Statement by the Staff Representative

of the International Monetary Fund

at the Paris Club Meeting on Sierra Leone

Paris, October 16, 2001

1 Since the last Paris Club meeting on Sierra Leone in March 1996, the country has experienced profound social and physical dislocations as a result of a brutal civil war. The war led to a massive disruption of economic activity, a devastating displacement of the population, with nearly half of the population internally or externally displaced, and to the destruction of bulk of the physical and social infrastructure, including schools, health centers and local administrative structures.

2. In July, 1999, the government and the rebels signed a peace agreement calling for a ceasefire and disarmament of combatants. The implementation of the ceasefire was disrupted in May 2000, when the rebels seized UN peacekeepers as hostages. Agreement was reached on a general ceasefire in November 2000 in Abuja Nigeria. Since that time, the ceasefire has held and the program of disarmament, demobilization and reintegration (DDR) of ex-combatants has proceeded in a generally satisfactory manner. As of end September, over 18,000 ex-combatants (or about 65 percent) have been disarmed and are undergoing reintegration training. The disarmament of ex-combatants is expected to be completed by the end of 2001; however, the process of reintegrating ex-combatants into their communities is expected to continue during 2002. A significant proportion of the displaced population has

started to return to their homes. As expected, the peace process has not been easy or smooth. It has continued largely because of the unflagging commitment of the United Nations, the UK, the USA, ECOWAS, and the international community at large, who have contributed generously in sustaining the process.

the social and physical infrastructure; servicing the heavy external and internal debt burden; and finally, against this background, maintaining macroeconomic stability.

4. The government's economic and social reconstruction program started soon after the signature of the peace accords in July 1999. In December 1999, the Fund approved the use of Fund resources by Sierra Leone under the emergency post-conflict assistance policy in support of the program for 2000. The World Bank provided support for the program with an Economic Recovery and Rehabilitation Credit (ERRC), a Community Reintegration and Rehabilitation project (CRRP), and the restarting of IDA-supported projects in the pipeline. The program received generous support from other bilateral and multilateral donors. The program was successfully implemented. As a result, the economic situation improved significantly. The growth of real GDP rose to nearly 4 percent in 2000, after several years of decline, inflation was sharply reduced, while external gross reserves of the Bank of Sierra Leone increased. In addition, the government made good progress in implementing structural reforms and in rebuilding capacity for policy making and implementation.

5. In order to address the desperate poverty situation in a more comprehensive manner, the Government has elaborated an interim Poverty Reduction Strategy Paper (PRSP) which spells out the medium term macroeconomic and structural policies to be implemented. The Government has adopted a two-phase poverty reduction strategy. In the transitional period 2001–02, government policies will focus on: the reestablishment of personal and state security and the consolidation of law and order; the rebuilding of the physical and social infrastructure; catering to the needs of the displaced population, war victims and veterans; and maintaining macroeconomic stability. For the second phase, the focus will shift to longer term development and poverty reduction issues, to be elaborated in the context of a full PRSP, following a more comprehensive participatory process. In September, 2001, the Fund approved a three-year arrangement under the Poverty Reduction and Growth Facility in an amount equivalent to SDR 130.84 million. During the same month, the Executive Boards of the Fund and the Bank agreed that Sierra Leone was eligible for debt relief under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative.

6. In line with the above priorities, government policies will consist of measures to: a) enhance the population's capacity to undertake income generating activities, such as the resettlement of the displaced rural population and the provision of key requirements to them to enable them to resume food and cash crop production; b) maintain macroeconomic stability through the pursuit of appropriate fiscal and monetary policies; and c) implement structural reforms to enhance the economy's capacity for growth through the development of a vibrant private sector.

The government's quantitative medium-term macroeconomic objectives are to: attain a real GDP growth rate of 5 percent in 2001, and 6-7 percent during 2002–04; limit inflation to about eight percent in 2001, and to 5 percent per year thereafter; and increase gross external reserves of the Bank of Sierra Leone (BSL) to over two months of import cover. Growth is expected to be bolstered by the planned resumption of rutile production, the recovery in agricultural production following the resettlement of the displaced population, and the continued expansion of light manufacturing and service sectors. Sierra Leone has significant potential for increasing diamond (kimberlite) and gold production, as well as in the fisheries sector.

8. Medium-term fiscal policies are aimed at enhancing government revenue growth, improving expenditure allocation and service delivery, and reducing the budget's reliance on domestic bank financing. Despite the projected significant rise in the ratio of revenue to GDP over the medium term (to about 14 percent), expenditures are projected to rise at a faster pace, reflecting the large resource requirements for rebuilding the social and physical infrastructure and poverty alleviation. The overall budget deficit(excluding grants) is projected to rise to over 28 percent of GDP in 2001 (17 percent in 2000), and to remain high (19 to 28 percent of GDP) over the medium term.

9. Reflecting this fiscal outlook, and the large reconstruction needs of the private sector, the external current account (excluding official transfers) is projected to rise from 18 percent of GDP in 2000 to a peak of 34 percent of GDP in 2002 (21 percent in 2001) and remain high

(17-25 percent of GDP) through 2004. Although a significant improvement in domestic savings is projected, Sierra Leone's external financing requirements would continue to remain large over the medium term.

10. The external financing gap is estimated at US$225 million in 2001, and at US$52 million in 2002. These gaps can be covered by Fund support under the PRGF (US$24 million in 2001), understandings in regard to arrears to multilateral creditors, for which discussions are underway, and by a comprehensive rescheduling of arrears and maturities falling due to bilateral and commercial creditors.

11. Preliminary estimates of potential debt relief under the HIPC indicate that after traditional debt relief mechanisms, Sierra Leone would need debt relief amounting to US$553 million in net present value terms to reduce its debt burden to150 percent of exports at the decision point. Assistance from multilateral creditors is estimated at US$ 326 million; US$ 189 million from official bilateral creditors; and US$38 million from private creditors. Sierra Leone is expected to reach the decision point later this year or in early 2002.

12. In conclusion, the staff believes that Sierra Leone has shown a strong commitment to implementing macroeconomic and structural reforms, despite the difficult transition from a devastating civil conflict. The interim PRSP produced by the government provides a good basis for addressing the daunting economic and social challenges confronting the government. To attain the government's policy objectives, Sierra Leone would require

sustained external support. The staff believes that the authorities' poverty reduction program deserves the full support of the international financing community.