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Staff Country Reports

Guinea-Bissau: Poverty Reduction Strategy Paper—Joint Staff Advisory Note

The attached Joint Staff Advisory Note (JSAN) on the Poverty Reduction Strategy Paper for Guinea-Bissau, prepared jointly by the staffs of the World Bank and the IMF, was distributed with the member country's Poverty Reduction Strategy Paper (PRSP) to the Executive Boards of the two institutions. The objective of the JSAN is to provide focused, frank, and constructive feedback to the country on progress in implementing its Poverty Reduction Strategy (PRS).

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL DEVELOPMENT ASSOCIATION
AND
INTERNATIONAL MONETARY FUND

GUINEA-BISSAU

FIRST POVERTY REDUCTION STRATEGY PAPER—JOINT STAFF ADVISORY NOTE

Prepared by the Staffs of the International Development Association (IDA)
and the International Monetary Fund (IMF)

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I. OVERVIEW

- This Joint Staff Advisory Note (JSAN) reviews the first ever full Poverty Reduction Strategy Paper (PRSP) prepared by the Government of Guinea-Bissau.** Political instability and conflict have hindered economic growth in Guinea-Bissau, which in turn has contributed to major fiscal and external imbalances. This situation seriously undermined the government's ability to mobilize the resources needed for implementing critical growth-enhancing infrastructure rehabilitation projects and poverty-reducing programs. By the same token, the preparation of the PRSP, which started in 2001, was repeatedly delayed due to political instability and weak technical capacity. Following parliamentary elections in 2003, a transition government was put in place, which prepared a first draft of the PRSP in 2004. The draft PRSP was subsequently revised in 2005 and finalized in 2006 by the government. While the implementation of the PRSP was initially designed to cover the period 2006–2008, it will now cover the period 2007–2010.
- The PRSP was prepared within a participatory process, and builds on grassroots consultations at the national level that involved all segments of society.** The consultative process included three levels of participation: (i) a political and institutional level, engaging the government and its development partners; (ii) a technical level, engaging national public and private sector leaders as well as civil society leaders; and (iii) a popular and community level based on consultation with stakeholders in rural and urban areas.

3. **The PRSP reflects the government’s long-term vision “*Djitu ten*,”**¹ which aims at (i) improving per capita income; (ii) gradually reducing the incidence of poverty to less than 60 percent by 2015; (iii) improving access to basic education by increasing gross enrollment rates to nearly 100 percent by 2015; and (iv) reducing infant mortality rates to less than 80 deaths per thousand by 2015. The PRSP is based on the following four pillars: (i) strengthening governance, modernizing the public administration and ensuring macroeconomic stability; (ii) enhancing economic growth and job creation; (iii) increasing access to social services and basic infrastructure; and (iv) improving the living conditions of vulnerable groups.

II. STRATEGIC ISSUES

4. **The PRSP indicates that, at current trends, none of the seven Millennium Development Goals (MDGs) will be achieved by 2015.** Staffs recommend that the two set of measures set forth in the PRSP for improving progress towards the MDGs (accelerated growth and well defined structural reforms) be further defined so as to identify key enabling policies and programs that can bring some MDGs into reach. In doing so, special attention should be paid to governance, education and health.

5. **The PRSP highlights broad areas of intervention for each strategic pillar but lacks a clear prioritization of activities and programs.** Staffs recommend that the authorities more clearly prioritize the various actions planned under each strategic pillar to ensure adequate sequencing and consistency with available resources. For example, this is the case of the various activities proposed for rural development (second pillar). The various activities proposed for the sector make sense individually, but a sense of priority or programmatic vision is lacking. Staffs, therefore, advise the authorities to address this issue while revising the PRSP at the next APR phase.

6. **Staffs agree with the PRSP’s emphasis that high unemployment rates and heavy reliance on agriculture as the main source of employment are major concerns for poverty reduction.** The prevalence of poverty is widespread in Guinea-Bissau. Moreover, poverty in urban areas is higher compared to other countries. As presented in the PRSP, the poverty profile shows that in 2002, at the household level, 64.7 percent of the population lived in poverty, with 20.8 percent living in extreme poverty. These findings are consistent with the conclusions of a poverty assessment carried out by IDA staff in 2006. At the national level, the unemployment rate among population over 15 years of age was 12.4 percent in 2002, with the rate at 19.3 percent in Bissau and 10.2 percent in other regions. Most of these unemployed people are also classified as being poor. In addition, some 63.5 percent of the working age population is employed in agriculture and they are poorer

¹ “*Djitu ten*” is a National Long-Term Perspective Study prepared by Government and stakeholders with the support of the United Nations’ African Futures Program in 1996.

than those employed in other sectors. Also, the higher incidence of poverty in the male population compared to the female population underscores the significance of gender issues for poverty in the country.² In view of the relative importance of employment, agriculture and gender issues, and possible policy interactions between them, staffs advise the government to deepen the analysis of the links between these areas and their impact on fostering economic growth. Additionally, restrictive labor and minimum wage regulations exist in the formal sector.³ In order to boost job creation, staffs recommend the government to alleviate these labor market rigidities in the medium term.

7. The PRSP candidly emphasizes the need to improve governance, but does not set out a detailed and sequenced strategy to achieve that goal. The government recognizes that improving governance would require: (i) restructuring the public administration based on the State's real needs and financial capabilities; (ii) strengthening the rule of law through judiciary reform; and (iii) carrying out decentralization reforms in the context of social consensus building. Staffs recommend that the government identify a well sequenced series of actions for achieving these objectives, and develop an anti-corruption strategy through a broadly consultative process. The strategy should provide guidance on how to improve transparency and reduce the scope of corruption in the public sector, with particular focus on: (i) management and incentive structures of the public sector; (ii) public financial management, including procurement practices; (iii) judicial sector reforms; and (iv) improving the business climate, including regulation, customs and taxation.

8. Staffs recommend that the PRSP consider specific measures for improving governance in the emerging mining (including oil) activities. In view of encouraging prospects for Guinea-Bissau to start producing oil and phosphate in the coming years,⁴ staffs advise the authorities to design specific measures for addressing potential governance issues by strengthening the legal and regulatory frameworks based on the recommendations of the NGO-sponsored workshop on oil held in Bissau in September 2006.⁵ The main

² This phenomenon is allegedly explained by the different family structures (monogamous vs. polygamous) and their distribution across urban and rural areas, as well as by the fact that women generally engage in various income generating activities, such as the processing of cashew nuts, to supplement the income of the household.

³ As in other African countries, the Labor Code offers protection and coverage to formal workers only.

⁴ The government has authorized Premier Oil (PO) to start oil exploration along Guinea-Bissau's coastal areas. PO has already drilled two oil wells and is currently planning to add two additional sites. Other oil companies are also in discussion with the government to drill seven additional sites. With regard to phosphates, reserves at Salquenha are estimated at 94 million tons and annual production is estimated at 2 million tons per year. Guinea-Bissau phosphate has 36.5 percent of Phosphorous Oxide and one of the best quality of Phosphoric Acid in the world.

⁵ The sponsoring NGO's were SWISSAID, Tiniguena, Action for Development, and International Union for Conservation of Nature (IUCN).

recommendation of the workshop was for increased transparency in the potential development of the oil sector, and the review of potential environmental impacts, possibly through joining the Extractive Industries Transparency Initiative (EITI) as other countries have done. Staffs consider that the most important objective for Guinea-Bissau in this area would be to set up a transparent system for the management of oil and other natural resources, as well for the use of related government revenues. The authorities would also need a strategy to manage the potential macroeconomic impact of oil and other natural resource revenues.

9. The PRSP would benefit from including a discussion on the reform of the security sector, which the authorities plan to implement within the PRSP timeframe.

Over the past three decades, conflict and political instability have represented the main obstacle to good governance, poverty reduction and growth in Guinea-Bissau. A dialogue between the government and the armed forces is ongoing aimed at defining a reform program for the security sector, including reducing the size of the armed forces and improving living conditions in military barracks. In addition to preserving peace and stability, a successful security sector reform will enhance fiscal consolidation through a reduction of the wage bill and a reallocation of public spending to priority poverty-reducing expenditures.

10. The PRSP appropriately considers the safeguarding of macroeconomic stability as a priority for achieving sustainable economic growth and poverty reduction.

The PRSP's macroeconomic framework builds on the execution of a cautious fiscal policy and the implementation of a prudent monetary policy by the Central Bank of the West African States (BCEAO). The government acknowledges that the country has greatly benefited from its adherence to the West Africa Economic and Monetary Union (WAEMU) and by adopting the regional currency. Staffs welcome the authorities' commitment to achieving and maintaining the convergence criteria of WAEMU.

11. The PRSP correctly underlines that a sound fiscal policy will be crucial for maintaining macroeconomic stability.

Given that monetary and exchange rate management falls under the purview of BCEAO, prudent fiscal and borrowing policies will remain key instruments for preserving macroeconomic stability. In this context, the authorities committed in the PRSP to: (i) execute a budgetary policy in line with the norms within WAEMU; (ii) implement fiscal reforms to broaden the tax base; (iii) limit current spending in order to generate primary fiscal surpluses; (iv) downsize the public sector through the retrenchment of redundant workers; and (v) ensure that domestic arrears do not accrue at levels harming the functioning of the private sector. On this last point, staffs urge the authorities to avoid any new accumulation of domestic arrears. In addition, the government plans to improve its external debt management through the creation of a debt monitoring committee and by strengthening the external debt unit at the Ministry of Finance. For its domestic debt, the authorities are planning to carry out an audit of all arrears through the end of 2005, and convert all audited arrears into formal debt.

12. **Staffs recommend that the PRSP consider alternative medium-term macroeconomic scenarios to take into account the potential risks to the economic outlook.** The document does not discuss contingent policies that would be pursued in the event that any of such risks is realized, and staffs' view is that the PRSP would benefit from an explicit treatment of these risks.

13. **The PRSP acknowledges that the private sector should be the main player in the recovery of the economy.** The authorities recognize the need to foster private sector development in order to achieve equitable economic growth and to encourage job creation. Staffs concur with the PRSP that fostering a favorable business climate with a legal and regulatory framework conducive to saving and investing, together with the improvement of political stability, will be crucial to achieve the PRSP objectives. Progress in the government's privatization program has been positive: 31 out of 44 small and medium State Owned Enterprises (SOEs)⁶ have been privatized/liquidated and the necessary environmental assessments have been completed and distributed to the new owners.⁷ To date, retrenchment payments for 23 companies, which includes 1,608 workers and totals CFAF 2.2 billion (about US\$4.5 million), have already been paid. Staffs welcome and encourage the Government's decision to establish under the Ministry of Economy a Unit for monitoring and following-up privatization processes and contracts.⁸ In addition, the country adopted the business legislation approved at the regional level within the framework of the supranational Organization for Harmonization of Business Law (OHADA) in 2003.

14. **The PRSP also acknowledges that basic infrastructure development is the cornerstone of the poverty reduction strategy.** The PRSP emphasizes the need to improve transportation, telecommunication, and utilities services. With respect to transportation, staffs recommend that the Government carry out a prior assessment of various management options including concessions, leases, "affermage" and management contracts and proceed with the implementation of the retained option to bring in private participation. In the area of aviation, staffs note that the Government is taking concrete steps in ensuring professionalization of the civil aviation sub-sector. The Civil Aviation Authority was legally established in March 2005 and is gradually becoming operational.⁹ Moreover, since January 2006, the management of

⁶ There are no large State SOEs in Guinea-Bissau.

⁷ The country ranked 173rd out of 175 on the Doing Business indicators for 2007. Moreover, private savings are weak and only four financial institutions are operating in the country (all of them located in the capital city Bissau).

⁸ The role of this Unit is expected to ensure that: (i) financial obligations and investment commitments are honored; and (ii) any fiscal and economic incentives permitted by the investment code and signed contracts are executed according to the law.

⁹ A partial perimeter fence and access road was constructed for the Bissau airport. The finalization of the full perimeter fence is ongoing under the Bank-supported private sector rehabilitation and development project.

the airspace is in the hands of the Regional Airport Security Agency (ASECNA), and a scaled-down Airport Authority (ENAG) is taking care of infrastructure management. Further, terminal and ground handling operations are being managed by the private sector. Staffs recommend that the government adopt aviation codes complying with regional and international standards (such as those being used in Cape Verde or Senegal). With respect to the telecommunication sector, staffs urge the Government to implement the interconnection regulatory framework, which was prepared and published recently by the Institute of Telecommunications of Guinea-Bissau (ICGB). As for utilities, staffs concur with the PRSP that the rehabilitation of water and energy services is a precondition to economic growth, private sector development and social services delivery. In that respect, staffs recommend that a multisectoral single agency be created to regulate the telecommunications, electricity, water and public terrestrial transport sectors.

15. **The PRSP needs to incorporate a strategy for the cashew sector.** As discussed in the PRSP, cashew production and marketing will continue to be an essential component of rural incomes. Staffs recommend that the Government abstain from intervention in marketing arrangements, which has caused disruptions in the marketing process in the past. This will have important implications for the overall poverty reduction goals set by the authorities. Over the medium term, staffs recommend that the authorities develop alternative sources of fiscal revenues, rather than continue to rely on export taxes from cashews.

16. **Staffs advise the government to strengthen the policy context of the fishery sector strategy given the potential of this sector for reducing poverty.** The PRSP envisions about US\$14 million of investment in the fisheries sector as one of the key aspects of the strategy to diversify the economy and enhance private sector investment. Staffs believe that this goal can be achieved only if combined with enhanced control over the exploitation of the resources and more sustainable resource management. At present, fishery resources are heavily exploited by illegal vessels, foreign industrial vessels that never land or process their catch in the country, and small-scale vessels from neighboring countries. Staffs encourage the authorities to strengthen management and mechanisms for control over resource exploitation, in collaboration with neighboring countries in the context of ongoing regional fishery initiatives supported by IDA and the European Union.

17. **The PRSP adequately identifies overall priorities in the health sector, but does not set priorities for the short to medium term, taking into account budgetary and capacity constraints.** As a result, many critical activities remain unfunded. Staffs recommend that the government revise the strategy and prioritize planned interventions depending on available financing and commitments received from donors for a given period. Critical areas in need of funding are increased wages for public sector health workers and key activities under the Second National Health Development Program (PNDS-2) currently being prepared with technical support from the United Nations specialized organizations (WHO, UNICEF, and UNFPA). The PRSP would also gain in highlighting reform areas planned to be included in the PNDS-2. These comprise health insurance schemes for the

private and public sector through an appropriate minimum package of benefits, pilot community health mutual funds,¹⁰ further strengthening of the cost recovery system, improving countrywide drugs and vaccines supply chains, enhancing the stewardship and regulatory role of the Health Ministry, and building capacity in the health sector.

18. **Greater prioritization among the various activities listed in the PRSP for the education sector would facilitate the elaboration and implementation of an education sector plan.** In particular, staffs recommend that priority activities be clearly identified in line with expected domestic and external financial resources. The PRSP rightly highlights the importance of increasing access to education especially for girls and poor households. In staffs' view, at least two issues must be dealt with urgently in order to achieve this objective. The first issue is teacher training and foremost pre-service teacher training. Information based on classroom observations suggests that teacher proficiency remains low. This is a complex issue, as many good teachers and teacher trainers fled the country during the civil conflict. The second issue is the restructuring of primary education into a six-year cycle. The current structure of a first cycle of four years followed by a second cycle of two years is costly for the government and the nonpublic sector.¹¹ Adopting a six-year primary education cycle has already been tried on a pilot basis, and a new curriculum albeit not perfect, has been drafted. Staffs advise to quickly roll out this new primary education structure.

III. IMPLEMENTATION ISSUES

19. **Staffs caution that the absorptive capacity of the economy needs to be improved.** A substantial portion of the PRSP programs are expected to be financed with external budget and project support. If such support materializes, it will represent a sizeable increase in external assistance compared to current levels. Staffs advise the authorities to take the necessary measures to maximize the effectiveness of increased donor support and reduce the potential negative macroeconomic effects. Also, staffs are of the view that regular Public Financial Management (PFM) reviews, as performed in 2004 and 2006 in collaboration with IDA and the IMF, need to be prepared. The reviews would provide important information on the efficiency of government outlays under the PRSP and on the implementation capacity of the different sector ministries, while allowing a revision of the original targets as necessary.

20. **Staffs advise the government to strengthen the PRSP monitoring and evaluation (M&E) mechanisms.** Staffs welcome the institutional and reporting mechanisms proposed by the PRSP as well as the use of the MDGs as M&E indicators. However, the MDGs cover only medium-term goals. As the PRSP covers a three-year time span, it will be important to

¹⁰ At the moment one experiment is being conducted in the northwestern region of Sao Domingo.

¹¹ Based on studies conducted in others Sub-Saharan African countries, children need at least six years of primary education to become and remain literate throughout their adult life.

develop also short-term indicators for purposes of evaluation. Further, the MDG indicators focus mainly on the social and environmental sectors, and do not address other areas such as governance, growth, and macroeconomic and structural policies. Staffs encourage the authorities to consider a more comprehensive but still selective set of indicators covering the broad spectrum of priority areas of poverty reduction over the short- and medium-term, which will serve as basis for developing a full M&E system. Moreover, staffs encourage the authorities to integrate such indicators within the overall umbrella of planned activities to strengthen Guinea-Bissau's statistical capacity, including through the country's participation in the General Data Dissemination Standards (GDSS) and associated plans for statistical improvement. In addition, the establishment and maintenance of a M&E system should be appropriately funded in the context of the PRSP.

21. Staffs welcome the wealth of information on the main characteristics and determinants of poverty in Guinea-Bissau. Staffs, however, note that the PRSP's poverty profile does not include a poverty trend analysis due to methodological differences in the design of the 1994 and 2002 household survey data. The authorities are advised to develop poverty statistics that are comparable over time, and strengthen the capacity to collect and analyze poverty data. Specifically, the authorities are encouraged to implement a new household survey to update the 2002 poverty data and serve as a baseline for assessing the impact of the PRSP implementation. Ongoing statistical capacity building support by donors could assist the authorities in this endeavor.

22. Staffs encourage the authorities to review the definition of 'vulnerable groups' to make it more useful for policy targeting. Staffs believe that under the current definition of "vulnerable groups" a large share of the population would qualify as vulnerable. A more realistic approach would be to recognize widespread vulnerability and then explain that limited resources impose choices in determining targeted groups. Staffs recommend that youth be a priority in light of the potential cost of inaction (violence, conflict, etc.). Land-mine victims are also a identifiable important vulnerable group to target, with preventive actions very much needed (e.g., pursuing de-mining operations in areas still affected by land-mines, and providing health care to land-mine victims). Also, it would be useful to distinguish between vulnerable groups that are pursued under other pillars (such as to improve access to education), and those that only fit under this pillar (such as programs for youth or de-mining).

IV. RISKS AND CHALLENGES

23. Risks of lower than expected economic growth. The government aims to achieve an average real annual growth rate of at least 5 percent for the period beyond 2006. Staffs regard this target as overly optimistic particularly given historical trends and considering that the economy is still recovering from the damage of the 1998 conflict. During 2001–2005, the economy contracted by about 1 percent on average, and the fiscal situation was still difficult by end-2006 with a low tax performance (about 11 percent of GDP) and a relatively high

wage bill (around 13 percent of GDP). Also, the economy heavily depends on the production and export of a single commodity (raw cashew nut) often subject to climatic and price fluctuations. These initial conditions are likely to constrain the full implementation of the PRSP. In order to mitigate these risks, staffs encourage the authorities to accelerate ongoing fiscal and economic diversification reforms, particularly in the cashew sector.

24. **Risks of shortfalls in external assistance.** Four-fifth of the PRSP financing needs are expected to be funded by external donors in the form of concessional assistance. As the latter is tied to policy performance, any setback in implementing reforms would limit the government's capacity to mobilize such resources. Mitigating these risks will require short and medium-term interventions. In the short term, the government will need to: (i) stabilize the political situation; and (ii) develop a contingency plan to prioritize actions in line with actual domestic and external resources. In the medium term, the authorities will need to: (i) accelerate and sustain the implementation of economic reforms while preserving political stability; and (ii) continue to implement sound macroeconomic policies to minimize the potential negative effects of foreign aid.

25. **Risks related to the external debt.** A recent debt sustainability analysis (DSA) indicated that Guinea-Bissau is currently in a debt distress position. In these conditions there are clear risks that the country may not be able to timely service its debt to development partners. As a result, financial support from these partners may be delayed or suspended. As indicated above, prudent debt management and the sustained and accelerated implementation of economic reforms will be critical to address these risks.

V. CONCLUSION AND ISSUES FOR DISCUSSION

26. **Overall, staffs believe that the PRSP is an encouraging first step toward addressing Guinea-Bissau's medium-term development challenges.** The authorities have made progress in updating and strengthening their poverty reduction strategy in line with the recommendations made in the Joint Staff Assessment (JSA) of the I-PRSP approved by the Boards of IDA and IMF in November 2000. Key achievements include: (i) updating the poverty profile; (ii) divestiture of public enterprises; (iii) reducing bureaucratic barriers to private sector activities; (iv) adoption and implementation of a strategic framework to fight HIV/AIDS; (v) strengthening treasury management, public procurement and monitoring public expenditures through the establishment of an independent treasury committee; and (vi) improving costing, monitoring, and the participatory approach of the poverty reduction strategy.

27. **Looking forward, staffs recommend that further work be undertaken to strengthen the implementation of the PRSP.** Specifically, priority areas for the authorities are: (i) prioritizing the proposed activities under each strategic pillar; (ii) clearly identifying constraints to growth such as those resulting from low productivity of the country's resources and unexplored comparative advantages, while defining specific policies and programs to

address them; (iii) developing a detailed and sequenced strategy to improve governance, including in the emerging mining and oil activities; (iv) preparing a security sector reform strategy through a broad consultative process; and (v) strengthening the monitoring and evaluation framework, including by developing poverty statistics that are comparable over time and strengthening the capacity to collect and analyze poverty data.

28. In considering the authorities' PRSP and associated JSAN, Executive Directors' views are sought on whether they agree with the main areas identified by staffs as priorities for strengthening the PRSP and its implementation. Director's views are also sought on whether they concur with the areas identified by staffs as key implementation risks.