budget support as the delivery instrument. Specifically, the proposed operation is linked with the JAS strategic objective (promoting growth and poverty reduction) and Pillar 1: outcome 6: "improved predictability, expenditure controls and transparency in public resource management". It is also consistent with the PRSP II priorities, ADF-12 operational priorities, Bank's Governance Strategic Action Plan; and the Strategy for Enhanced Engagement in Fragile States, all of which emphasise good governance as a prerequisite for economic and social stability. Table 4 illustrates the alignment of EGRP II with both the PRSP II and the JAS, while annex 5 provides other complementarities.

Table 4: Linkage of the EGRP II with the PRSP II and JAS

PRSP II	AfDB/WB JAS	EGPR II
<p><i>Strategic Objective</i> Poverty reduction through sustained economic growth, with emphasis on the private sector</p>	<p><i>Strategic Objective</i> To support Sierra Leone's growth and poverty reduction program.</p>	<p><i>Operational policy objective</i> To improve PFM transparency and accountability essential for inclusive economic growth and poverty reduction.</p>
<p><i>Priorities</i> i. Energy ii. Transportation iii. Agriculture and fisheries iv. Human development</p> <p><i>Pre-conditions/principles</i> i. Good governance ii. Macroeconomic stability iii. Private sector development iv. Management of natural resources.</p>	<p><i>AfDB/WB JAS Pillars</i> i). Inclusive growth: Infrastructure and agribusiness ii) Provision of basic services (health, education and social protection)</p> <p><i>Cross-cutting themes:</i> i) Governance – outcome 6: improve predictability, expenditure controls and transparency in public resource management ii) Private sector development</p>	<p>i). EITI implementation and mining revenue transparency ii). Macroeconomic stability iii). Strengthening PFM systems iv). Energy sector legal and institutional reform</p>

### Country Readiness Assessment

3.1.2 **Sierra Leone fulfils the eligibility criteria for fragile state facility<sup>3</sup> and the general and technical prerequisites for Development Budget Support Loan (DBSL)** as presented in Table 5. Continued support under the FSF pillar I during ADF-12, will build on the significant gains achieved under ADF 11 to strengthen Sierra Leone's growth and poverty reduction effort and help it move out of fragility.

**Table 5: A Summary Assessment of the Prerequisite Conditions of the Program**

Pre-requisite Conditions	Focus	Comments on the Current Situation
General Prerequisites:	<p>Political stability.</p> <p>(ii) Economic Stability &amp; Government's commitment.</p>	<p>(i) The political situation has continued to be stable since the end of the civil war in 2001. Two presidential and parliamentary elections have since been held (2002 and 2007), both leading to peaceful transition of government. The prevailing political situation provides a good reason for optimism that a feasible and sustainable, pluralistic democratic system is gradually being established and that the next national elections in 2012 would be peaceful and democratic.</p> <p>(ii) Sierra Leone economic stability is also gradually improving. The country has successfully implemented two <i>ECF</i> with the IMF, and is currently on the third <i>ECF</i> (2010-2013). Despite slippages in the second half of 2010, economic policies have been brought back on track as Government intensifies reforms to maintain macroeconomic stability. This would facilitate the conclusion of the IMF second <i>ECF</i> review.</p>
Technical Prerequisites	<p>(i) Existence of well-designed PRSP or NDP and effective implementation mechanism.</p> <p>(ii) Viable</p>	<p>(i) The Agenda for Change (PRSP II) covering the period 2008-2012, was formulated within a perspective of the <i>Vision 2025</i>. it was designed to address key priority areas (power, infrastructure, agriculture, education and health), which are considered vital for economic growth, poverty eradication and economic development. PRSP II benefitted from lessons learnt from implementing PRSP I, nationwide consultations and priority-setting exercise, and the growth diagnostic analysis for Sierra Leone. The feasibility of PRSP implementation is enhanced by joint government/donors monitoring and regular annual reports, which have shown a significant shift towards pro-poor expenditure.</p>

<sup>3</sup> The JAS Cover Note recommends to the Board of Directors to renew Sierra Leone's access to FSF.

	<p>macroeconomic and financial medium-term framework.</p> <p>(iii) Strong partnership between Sierra Leone and donors.</p> <p>(iv) Strong partnership among donors.</p> <p>(v) Satisfactory fiduciary review of the public financial management system (use of country system).</p>	<p>(ii). MOFED prepares an annual macroeconomic medium-term framework, which is used as an input into a three year rolling medium term expenditure framework (MTEF).</p> <p>(iii). There is a strong partnership between Sierra Leone and donors. The PRSP II and IPFMRP provide the frameworks for donor support and alignment of their interventions with government priorities. The feasibility of the existing partnership is enhanced by the existence of Government/donors platforms for regular dialogue and monitoring of the implementation of the reform agenda.</p> <p>(iv) A strong partnership among donors is evidenced by the JAS (2009-2012) between the AfDB and the World Bank; and a strategy paper (2008-2013) between the EU and the DFID. Other important developments include joint missions, MoU on Multi-Donor Budget Support (MDBS), and joint ESW (e.g. PEFA).</p> <p>(v) The government has developed, together with donors, a medium-term PFM Reform Program (i.e. IPFMRP), informed by a baseline PEFA assessment. The bi-annual assessments by the MDBS partners of the PAF constitute satisfactory fiduciary reviews. The GoSL in conjunction with its development partners (including the Bank) has carried out PEFA assessment to examine the PFM performance and progress made since 2007. The Bank also conducted a fiduciary risk assessment including mitigation measures (para. 2.2.9 and 2.2.10) in May 2011 based on the findings of the PEFA assessments.</p>
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### Analytical Works Underpinnings

**3.1.3 The design of the budget support operation has been guided by various analytical diagnostic works. In addition, consultations were also held during the appraisal mission with government officials, the civil society organisations, the private sector actors and the development partners.** The 2010 PEFA Assessment (Annex 4) constitutes the major underpinning analytical work for the operation. Others are the OPEV evaluation of policy based operations (2010), the AfDB/World Bank Common Approach Paper<sup>4</sup> (2011), EITI reconciliation and validation reports (2010), the PCRs of Bank-supported policy based operations in Sierra Leone, and IMF reports. Important conclusions from these upstream studies are as follows:

- Overall, the regulatory framework for PFM has been positively transformed<sup>5</sup> but some challenges still remain especially in the areas of effectiveness in the collection of taxes, effectiveness of payroll controls, effectiveness of internal audit, and legislative scrutiny of audit reports (PEFA Assessment and IMF report).
- The Bank should identify potential synergies and contributions that it can make through policy dialogue or complementary activities as well as synergies between Bank's portfolio in a country and cross-sector needs, and these should be explicitly built into Policy Based Operations. Consideration should also be given to ensuring that sufficient capacity and resources are available (for instance in Field Offices) to enable these contributions to be made effectively. The Bank should also develop a medium-term framework for the provision of budget support that can provide a more streamlined and predictable approach (OPEV report).

<sup>4</sup> Providing Budget Aid in Situations of Fragility", prepared in consultation with the IMF and EC, and in which Sierra Leone was a case study.

<sup>5</sup> The 2010 scores for the 31 indicators were A (3), B/B+ (6), C/C+ (12), D/D+ (9) and no score (1) as against the 2007 scores of A (2), B/B+ (4), C/C+ (14), D/D+ (9) and no score (2).

- Budget support, in combination with other aid instruments, plays a key role in underpinning fragile social and political processes and in supporting macro-budgetary stability. A common approach is needed to strengthen donor coordination, improve aid predictability and enhance risk management (Common Approach Paper).
- Sierra Leone has been a candidate of the EITI since 2008, but it has failed to attain compliance status so far because of weaknesses in governance within the mining sector, particularly in terms of the legal framework of agreements and contracts for exploiting mineral resources (EITI reconciliation and validation reports).

**3.1.4 The analytical reports and consultations have helped to shape the objective and focus of the operation.** On the basis of these diagnostic works and consultations, the appraisal team took key decisions relating to the components of the operation, risk management, front loading disbursement to meet government resource needs in 2011, and strengthening the mining and energy sectors governance in view of its potential for growth and poverty reduction.

## 3.2 Collaboration and coordination with other donors

**3.2.1 A Partnership Framework for a common approach to budget support has been developed to strengthen collaboration among MDBS partners.** The GoSL concluded in 2006, a Memorandum of Understanding (MoU)<sup>6</sup> with four major budget support partners namely, AfDB, World Bank, EC and DFID. The MDBS partners and government have agreed to consolidate the benchmarks into a single Performance Assessment Framework (PAF, 2011-2013)<sup>7</sup> [Appendix 2]. Progress against PAF targets are jointly monitored through annual and mid-term reviews. The EC and DFID budget support operations focus on social sector and civil service reform, but they base the disbursement of their variable tranche on satisfactory fulfilment of all benchmarks in the PAF using a point system. Each benchmark has equal point and the amount disbursed depends on the number of benchmarks satisfied. The focus of the World Bank budget support operation is procurement, budget formulation and execution and energy sector (tariff study), but it also supports infrastructure and private sector development. The AfDB's budget support operation complements those of the other partners by focussing on expenditure management (payroll and external oversight) and revenue transparency governance in the mining and energy sectors. Unlike the EC and DFID, the World Bank and AfDB have no fixed/variable tranche dichotomy and they base their tranche disbursements on satisfaction of specific benchmarks in the PAF consistent with their areas of focus. The Bank's budget support operation is designed and will be implemented within this common arrangement. Table 6 presents more information on the budget support operations of the IMF and other MDBS partners.

Table 6: Budget support operations of IMF and the other MDBS partners

Partner	Period	Amount (million)	Features	Amount Disbursed as at 15 June 2011
IMF	2010-2013	Third ECF SDR 31.11	SDR 4.4 million per tranche after each successful review	SDR 8.8 million
World Bank	2010-2012	USD 10.0 per Year	Disbursed after board approval upon the satisfaction of specific prior actions. 2011 BSO to be prepared in the fourth quarter of 2011	USD 10 million for 2010 was disbursed in October 2010.
EC	2011	EUR 11.5	Fixed tranche: EUR 9.0m Variable tranche:	EUR 9.0 m. fixed

<sup>6</sup> "Partnership Framework for a Common Approach to a Multi-Donor Budget Support".

<sup>7</sup> The PAF comprises 10 benchmarks and 22 indicators.

	2012-2014	EUR 14.0 per Year	EUR 1.5m Fixed Tranche : EUR 8 m Variable Tranche* : EUR 6 m	tranche disbursed
DFID	2011	GBP 15.0	Fixed Tranche: GBP 10 m Variable Tranche*: GBP 5 m	GBP 10.0 m disbursed
	2012	GBP 10.0	Fixed/variable tranche	

### 3.3 Outcomes of Past and On-going Similar Operations and Lessons

**3.3.1 The design of this operation has benefitted from lessons learnt from the past Bank-supported policy-based operations in Sierra Leone and OPEV assessments.** Table 7 summarizes the main lessons and how they have been incorporated into the new operation while annex 6 details.

Table 7: Lessons learned from past Bank-supported policy based operations

Lessons learned	Actions taken to integrate lessons into the PCN
(i) The significance of country ownership and commitment and the need to anchor the program on the country's development strategy to ensure successful program implementation.	The proposed operation is based on Agenda for Change (PRSP.II) and the IPFMRP, both of which identify good governance as key to growth and poverty reduction.
(ii) Importance of focusing on few but crucial reform priorities and performance indicators for monitoring results. Disbursement triggers should be realistic, giving consideration to the policy environment and the feasibility of legal changes.	The proposed operation has two main components with the aim to consolidate/build on the achievements of the first budget support operation. The selection of disbursement triggers are guided by the PAF and lessons learnt from the previous operation.
(iii) Value of working in collaboration and coordination with development partners to ensure successful program execution.	The operation is developed in collaboration with MDBS partners in the context of the common approach and PAF, jointly developed by the GoSL and the MDBS partners.
(iv) Need to address capacity constraints in program implementation.	A complementary capacity building project is being developed to strengthen implementation capacity of MOFED and other key PFM institutions, and to address potential fiduciary risks thereby enhancing the prospects of program development outcomes.
(v) The need for a strong monitoring and evaluation (M&E) system as an integral part of program implementation.	The operation will utilize country M&E system, which was successfully used for the first budget support operation. The SLFO, which participated in the design of the operation, will play a lead role in program implementation monitoring in the context of the common approach.
There should be synergies between Bank's portfolio in a country and cross country needs.	This operation includes a component on mining and energy sector governance to strengthen multi-sectoral approach to budget support.

### 3.4 Relationship to on-going Bank's operations

**3.4.1 This operation has a strong relationship with the other Bank Group funded operations in Sierra Leone (Annex 6).** The proposed operation will allow the continuation of reform initiated under the EGRP I and complemented by capacity building project which is being designed concurrently, and regional integration initiatives (e.g. WAMZ payment system) to consolidate transparency and accountability in the management of public resources. The capacity building project has components on extractive industries governance and strengthening of the capacity of local councils and accountability institutions (ASSL and ACC), which are a key focus of the budget support operation and address risk mitigation of EGRP II. The Bank has also approved a Technical Assistance (TA) grant under FSF Pillar III to assist with the verification of Teachers' payroll and is the process of preparing TA to

strengthen the oversight function of the Public Account Committee (PAC) of Parliament. In terms of its relationship with the general Bank's portfolio, the proposed operation will enhance the fiscal space to sustain Bank-funded development projects in Sierra Leone. By strengthening PFM and providing fiscal space to cover recurrent and capital expenditures, the proposed operation will help improve the efficiency of sector spending and the effectiveness of the on-going Bank sector operations in Sierra Leone, particularly infrastructure (energy, water and sanitation); and social sector (health and education). Specifically, there is synergy with Bank's investment in the energy sector, as the work on institutional reform and electricity tariff is part of ensuring a coherent and comprehensive support to the energy sector.

### 3.5 Bank's Comparative Advantages and Added Value

**3.5.1 The proposed operation will build on the first budget support operation and complement other donors' budget support programs in Sierra Leone.** The Bank comparative advantage in supporting the program derives from a number of factors including: (i) the Bank being an African premier multilateral development institution with a deep knowledge of the African socio-economic setting; (ii) scaling up of the Bank's engagement and the reorientation of its policy and institutional actions to respond to challenges in economic governance in Africa; (iii) the Bank's experience working with African and regional institutions such as AFROSAI, ATAF, and WAMI will serve as impetus to guide financial and governance reform. In terms of added value, the operation will promote economic growth. The Bank's strengthened field presence positions it to make effective contribution to policy dialogue and implementation of reforms; while the Bank's support to APRM provides a unique opportunity to promote country-led governance assessment and generate knowledge on governance to better inform policy dialogue and reform implementation.

### 3.6 Application of Good Practice Principles on Conditionality

**3.6.1 The program, including the design of conditionality, applies the good practice principles on conditionality (Box 1).** The Bank has consulted the IMF, World Bank, EC and DFID who have been providing budget support to ensure coordination and synergy.

#### Box 1: Application of good practice principles on conditionality

**Principle 1: Reinforce Ownership:** The proposed budget support program supports the Government's "Agenda for Change" (PRSP.II) endorsed by donors in 2008, whose objective is to reduce poverty through sustained growth with emphasis on the private sector. The Agenda for Change is based on lessons learnt from PRSP I; nationwide consultations and priority-setting exercise; and the growth diagnostic analysis for Sierra Leone. The operation is also consistent with the Government's Integrated Public Financial Management Reform Programme (IPFMRP), 2009-2012; and disbursement triggers are drawn from a PAF agreed with the Government by the MDDBS partners. Thus, the operation reinforces country ownership.

**Principle 2: Agree up front with the government and other development partners on a coordinated accountability framework:** The GoSL and the MDDBS partners agreed on a PAF, which is a coordinated accountability framework for the joint monitoring of the budget support program, based on benchmarks derived from the PRSP. The PAF is periodically jointly reviewed by the Government and donors and amended as appropriate. The Public Financial Management Reform Unit (PFMRU) in MOFED has responsible for reform implementation. The Government and donors have instituted an MDDBS platform which monitors the implementation of budget support operations. The periodic review of the IMF-supported ECF provides opportunities for monitoring the macroeconomic situation, while the regular PEFA assessments provide opportunity to monitor targets against baseline.

**Principle 3: *Customize the accountability framework and modalities of Bank support to country circumstances:*** Under the MDBS platform, triggers for budget support operations has been consolidated into a single PAF (2011-2013), to reduce transaction cost. Progress against the PAF is assessed through annual and mid-term reviews. The disbursement triggers of the Bank’s budget support operation are drawn from the PAF.

**Principle 4: *Choose only actions critical for achieving results as conditions for disbursement:*** Each tranche is subject to a maximum of three disbursement benchmarks or triggers. These triggers are chosen on the basis of their importance for the achievement of the operational policy objectives the Bank’s operation and the strategic objectives of the PRSP, as well as policies or institutional actions aimed to improve the country’s fiduciary environment as well as expenditure and revenue management, which are the two components of the program.

**Principle 5: *Conduct transparent progress reviews conducive to predictable and performance-based financial support:*** A PFM Oversight Committee, headed by the Finance Secretary, has overall responsible for strategic oversight and monitoring of the reform program. Progress against the PFM action plan is monitored jointly by Government and donors through quarterly oversight meetings, while the MDBS partners conduct annual and mid-term reviews of the PAF.

### **3.7 Application of Bank Group policy on non-concessional borrowing and debt accumulation**

3.7.1 **The EGRP fully complies with the Bank Group policy on non-concessional borrowing and debt accumulation**, whose purpose is to discourage countries that have benefitted from debt relief under HIPC and MDRI from accumulating further debt. The Government is fully committed to borrow only from highly concessional sources, guided by its Debt Management Act<sup>8</sup>.

## **IV. THE PROPOSED PROGRAM**

### **4.1 Program Goal and Purpose**

4.1.1 The goal of the program is to assist the Government in promoting inclusive economic growth and poverty reduction through PFM reform. A sound PFM system will contribute to improved transparency and efficiency in the use of public resources as well as create the fiscal space for enhanced pro-poor expenditure and social service delivery in line with PRSP priorities with huge positive social benefits. The proposed budget support operation focuses on two components namely: (i) strengthening public expenditure management, and (ii) strengthening revenue governance in the mining and energy sectors. The program’s operational policy objective is to improve PFM transparency and accountability essential for promoting inclusive economic growth and poverty reduction. EGRP II builds on the results of EGRP I taking account of outstanding areas of PFM reform indicated in the 2010 PEFA and the PCR of EGRP I.

### **4.2 Program pillars, operational objectives and expected results**

4.2.1 **Component I: Strengthening public expenditure management:** This component covers aspects of public expenditure relating to payroll control and external scrutiny.

<sup>8</sup> ADB provided technical assistance for the preparation of the draft bill leading to the Act.

### ***Sub-component 1.1: Effectiveness of payroll control***

4.2.2 As part of the civil service and financial management reform aimed to tighten expenditure control, Government has embarked on bio-metric verification of payrolls in MDAs with the aim to address weaknesses in the payroll system in terms of completeness and accuracy of personnel records and database, including the existence of ghost employees and payroll related fraud. Some progress has been made in this regard. The civil service payroll bio-metric verification has been completed, resulting in the reduction of staff on the payroll from 16,000 to 12,000 and salary savings of 500 million Leones per month. The health sector payroll verification has also been successfully completed leading to hiring of more staff to manage the health services with positive implications for social benefits. The next challenge is ensuring the integrity of teachers' payroll, since teachers constitute about 50% of public employees. The problem with teachers' payroll was reflected in the poor score (D+) of effectiveness of payroll controls (PI-18) in both 2007 and 2010 PEFA Assessment. The integrity of teachers' payroll is significantly undermined by lack of complete personnel records and personnel database as well as existence of anomalous files. Although files have now been created for all the 35,505 teachers, payroll integrity can only be maintained when physical verification of teachers is carried out.

4.2.3 The Bank's operation will support this physical verification exercise in the context of the effort and plan of the Government to put teachers' record in order and maintain the integrity of teachers' payroll system including updating of records in teachers' files and reconciling all files with the master file held by Human Resource Management Office and with IFMIS. The operation will also support the plan of the Government to establish the Teachers' Commission which will have responsibility for maintaining the teachers' records and sustaining effective management of the work force and payroll control. The expected outcome of the Bank's support is enhanced integrity of payroll and accountability in personnel record keeping and audit trails, and elimination of ghost teachers. Effective management of the teaching workforce will impact positively on the standard of education and enhance the social benefits from the education sector.

### ***Sub-component 1.2: External Scrutiny***

4.2.4 Progress has been made with respect to timely preparation of financial statements and auditing. The audit of 2009 financial statements has been completed while that of the 2010 commenced in April 2011. The PEFA scores for indicators regarding accounting, recording and reporting improved in 2010 compared to the 2007 scores, but there are still concerns in the area of follow-up of audit recommendation and external scrutiny, as well as financial independence of ASSL. To enhance financial independence of the ASSL, the Audit Act needs to be amended to enable ASSL to retain revenue (audit fees and charges) from audits of parastatals and projects. Though progress is being made with respect to parliamentary review of the audit reports, including holding of public hearings, delays in consideration of the Auditor General's reports and follow up on the recommendations of the PAC remain a weak link in overall scrutiny and oversight. The 2010 PEFA assessment indicates that while the score of PI-26 (scope, nature and follow-up of external audit) improved from D+ to C, the score for PI-27 and PI-28 (legislative scrutiny of annual budget and audit reports) remained unchanged (i.e. C+ and D+ respectively) in both 2007 and 2010. The Government has started to address this problem through collaboration among the Auditor General, PAC, Attorney General and Accountant General.

4.2.5 The Bank's operation will support the effort and plan of the Government to: (i) put in place a system in ASSL for tracking of the follow-up of audit recommendations, (ii) improve the share of payment vouchers presented by the AGD to the ASSL team auditing the 2010

and 2011 annual public accounts, (iii) amendment of audit act to enhance financial independence of ASSL, and (iv) ensure that defaulters are held accountable including sanctions. The expected outcome of the Bank's support is enhanced external scrutiny leading to improved accountability in the management of public resources.

**4.2.6 Component 2: Strengthening revenue governance in the mining and energy sectors.** This component covers improving revenue management in the mining and energy sectors.

***Sub-component 2.1: Improving transparency and accountability of mining sector revenue:***

4.2.7 The mining sector is a key growth driver of the Sierra Leonean economy and a major source of revenue to the Government. Recent estimates by USAID indicate that the mining sector contributes 20% of GDP, 8% of government revenue and about 90% of total exports<sup>9</sup>. There are also huge social benefits in terms of potential employment opportunities and improved income generation with increased investments in the mining sector. The Government is committed to ensure the maximum utilization of Sierra Leone's huge mineral potential for the benefit of the population. To this end, all mining agreements have been reviewed with a view to increasing the contribution of the sector to socio-economic development. A new Mines and Mineral Act has also been enacted to guide government intervention in the sector. However, for these benefits to fully accrue to the country there is the need to strengthen transparency and accountability of extractive sector management including contracting and revenue management. The Government has developed a transformation plan that includes restructuring of the Ministry of Mineral Resources and establishment of a National Minerals Agency to better strengthen government capacity to manage and improve governance in the extractive sector. Sierra Leone became an EITI candidate country in February 2008; the first EITI Report (covering 2006-07) was published in March 2010; and the final validation report was issued in August 2010. The reconciliation and validation reports contain a number of recommendations for improving revenue management and to help Sierra Leone achieve compliant status in 2012.

4.2.8 The Bank's operation will support the effort and plan of the Government to accelerate the implementation of (i) the recommendations of the EITI reconciliation and validation reports, (ii) SL-EITI annual work plan, (iii) disclosure of the mining sector revenue in line with its commitment to the 2009 Mines and Minerals Act, (iv) disclosure, on a yearly basis, of disaggregated figures on mining revenues (licenses, royalties, withholding tax, etc) from the 10 largest mining companies; and (iv) the Ministry of Mineral Resources institutional reform. The expected outcome of the operation is enhanced transparency and accountability in the Extractive Industries to ensure that the full benefit of revenue from the sector accrues to the Government and people of Sierra Leone.

***Sub-component 2.2: Improving revenue management in the energy sector:***

4.2.9 The energy sector also constitutes an important growth driver for the Sierra Leonean economy in terms of spurring growth in the productive sectors. The improved electricity supply to Freetown, following the commissioning of Bumbuna hydropower plant at the end of 2009, enhanced the growth performance of the manufacturing sector in 2010, with positive impact on social benefits in terms of employment generation and welfare improvement.

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<sup>9</sup> However, as a result of many channels through which revenue streams flow from the mining sector to Government, it is difficult to accurately determine the sector's contribution to public revenue.

However, there are still considerable challenges in the sub-sector including low generating capacity, rising transmission and distribution losses, (about 45% system losses in 2008), and poor revenue collection and billing system. Electricity tariffs are among the highest in the region<sup>10</sup>, yet the National Power Authority (NPA) is in considerable financial distress because of high technical, non-technical and commercial losses, exacerbated further by accumulated arrears. Energy supply and access remain a problem despite completion of the Bumbuna hydropower station. A more cost reflective electricity tariff would provide performance-based incentives to improve transparency in billing and revenue collection, make energy more affordable and encourage consumers to pay. A more wide-spread use of pre-paid meters, which is currently limited to some 40,000 units, would further enhance transparency and facilitate revenue collection. Government has embarked on energy sector reform to improve the performance of the sector and increase access to electricity nationwide. In this context, Government published a National Energy Policy and Strategic Plan in September 2009, and has also prepared the Energy and Water Regulatory Bill, the Electricity Bill, and the Rural Energy Agency Bill. These bills, when enacted into laws, will provide the legal basis for the restructuring of the NPA, especially its unbundling into an Energy Generation and Transmission Company, and a Distribution Company; and the rationalization of electricity tariff. With the World Bank's assistance, a consultant has started work on electricity tariff study, which will provide an analytical basis for the adoption of a cost-reflective tariff formula. The study is expected to be completed before the end of 2011 while the new tariff formula is expected to be adopted by Cabinet in the first half of 2012.

4.2.10 The Bank's operation will support the effort and plan of the Government to: (i) restructure the power sector including a policy commitment to reform the NPA; (ii) submit to Parliament the necessary legislations related to energy sector reform, (iii) establish the regulatory and utility companies as per the energy policy and legislations; (iv) complete the electricity tariff study to provide the methodology and guidance on tariff setting; (v) adopt and implement an electricity tariff derived from the completed tariff study and measures to reduce the technical and non-technical losses related to the operation of the NPA; and (vi) expand the installation and use of pre-paid meters to bring down losses and improve revenue collection rates. The expected outcomes of the Bank's support are improved energy sector governance; restructured and modernized NPA significantly improving on its revenue and financial viability; and enhanced legal and institutional framework for better performance of the energy sector.

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<sup>10</sup> Current electricity tariff rates are roughly USD 0.31/kWh for domestic customers and USD 0.41-0.54/kWh for commercial and industrial customers.

### 4.3 Financing Needs and Arrangements

4.3.1 The proposed budget support operation is part of the external financing sources (Table 8) that will help close the 2011-2012 financing gap.

Table 8: Projected Financing requirements and sources, 2011 and 2012 (in billion Leones)

	2010 Prel.	2011 Proj.	2012 Proj.
<b>Total Revenue and grant</b>	<b>1550.2</b>	<b>1,748.6</b>	<b>2053.7</b>
<b>Domestic Revenue</b>	<b>1,007.6</b>	<b>1156.6</b>	<b>1413.1</b>
Income Tax	303.0	296.6	329.3
Goods and Service Tax	246.4	299.0	365.4
Customs and Excise	329.9	387.3	473.2
Mines Department	24.2	64.7	86.0
Other Non-Tax Revenue	52.1	71.2	79.9
Road User Charges	52.0	64.8	79.2
<b>External Grants</b>	<b>542.6</b>	<b>591.0</b>	<b>640.7</b>
Program Grants	265.4	198.9	216.1
Debt relief	47.6	20.0	20.8
External Budget support	217.9	178.9	195.3
DFID	78.4	82.0	92.7
EC	110.9	55.4	59.8
AfDB	28.5	41.5	42.8
Peace Building Fund	0.9	44.4	76.2
Project Grants	276.3	347.7	348.4
<b>Expenditure and net lending</b>	<b>2073.8</b>	<b>2239.7</b>	<b>2558.4</b>
<b>Overall balance</b>	<b>(523.5)</b>	<b>(492.1)</b>	<b>(504.7)</b>
<b>Financing</b>	<b>523.5</b>	<b>492.1</b>	<b>504.7</b>
<b>External financing (net)</b>	<b>161.7</b>	<b>271.3</b>	<b>300.4</b>
Project Loans	155.0	304.2	334.6
Program Loans from WB	67.5	41.1	29.6
Amortization	(60.8)	(74.0)	(63.8)
<b>Domestic Financing (net)</b>	<b>361.8</b>	<b>220.8</b>	<b>204.3</b>
<b>Financing gap</b>	<b>0</b>	<b>0</b>	<b>0</b>

Source: Sierra Leone MOFED Budget Bureaus, June 2011

### 4.4 Beneficiaries of the Program

4.4.1 The EGRP is designed to assist the GoSL to implement its Poverty Reduction Strategy and the integrated PFM reform program. The direct beneficiaries are Sierra Leonean key public institutions of PFM responsible for fiduciary control. The indirect beneficiaries are the population of Sierra Leone in general, who will benefit from better public financial management and improved fiscal space for pro-poor budgetary allocation for social services delivery, thus enhancing social benefits for the population.

### 4.5 Impact on Gender

4.5.1 The operation will have a positive impact on gender equity, which remains a major concern in Sierra Leone. The Bank's Gender Profile for Sierra Leone shows that women constitute 51.3% of the population but are generally less empowered than men and are underrepresented in public and political life as well as in formal sector employment. The proportion of women holding seats in parliament is 13.7%, cabinet ministers is 10%, deputy

ministers is 13.1%, and women local government councillors is 25%. There is therefore the need for more effort to improve gender equality. At the international level, Sierra Leone has ratified the Convention on the Elimination of Discrimination Against Women (CEDAW) and is a signatory to the Solemn Declaration on Gender Equality in Africa and the Beijing Platform for Action. At the national level, it has adopted the Gender Mainstreaming Policy and the National Policy on the Advancement of Women, both of which aim to create an enabling environment to improve women's status and participation in the development process. The President has also promised to institute a gender quota in the 2012-17 electoral cycle and abide by women demand for a 30% quota in Parliament and other significant areas of governance.

4.5.2 Through direct provision of resources into the national budget, the proposed operation will support government effort and plan to enhance gender budgeting and gender mainstreaming into development programs. Specifically, the complementary institutional support project will support training in gender budgeting, which Government has initiated to facilitate a gendered analysis in the formulation of government budgets and allocation of resources. A gender budgeting committee, made up of 15 stakeholders drawn from MDAs has been set up. The program in the mining and energy sectors will also have a positive impact on women employment and income generation opportunities.

#### **4.6 Environmental Impacts**

4.6.1 **The EGRP II is classified as category III according to the Bank's procedure for the environmental and social impact assessment.** The operation therefore has no adverse impact on the environment and natural resources. It could however have indirect environmental impact since increased investments in the mining and energy sectors, due to reform and efficiency gains will have implications for the environment, including climate change impact. The Environmental Protection Authority of Sierra Leone makes it mandatory for all projects that fall within Environmental Impact Assessment (EIA) categories to obtain EIA's licence. Government has also undertaken an initial assessment of climate change impact in the country, and has prepared the first communication, containing vulnerability assessment and mitigation measures. By providing resources directly into the budget to implement the PRSP, the Bank's operation will support the effort and plan of the Government towards environmental sustainability, thereby having a positive environmental impact. In addition, the complementary institutional support project will provide support to strengthen national capacity to undertake environmental audit.

### **V. IMPLEMENTATION, MONITORING AND EVALUATION**

#### **5.1 Implementation Arrangements**

5.1.1 Implementation institutional framework: The Ministry of Finance and Economic Development (MOFED) will have overall responsibility for implementing the reform program supported by EGRP II. MOFED has adequate capacity to implement EGRP II as demonstrated by the implementation of the EGRP I. To further enhance capacity, MOFED has embarked on capacity development of MDAs in key disciplines such as procurement and internal audit.

5.1.2 Disbursement: The proposed grant of UA10 million will be disbursed in two tranches in 2011 and 2012, upon satisfactory fulfilment of disbursement triggers drawn from the PAF.

The first tranche of UA 6.0 million is planned to be disbursed in October 2011; and the second tranche of UA4.0 million in June 2012. The disbursement schedule takes into account the requirements of cash flow by the Government and the need to improve predictability. The proceeds of the grants will be deposited into a Consolidated Revenue Fund held at the Bank of Sierra Leone in the name of the Ministry of Finance and Economic Development.

5.1.3 **Procurement:** The procurement arrangements for activities implemented under the operation will be undertaken using country systems. The findings of the CPAR, PEFA and MDDBS review mission revealed that Sierra Leone has made significant progress in developing a sound procurement system, including the revision of the National Procurement Act and the establishment of a procurement cadre. There have also been improvements in the Quality of procurement plans submitted by MDAs and the share of procurement contracts going through competitive bidding that are above the threshold.

5.1.4 **Audit:** The audit arrangements will be undertaken by an independent external audit firm in line with the standard Bank's ToRs. This is in conformity with the guidelines of the utilization of resources from the Fragile State Facility, and constitutes an additional fiduciary safeguard.

## 5.2 Monitoring and Evaluation Arrangements

5.2.1 **The Bank's operation will utilize the existing national monitoring and evaluation system.** There are government-donors platforms in place for policy dialogue and monitoring and evaluation of the PRSP, PFM Action Plan and budget support operations. The MDDBS PAF review is undertaken in conjunction with the Government bi-annually. The SLFO will play a significant role in the monitoring and evaluation process. A project completion report will be prepared at the end of the program in 2012 to evaluate progress against outputs and outcomes and draw lessons for follow-up operation.

## VI. LEGAL DOCUMENTATION AND AUTHORITY

### 6.1 Legal documentation

6.1.1 Grant Protocol of Agreement between the African Development Fund and the Republic of Sierra Leone.

### 6.2 Conditions associated with Bank Group intervention

**6.2.1 Entry into force of the Grant Agreement:** The grant protocol of agreement shall enter into force on the date of signature by the Recipient and the Fund.

**6.2.2 Condition precedent to disbursement of the first tranche (UA6.0 million):** The obligations of the Bank to disburse the first tranche of the Grant shall be conditional upon the entry into force of the grant protocol of agreement, government maintaining on track the IMF ECF, and the Recipient providing evidence of the fulfilment of the conditions specified in Box 2, in the form and substance satisfactory to the Bank.

<b>Box 2: Conditions precedent to disbursement of the first tranche (UA 6.0 million)</b>	
<p><b>Agreed Actions</b></p> <ol style="list-style-type: none"> <li>1. The share of payment vouchers presented by AGD to ASSSL team auditing the 2010 annual public accounts by the end of the audit period reaches 80% (paragraph 4.2.6).</li> <li>2. Statement on mining revenues collected from 10 largest mining enterprises by turnover for public disclosure in the first half of 2011 in accordance with the Act (paragraph 4.2.9).</li> <li>3. Submission to Parliament of the Energy and Water Regulatory bill and the Electricity Bill by August 2011 (paragraph 4.2.11).</li> </ol>	<p><b>Required Evidence</b></p> <ol style="list-style-type: none"> <li>1. MDBS review report of June 2011.</li> <li>2. MOFED report on mining revenue for first half of 2011.</li> <li>3. The draft bills, transmitter and acknowledgement letter</li> </ol>

**6.2.3 Conditions precedent to disbursement of the second tranche (UA4.0 million):** The obligations of the Bank to disburse the second tranche of the Grant shall be conditional, upon government maintaining on track the IMF ECF, and the Recipient providing evidence of the fulfilment of the conditions specified in Box 3, in the form and substance satisfactory to the Bank.

<b>Box 3: Condition precedent to the disbursement of the second tranche</b>	
<p><b>Agreed actions</b></p> <ol style="list-style-type: none"> <li>1. Teachers' verification exercise completed and all teachers on the payroll have had key data on their records verified by physical interview (paragraph 4.2.4).</li> <li>2. Disclosure on a yearly basis by the Minister of Finance, disaggregated figures on mining revenues (paragraph 4.2.9).</li> <li>3. Approval by Cabinet of an electricity tariff methodology derived from a completed tariff study providing guidance on tariff setting (paragraph 4.2.11).</li> </ol>	<p><b>Evidence required</b></p> <ol style="list-style-type: none"> <li>1. MDBS review report of May 2012</li> <li>2. MOFED report on Mining revenue for 2011.</li> <li>3. Cabinet decision memo on the recommendations of the tariff methodology.</li> </ol>

### **6.3 Compliance with Bank Group policies**

**6.3.1 This programme complies with all applicable Bank Group policies and guidelines.** These include: (i) Operations Guidelines of the Fragile States facility, (ii) the 2004 Guidelines for Development Budget Support Loan, (iii) the AfDB/World Bank JAS for Sierra Leone, 2009-2012, and (iv) the Bank's Governance Strategic Directions and Action Plan for 2008-12.

## **VII. RISK MANAGEMENT**

- **Macroeconomic risk:** Sierra Leone is vulnerable to external shocks due to its dependence on imported food and fuel as well as on primary exports. Increasing fuel and food prices has impacted negatively on the economy and poverty outcomes and this has been compounded by Sierra Leone's fragility situation. [Probability: Medium Impact: High].

**Mitigating Measures:** Continued implementation of macroeconomic policy framework supported by the IMF will help to mitigate the macro-economic risks. The MDBS programs would help create the fiscal space for government to implement pro-poor projects that will help mitigate the pains of rising fuel and food prices. Furthermore, the Government plans to increase financial resources for safety net programs and enlarging the size of the public bus fleet.

- **Election risk:** As the 2012 elections approaches, there is the risk that substantial “spending” could lead to a large fiscal deficit – this includes financing election, and spending pressure to improve social indicators and fund civil service wage increase. Election related tension could also undermine revenue performance [Probability: Medium Impact: High].

**Mitigating Measures:** Development partner’s support to election through trust fund will help to relieve pressure on the budget for election expenses, and enhance the chances of democratic and peaceful election. The increased role of civil society organizations in budget monitoring and oversight, and donors’ budget support disbursement triggers would strengthen fiscal discipline and mitigate the potential risks of fiscal slippages during the election period. Government commitment to PFM reform also provides comfort in this regard.

- **Fiduciary and implementation capacity risk:** Government could back slide in implementing PFM reform and addressing weaknesses in the fiduciary control environment. This can also be aggravated by weak institutional capacity which could undermine the implementation of PFM reform program aimed at reducing the level of fiduciary risk [Probability: Medium Impact: High].

**Mitigation Measures:** Progress against PFM reform is critical indicators in the PAF. Government led reform program backed by the MDDBS partners provides strong platform to encourage and monitor change. The on-going multi-donor supported IPFMRP and a complementary capacity building project by the Bank will help strengthen PFM systems and the capacity of key institutions that are entrusted with the responsibility of ensuring transparency and accountability (e.g. ACC, SL EITI and ASSL).

## **VIII – RECOMMENDATION**

8.1 Management recommends that the Board of Directors approve the proposed FSF grant of UA 10.0 million to the Republic of Sierra Leone for the purposes and subject to the conditions stipulated in this report.

**APPENDIX 1**  
**LETTER OF DEVELOPMENT POLICY**

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Ministry of Finance &  
Economic Development  
Treasury Building  
George Street  
FREETOWN  
8th June, 2011

**Dr. Donald Keberuka,**  
**President**  
**African Development Bank**  
**Tunis, Tunisia**

**Dear President Kaberuka**

**SECOND ECONOMIC GOVERNANCE REFORM PROGRAMME (EGRP II)**

I am writing on behalf of the Government of Sierra Leone to request the approval of the second Governance Reform Programme (EGRP II) in the sum of UA10 from the Fragile states Facility to support the efforts of Government to accelerate economic growth and poverty reduction through the consolidation and deepening of public financial management reforms consistent with our poverty reduction strategy-the AGENDA for CHANGE. The proposed grant will support efforts to improve transparency and accountability in public expenditure management and improve revenue governance in the mining and energy sectors.

The main objective of the Agenda for Change is to reduce poverty through sustained and inclusive economic growth. To achieve this objective, the Agenda for Change focused on four strategic priorities, namely: (i) Ensuring reliable energy supply nationwide, (ii) Develop the national transportation network (iii) Increase productivity and value -addition in agriculture and fisheries and (iv) Improving human development through the provision of enhanced services in the education and health sectors.

The Agenda for Change also clearly outlines the prerequisites for achieving the above mentioned strategic priorities. These include deepening governance reforms; sustaining macroeconomic stability; promoting private sector development; and improving natural resource management. Sierra Leone is making considerable progress in the implementation of the Agenda for Change, with primary focus on improving infrastructure and enhancing the delivery of social services while maintaining macroeconomic stability. With the support of our development partners, significant progress has also been achieved in strengthening public financial management to improve accountability, transparency and effectiveness in the use of public resources. This is strengthening the foundation for sustainable growth and poverty reduction.

## **Recent Economic Developments (2008-2010)**

After growing strongly by 5.5 percent in 2008, the Sierra Leonean economy slowed down to 3.2 percent in 2009 mainly due to the impact of the global financial and economic crisis, which adversely affected mining output and exports as well as inward remittances. The economy has started to recover with real GDP expanding by 5.0 in 2010 driven mainly by recovery in the mining sector, manufacturing and higher agricultural output combined with public investment in basic infrastructure. Trends in consumer prices were largely influenced by the global food and fuel price shocks. The spike in food and fuel prices in 2008 resulted in higher inflationary pressures during most of the year. Consumer prices moderated toward the end of 2008 as food and fuel prices increase eased, with end period inflation declining to 12.2 percent from 13.8 percent in 2007. The declining trend in inflation continued into most of 2009, and end period inflation reached 10.8 percent in 2009. But, inflation rose sharply in early 2010 reaching 17.8 percent following the introduction of the Goods and Services Tax (GST) in January 2010. I

Export growth (in US dollar value terms) slowed down in 2008 and 2009 due a combination of internal and external factors. The suspension of operations by Koidu Holdings- the Kimberlite mining company resulted in a 21 percent drop in mineral exports in 2008. The onset of the global financial and economic crisis and the associated drop in global demand resulted in 18.5 percent drop in mineral exports in 2009. However, the slump in mineral exports was largely compensated by the unexpected strong growth in agricultural exports. Overall, total exports drop by 3.0 percent in 2008 and further by 1.0 percent in 2009. However, exports recovered strongly, growing by 33.5 percent in 2010 reflecting the recovery of mineral export by about 43 percent during the year.

The value of imports fluctuated during the period, dictated largely by movements in the international prices of fuel and food products. The US Dollar value of total imports increased by 24.8 percent in 2008 on account of the higher international prices of food and petroleum products. The value of imports however, dropped by 2.6 percent in 2009, as the international prices of fuel and food moderated during the year. Import grew by 12.3 percent in 2010, driven largely by import of machinery and transport equipment to support mining and road construction activities. The spike in food and fuel prices also contributed to the higher import bill.

As a result of the decline in export and high import bill during 2008, the current account deficit, including official transfers, rose to 11.5 percent of GDP. The improved performance in agricultural exports largely compensated for the drop in mineral exports in 2009, resulting in the reduction of the current account deficit to 8.4 percent of GDP. The current account deficit, however, widened to 9.7 percent of GDP in 2010.

Domestic revenue increased from 11.5 percent of GDP in 2008 to 13.3 percent of GDP in 2010. The introduction of the Goods and Services Tax (GST) and stricter tax enforcement contributed to the improved performance. Total expenditure and net lending increased from 20.7 percent of GDP in 2008 to 27.3 percent of GDP in 2010, reflecting mainly higher spending on domestically funded capital projects and fuel subsidies. Hence, the overall deficit, excluding grants increased from 9.2 percent of GDP in 2008 to 14.0 percent of GDP in 2010. Including grants, the overall deficit, widened from 4.7 percent of GDP to 6.9 percent of GDP over the period.

Monetary policy was pro-active in containing monetary growth, and broad money growth slowed down to 21.8 percent in 2010 from 30.8 percent in 2008. Gross international reserves increased to 6.1 months of imports in 2009 from 4.4 months of imports in 2008, reflecting in part the allocation of equivalent of US\$ 128 million by the IMF to Sierra Leone. Although gross reserves in nominal terms increased to US\$ 338.5 million in 2010, in months of imports, gross reserves declined to 5.2 due the increase in the import bill.

The nominal exchange rate of the Leone to the US dollar remained relatively stable in 2008. However, the drop in exports and inward remittances on account of the global economic crisis reduced the availability of foreign exchange in 2009. As a result, the monthly average exchange rate of the Leone to the US dollar depreciated by 28 percent between December 2008 and December 2009. The value of the Leone became relatively stable in 2010, depreciating by just 7.7 percent during the year.

### **Medium Term Economic Outlook**

The medium-term prospects of the economy are bright. The economy is projected to grow further by 5.1 percent in 2011 and reach 6 percent by 2012. The projected growth rate is underpinned by public investment in basic infrastructure (roads, electricity and water supply) and initiatives to improve the business climate and raise agricultural productivity. The recovery in the global economy is expected to increase the demand for Sierra Leone's exports, which should increase the supply of foreign exchange in the economy and hence contribute to exchange rate stability. The projected increase in domestic food production combined with a stable exchange rate and supported by prudent fiscal and monetary policies is expected to dampen inflationary pressures. Reflecting the projected increase in imports to support the increase in economic activities, gross foreign reserves are projected to decline from 5.2 months of imports in 2010 to 4.5 months of imports by 2012.

The implementation of the two newly signed mining lease agreements for iron ore is expected to boost economic activity in the medium-term. Assuming full implementation of the planned investments, GDP is projected to grow by nearly 12 percent in 2012, exports would triple while tax revenue would increase substantially in the medium term.

**Monetary and Exchange Rate Policies:** Monetary policies will aim at achieving single-digit inflation in the medium-term. The Bank of Sierra Leone will continue to use open market operations through repos and reverse repos to contain the growth in excess liquidity and hence inflationary pressures. To strengthen monetary policy operations, the BSL has reviewed its monetary policy framework and introduced a benchmark interest rate—the monetary policy rate, which is used to signal the stance of monetary policy to the market.

To achieve the objective of single digit inflation, reserve money is programmed to slow down to 19.0 percent and 16 percent in 2012 and 2013, respectively. Broad money will also slow to 26.2 percent in 2012 and 20.2 percent in 2013. This monetary programme will also accommodate a 34 percent and 19 percent increase in credit to the private sector in 2012 and 2013, respectively.

Government is committed to maintaining a flexible exchange rate to facilitate the adjustment of the economy to external shocks. The BSL will limit its foreign currency sales to absorb foreign-financed budget spending and smooth short-term market volatility. The BSL will seek to enhance its foreign exchange management strategy by promoting inter-bank foreign market transactions and move to a whole sale foreign exchange auction system.

**Fiscal Policy:** Consistent with the priorities laid out in the Agenda for Change, public expenditures will be re-oriented in favour of capital spending. The emphasis will be to create fiscal space to improve basic infrastructure while maintaining macroeconomic stability. Fiscal space will be created by not only strengthening domestic revenue collection but also the efficiency of public spending through containing non-priority expenditures and better project selection and implementation. Domestic revenue is projected to increase to 13.7 percent of GDP by 2013 taking into account the efficiency gains from the introduction of GST and improvement in tax administration. To achieve this target, the GoSL will fully apply the fiscal regime stipulated in existing tax and customs acts and will minimize the granting of discretionary tax exemptions.

**Debt management Policy:** Debt sustainability will remain a top priority of economic management in the medium-term. The GoSL is committed to a conservative strategy of external borrowing on highly concessional terms. A comprehensive national debt law and procedures manual has been adopted. The Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) will be electronically linked with IFMIS to improve the recording and reporting of debt data. In order to further improve on debt management, the Government is requesting assistance from the World Bank and the Fund with respect to developing a comprehensive Medium-Term Debt Management Strategy (MTDS). To maintain fiscal and debt sustainability, the GoSL is committed to keeping domestic financing below 2.0 percent of GDP.

## **PROGRESS IN THE IMPLEMENTATION OF THE AGENDA FOR CHANGE**

Mr. President, Government has made significant progress in the implementation of the AGENDA for CHANGE during 2008 to 2010. The programmes and projects implemented under each of the strategic priorities of the AGENDA for CHANGE are detailed below:

**Energy:** Government recognised that access to reliable and affordable energy supply on a sustainable basis promotes economic development and has therefore prioritized the improvement of electricity supply throughout the country.

The Bumbuna Hydro electric Dam was completed and commissioned in late 2009 and this has improved the supply of electricity in Freetown. With assistance from the Japanese International Cooperation (JICA), a 10MW thermal plant was also installed at the Kingtom Power Station in 2010 to augment electricity supply to the Western Area. With Support from the Arab bank for Economic Development in Africa (BADEA), two thermal plants of 8.25 MW at the Black hall Road Power station to supplement power from Bumbuna especially during the dry season. In the provinces, the Bo-Kenema thermal plants are being overhauled while the Dodo Hydro dam is expanded to increase the supply of electricity.

However, the adequacy and reliability of electricity supply continues to be hampered by a fragile Transmission and Distribution (T&D) network which is over 40 years old. To improve on the T&D network, Government has provided substantial funds to replace the old network. The installation of 33kV lines in Freetown and the Western Area and is expected to increase the transport capacity of the T&D network from the current 30MW to about 45MW by the end of 2011. Government is also pursuing programmes to increase the supply of electricity in the rural areas through the use of solar technology. To this end, Government piloted a Solar Electrification Programme with support from the Barefoot College in India.

**Roads:** The important role of a good road network in supporting other economic activities as well as the delivery of basic services cannot be over-emphasized. In this regard, Government embarked on a major road construction programme to link different parts of the country and facilitate the movement of people and goods. The construction/reconstruction of major highways (e.g. Masiaka-Bo, Bo-Kenema, and Makeni-Matotoka Highway) have been completed, and the construction of the Rogberay-Pamlap Highway and other roads (Tokeh-Lumley, the Hill-Side Bye Pass Road, widening of the Wilkinson Road and the rehabilitation of streets in Freetown and the provincial headquarter towns) are in progress. In addition, About 555km of feeder roads were completed in 2010 and work on other feeder roads are nearing completion.

**Agriculture:** To promote agricultural development, Government developed a National Sustainable Agriculture Development Plan (NSADP, 2010-2030) within the framework of the Comprehensive Africa Agriculture Development Programme (CAADP) in 2009. With support from development partners, Government introduced the Smallholder Commercialisation Scheme (SCS) within the framework of the NSADP to ensure the effective provision of services to all farmers nation-wide. As most of the poor are farmers, mainly engaged in small farming operations, it was critical that Government singled out this programme within the agricultural sector. The SCS has brought together 10,000 farmers, who were provided with packages of subsidised inputs, machinery and training. Also, 150 Agricultural Business Centres (ABCs) are being constructed across the country. An agricultural machinery and equipment hire purchase scheme was launched in 2010 to promote agricultural commercialization through mechanization. The 265 tractors and other agricultural machinery were acquired under a Line of Credit from the Government of India. These tractors have been deployed throughout the country.

**Education:** Government realised the importance of increasing attendance in schools but further recognises the importance of retaining these students in the long run. As a result, government formulated the National School Feeding Programme to supplement the WFP School Feeding Programme already in existence with the aim to increase attendance rate, retention and minimise child stunting which is very endemic in Sierra Leone. Government, with assistance from development partners provided in-service training for teachers as well as developing a code of conduct for teachers to improve ethical standards in the educational system. Government through the SABABU project supplied 1,000,000 sets of textbooks to primary schools and 100,000 to secondary schools. An Educational Management Information System (EMIS) has also been installed in the MEST.

**Health:** Government's health policy objective was to improve the health of the population, especially mothers and children, through strengthening national health systems. A key priority on the Government's development agenda for 2010 was the implementation of the Free Healthcare Initiative. To ensure this, Government provided additional resources towards improving the conditions of service of medical staff, procurement of drugs and equipment, and strengthening sector supervision. Essential drugs have been provided to each district for the implementation of the Free Health Care Policy. To improve the quality of health care in health delivery facilities, Government also procured medical equipment for the 6 referral hospitals in the country.

Government also undertook a nationwide distribution of 3 million treated bed nets in December 2010 to control the spread of malaria. Furthermore, Government in its efforts to increase the number of peripheral health facilities with at least two health personnel, additional 1,000 healthcare staff were recruited.

## **Structural Reforms**

**Public Financial Management:** Government continues to implement public financial management reforms under the multi-donor funded Integrated Public Financial management Reforms project (IPFMRP), which seeks to consolidate and deepen reforms undertaken in earlier years. A comprehensive review of the National Public Procurement Act (2004) and Government Budgeting and Accountability Act(2005) and their respective supporting regulations is being undertaken. Government has adopted a comprehensive debt management law in 2011.

Efforts continue to be made to strengthen the Medium-Term Expenditure Framework (MTEF) by enhancing the planning, monitoring and evaluation process for capital projects. To this end, Government amended the GBAA (2005) in support of an appropriate framework. Going forward, Government will fully integrate three-year public investment plan with the budget process. To further strengthen the budget planning process, an IMF style Financial Programming and Policies model (the Sierra Leone Integrated Macroeconomic Model-SLIMM) has been developed. The model is now used to produce consistent and robust medium-term macro-fiscal forecasts which feed into the budget planning process.

Following the enactment of the National Public Procurement Act in 2004, significant progress has been made in improving the public procurement process. Good quality procurement plans are now prepared by MDAs and the volume and value of public procurements that go through competitive process is also increasing steadily. A cadre of procurement professionals has been established in the civil service and procurement specialist have been recruited and deployed in key MDAs.

Progress continues to be made in strengthening the internal audit function across Government. In 2010, Government recruited 51 internal audit personnel including a Deputy Director, Principal Auditors and Senior Auditors. These were deployed in key MDAs. As a result, the number of MDAs with fully functional internal audit units has been increased from 8 in 2009 to 31 in 2010. Internal audit committee have also been established and are meeting regularly to follow up on audit recommendations.

With regards to external audit, the Auditor-General's report on 2009 Public Accounts has been laid in Parliament. The audit of the 2010 Annual Public Accounts is in progress. Government continues to implement Public Expenditure Tracking Surveys (PETS) to ascertain the proportion of disbursed public resources that reach the intended beneficiaries. The 2010 PETS covering selected 2009 and 2010 poverty-related expenditures was implemented in September 2010. A draft report on the findings was produced in May 2011.

The roll-out of the Integrated Public Financial Management Information System (IFMIS) continues. The IFMIS has now been rolled out to 11 MDAs to foster commitment control and the processing of public financial transactions. Plans are at an advanced stage for the roll-out of IFMIS to additional 6 MDAs. MOFED continues to provide training and support to IFMIS users across MDAs. To improve financial management in the local councils, the PETRA Accounting package-a financial management information system has been rolled out to 8 local councils. Plans are underway to roll-out to three additional local councils.

**Private Sector Development:** Government recognises that the private sector constitutes the main engine for economic growth and development, noting that only about 20 percent of national businesses is in the hands of the state, the rest, though operated mostly informally, are in the hands of the private sector. Thus, within the framework of the national poverty reduction strategies, Government has been implementing reforms to improve the investment climate.

These include removing the administrative barriers to investment, strengthening and modernizing the legal and regulatory framework for business development. A private sector development strategy has been developed. A comprehensive Investment Incentives Policy was also approved in 2009. In 2010, a National Trade Policy was developed and launched, including initiating the process for the development of an industrial policy. More recently, Public-Partnership Policy (PPP) framework was put together and a draft PPP law has been enacted by Parliament and is awaiting Presidential assent.

**Anti-Corruption Efforts:** As part of its effort to improve governance and fight corruption, Government established the Anti-Corruption Commission (ACC) following the enactment of the Anti-Corruption Act in 2000. The ACC recorded some successes during 2005-07 but was constrained by its inability to prosecute corrupt cases, without reference to the Office of the Attorney-General and Minister of Justice.

The Anti-Corruption Act 2000 was therefore repealed and replaced with the Anti-Corruption Act 2008. The new 2008 ACC Act gave prosecutorial powers to the Anti-Corruption Commission. The amendments to the 2000 Act include creating new offences such as illicit enrichment, abuse of office and misuse of office; providing adequate protection for whistleblowers and informers; making it compulsory for all public servants to declare their assets and make adequate provision for international cooperation in the fight against corruption. The amendments have ensured that the national legislation is in tandem with the United Nations Convention Against Corruption (UNCAC), which Sierra Leone has ratified, and the African Union Convention on preventing and Combating Corruption, which Sierra Leone will soon ratify. Government also revised, adopted the National Anti-Corruption Strategy (2008-13). In 2010, the ACC handled 117 cases, eight (8) of which led to convictions, including two Government Ministers.

## **THE SECOND ECONOMIC GOVERNANCE REFORM PROGRAMME (EGRPII)**

Mr President, the second Economic Governance Reform programme will support the implementation of the Agenda for Change to accelerate economic growth and poverty reduction through public financial management reforms. In particular, the proposed operation will consolidate reforms achieved under the first Economic Governance Reform Programme (EGRPI) and to deepen further the reform agenda set out in the same programme by supporting actions to (i) strengthen public expenditure management and (ii) improving revenue governance in the mining and energy sectors.

**Strengthening Public Financial Management:** This component covers aspects of public expenditure relating to the effectiveness of payroll control and external scrutiny

### **(a) Effectiveness of payroll control**

The instability of the Government payroll in general and the teachers' payroll in particular is one of the key challenges in public expenditure management in Sierra Leone. As part of the

wider public sector and public financial management reforms, Government undertook a biometric verification of payrolls in MDAs to address the problem of incomplete and inaccurate personnel records and database. The aim was to identify ghost workers and reduce the opportunities for payroll fraud. Significant progress was made in this regard. The biometric verification of the civil service, which has been completed resulted in the reduction of the civil service payroll from 16,000 to 12,000 and associated salary savings of Le500 millions per month. The verification of the health sector payroll has also been successfully completed. The next challenge is ensuring the integrity of the teachers' payroll which constitutes 50% of public employees. The integrity of the teachers' payroll is significantly undermined by the lack of complete personnel records and personal database as well as the existence of anomalous files. In an effort to address this issue, files have been created for all the 35,505 teachers.

Going forward, government will:

- (i) continue with efforts to improve the credibility of the teachers' payroll by carrying out a physical verification of all teachers as well as updating records in teachers' files and reconciling all files with the master file held by the Human Resources Management Office and with the IFMIS.
- (ii) establish the Teachers Commission, which will be charged with the responsibility for maintaining the teachers records and sustain effective management of the workforce and payroll control.

**(b) External scrutiny:** Significant progress has been made with respect to external scrutiny and oversight including the timely preparation of the Annual Public accounts and the auditing of same. The audit of the 2009 public accounts has been completed while that of the 2010 accounts commenced in April 2011. This led to significant improvements in the 2010 PEFA scores for indicators regarding accounting, recording and reporting compared to the 2007 PEFA scores.

However, though significant progress is being made in terms of overall scrutiny and oversight, including parliamentary review of the audit reports, delays in consideration of the Auditor General's reports and follow up on the recommendations of the PAC remain a weak link in the overall scrutiny and oversight. Government represented by the Attorney-General, Auditor-General, Accountant-General and the PAC in collaboration with the MDDBS partners have started to address this problem. Government will continue with efforts to address these concerns in the near term by:

- (i) putting in place a database in ASSL for registering audit recommendations and follow up of audit recommendations
- (ii) improving the share of payment vouchers presented by the AGD to the ASSL team auditing the 2009 and 2010 annual public accounts
- (iii) ensuring that defaulters are held accountable including sanctions

### **Strengthening revenue governance in the mining and energy sectors**

#### **(a) Improving transparency and accountability of revenue from the mining sector**

Government recognises the significant role of the mining sector as a key growth driver of the Sierra Leonean economy and a major source of revenue, foreign exchange and employment. Government is therefore committed to ensuring the fullest utilisation of Sierra Leone's huge mineral potential for the benefit of the population. In this regard, Government is putting in

place measures to improve transparency and accountability in the management of mining revenues. All mining agreements have been reviewed with a view to increasing the contribution of the sector to socio-economic development. A new Mines and Mineral Act with an appropriate fiscal regime was also enacted in 2009 to regulate activities in the sector. The Ministry of Mines and Mineral Resources is being restructured with the establishment of a National Minerals Agency to strengthen capacity and improve governance of the extractive sector. Sierra Leone became an EITI candidate in 2008; the first EITI report (2006-07) was published in March 2010; and the final validation was issued in August, 2010. The reconciliation and validation reports contain a number of recommendations for improving revenue management in the extractive industries to assist Sierra Leone achieve compliant status in 2012.

To ensure the full realisation of the benefits of the mining sector to the population, there is the need to further strengthen transparency and accountability of the extractive sector including revenue management. To this end, Government will:

- (i) implement the recommendations of the EITI reconciliation and validation reports.
- (ii) implement the SL-EITI annual work plan
- (iii) disclose the mining revenue from the 10 largest mining enterprises
- (iv) ensure the disclosure by the Minister of Finance and Economic Development on a yearly basis, disaggregated figures on mining revenues (licenses, royalties, withholding tax, etc); and
- (v) implement the institutional reforms in the Ministry of Mines and Mineral Resources

**(b) Improve revenue management in the energy sector**

Government also recognises the energy sector's contribution towards economic development in terms of spurring growth in the productive sectors, expanding employment and reducing poverty. Despite this potential, there still remain considerable challenges in the sector, which inhibit the growth and development of the economy. The sector is characterised by low generating capacity, rising transmission and distribution losses, poor revenue collection and restricted distribution in major towns. There is also the need to improve the pricing methodology for electricity to make it more transparent, affordable and cost reflective.

Government has embarked on energy sector reform to improve the performance of the sector and improve access to electricity nationwide. As a first step in addressing these challenges, Government adopted and published an Energy Sector Policy and Strategic plan in September 2009. Other actions taken to facilitate the reform of the electricity sector include the preparation and submission to Parliament of the Energy and Water Regulatory Bill and the Electricity Bill. A Rural Energy Agency Bill has also been prepared. These bills, when enacted into law, will provide the legal basis for the restructuring NPA and the rationalization of the electricity tariff. With support from the World Bank, work on the cost-based electricity tariff has commenced.

To improve governance of the sector and strengthen revenue management in the energy sector, Government will:

- (i) continue to pursue the restructuring of the NPA;
- (ii) submit the supporting legislations to Parliament;
- (iii) establish the regulatory and utility companies as per the national energy policy and legislations
- (iv) complete the electricity tariff study to provide methodology and guidance on tariff setting;
- (v) adopt and implement an electricity tariff derived from the completed tariff study; and

- (vi) formalise power sales from Bumbuna to NPA through a legally binding power purchase agreement. Government will also expand the use of pre-paid meters to bring down losses and enhance transparency of revenue collection.

## **CONCLUSION**

Mr. President, macroeconomic and budgetary management during 2011 has been very challenging due to the adverse impact of the recent food and fuel crisis. The country also continues to grapple with the challenges of widespread poverty and high levels of unemployment. The Government of Sierra Leone continued to implement policy and institutional reform measures including programs supported under the IMF Extended Credit Facility.

Government remains committed to the implementation of the programmes and policies presented in the AGENDA for CHANGE including those supported by the series of Economic Governance and Reform Programme to address these challenges. This however, requires continued financial and technical support from our development partners including the African Development Bank. While Government continues to pursue measures to enhance domestic revenues, the continued support of our development partners remains critical in implementing the programmes and policies articulated in the second PRSP.

Your approval, therefore of this programme will facilitate reform implementation aimed at broadening the fiscal space for enhanced service delivery to the people of Sierra Leone

Yours sincerely

**SAMURA W.W KAMARA**  
**MINISTER OF FINANCE AND ECONOMIC DEVELOPMENT**