AFRICAN DEVELOPMENT FUND

MADAGASCAR

ENERGY SECTOR REFORM SUPPORT PROGRAMME (PARSE)

APPRAISAL REPORT

OSGE/ONEC DEPARTMENTS

November 2016

Translated Document

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CURRENCY EQUIVALENTS
September 2016

UA 1	=	EUR 1.25
UA 1	=	USD 1.39
UA 1	=	MGA 4215.8
UA 1	=	SDR 1.008

FISCAL YEAR
1 January to 31 December 2016

ACRONYMS AND ABBREVIATIONS

ADER	Rural Electrification Development Agency
ADF	African Development Fund
AFD	French Development Agency
AfDB	African Development Bank
CPIA	Country Policy and Institutional Assessment
CSP	Country Strategy Paper
JIRAMA	JIro sy RAno Malagasy (Malagasy Water and Electricity Company)
MFB	Ministry of Finance and Budget
MGA	Malagasy Ariary (currency unit)
PDN	National Development Plan
ORE	Electricity Regulatory Authority
PAGI	Institutional Governance Support Project
PAPI	Investment Promotion Support Project
PARGE	Economic Management Reform Support Programme
PRSP	Poverty Reduction Strategy Paper
PUP	Presidential Emergency Programme
SDR	Special Drawing Rights
TFP	Technical and Financial Partners
USD	United States Dollar
WB	World Bank

PROGRAMME INFORMATION SHEET

INSTRUMENT : ADF loan

PBO DESIGN MODEL : Sector budget support,
Single-tranche operation

LOAN INFORMATION

Client Information

BORROWER : **Republic of Madagascar**

EXECUTING AGENCY : **Ministry of Finance**

Financing Plan

Source	Amount (2016)
ADF – ADF LOAN	**UA 13.77 million**
World Bank	USD 65 million
France (AFD)	EUR 5 million

Key ADF Loan Information

Loan currency	UA
Interest type*	n/a
Interest rate margin*	n/a
Commitment charge*	0.5%
Service charge	0.75%
Repayment period	30 years
Grace period	10 years
Maturity	40 years

**as the case may be*

Implementation Schedule – Key Milestones (projected)

Programme identification	July 2016
Concept Note approval	September 2016
Programme approval	November 2016
Effectiveness	December 2016
Completion	December 2017
Last disbursement (single tranche)	December 2017

PROGRAMME EXECUTIVE SUMMARY

Paragraph	Issues to be addressed
General programme overview	Programme title: Energy Sector Reform Support Programme (PARSE) Expected results: PARSE will have a positive impact on the entire national economy and the Malagasy population. The improved financial health of the National Water and Electricity Company (JIRAMA) will enable the State to gradually reduce subsidies granted to the latter and devote its budget to investment expenditure that can generate sustainable and inclusive growth. Overall implementation schedule: Sector budget support (August 2016 - December 2017) Programme cost: UA 13.77 million
Programme outcomes	Improvement of JIRAMA's governance; improvement of the Company's financial management by reducing electricity generation costs and increasing its revenue recovery rate; improvement of electricity generation efficiency by contributing to better management of the thermal park and encouraging production diversification; improvement of the Company's service quality by reducing outages.
Alignment on Bank priorities	PARSE is aligned on Pillar I of the Bank's 2014-2016 Interim CSP for Madagascar, namely "Enhancing governance". The programme is also consistent with the priorities of the Bank's Ten-Year Strategy (2013-2022), notably infrastructure development, private sector promotion and good governance. It addresses two of the Bank's High 5s: "Light up and power Africa" and "Improve the quality of life for the people of Africa". It is also aligned on the Bank's New Deal on Energy for Africa (2016-2025), specifically in connection with building the capacity of power companies to guarantee their success (which is one of the 7 strategic themes selected). PARSE is also aligned on the Bank's Strategy for Addressing Fragility and Building Resilience in Africa (2014-2017), as well as on Pillars I "Public sector management and economic management" and II "Sector governance" of the 2014-2018 Governance Action Plan (GAP II). It is also consistent with the Programme-based Support Operations Policy
Needs assessment and rationale	The IMF approved an SDR 220 million Extended Credit Facility (ECF) for Madagascar in July 2016. One of the core conditions to be fulfilled by the Malagasy Government to benefit from this ECF, is to cover its financing deficit for the 2016 fiscal year, estimated at USD 45 million. The Malagasy Government then approached its technical and financial partners, including the Bank, to bridge the gap. The sector budget support programme helps to meet this urgent financing need by focusing on the priority area of energy, to which the State grants a large share of its current operating expenses.
Harmonization	Under this ECF, several Administration and public expenditure reform programmes are expected. A "public finance and budget support" partnership framework, comprising the World Bank, AFD, AfDB and EU, has been established. This group works actively for the establishment of a common matrix for evaluating Government's reform implementation performance. PARSE is aligned on this common matrix.
Bank's value-added	The Bank is one of Madagascar's key development partners. Although its interventions in the energy sector have so far been limited, the Bank remains an important partner for the next five years, with an ambitious intervention programme in the country. Therefore, this programme is strategic in that it will help to improve the overall governance framework of the energy sector to facilitate its implementation and ensure the impacts of future Bank interventions. By giving priority to the energy sector in its ten-year programme and implementing the New Deal on Energy for Africa, the Bank intends to be one of the privileged partners to support Madagascar in addressing its energy challenges. Furthermore, this programme reflects the Bank's capacity to adapt its interventions to the needs of a fragile member country, whose public finance management remains focused on emergency situations.
Contributions to gender equality and women's empowerment	The programme will help to improve the living conditions of women, who are particularly affected by outages. Women are active in the informal sector (small businesses, catering, handicrafts, food processing) and do not have enough resources to equip themselves with backup generators.
Policy dialogue and associated technical assistance	This operation is in line with the consolidation of dialogue with authorities within the framework of general budget support (PARGE) approved in March 2016. This dialogue will be backed by analytical work that will be produced by the World Bank-financed PAGOSE investment project, and the AfDB-financed PAPI and PAGI projects, namely: (i) JIRAMA's management improvement plan to enhance the Company's governance; (ii) the revenue protection programme to reduce non-technical losses; (iii) the preparation of an investment needs plan to reduce technical losses and improve electricity generation; (iv) the preparation of a public finance management modernization strategy; and (v) the feasibility study for a PPP study in the energy sector and support to the completion of the transaction.

RESULTS FRAMEWORK

Country/Project Title: MADAGASCAR/ENERGY SECTOR REFORM SUPPORT PROGRAMME (PARSE)
Project Goal: Improve energy sector performance to create conditions for inclusive economic growth

	RESULTS CHAIN	PERFORMANCE INDICATORS			MEANS OF VERIFICATION	RISKS/ MITIGATION MEASURES
		Indicator (including ISCs)	Baseline Situation	Target		
IMPACT	Inclusive and sustainable economic growth backed by an efficient energy sector	Gross Domestic Product (GDP) growth rate	3.1 in 2015	4.5% in 2017	MFB/IMF/UNDP	
		Equivalent Outage Time (EOT) per year	921 hours (total 2015)	500 hours in 2017 (estimate)	JIRAMA's activity report	
OUTCOMES	**OUTCOME 1: IMPROVEMENT OF JIRAMA'S GOVERNANCE AND FINANCIAL MANAGEMENT FRAMEWORK**	Increase in JIRAMA's recovery rate	40% in 2015	60% in 2017	JIRAMA's activity report	**Risk 1 :** The political and institutional risk that could affect the conduct of reforms **<u>Mitigation measure:</u>** The ongoing political dialogue, with international community support **Risk 2 :** Macroeconomic instability **<u>Mitigation measure</u>**: The affirmed political will, strengthened by the partnership established among technical and financial partners (including AfDB) around ongoing reforms, as well as the IMF's ECF **Risk 3 :** The weak institutional capacity to oversee and implement reforms as scheduled **<u>Mitigation measure:</u>** The will of the State to work together with JIRAMA to quickly exit the crisis **Risk 4:** Corruption **<u>Mitigation measure:</u>** The continued implementation of reforms to fight corruption, especially with the gradual establishment of anti-corruption units in ministries and institutions.
		Reduced connection time for new subscribers to electricity (this indicator is part of the performance contract)	450 days in 2015	350 days in 2017	Doing Business Report	
		Decrease in the level of subsidy necessary for the sector's financial balance	MGA 309 billion in 2015 (USD 101 million)	MGA 250 billion in 2017 (USD 83 million)	MFB/IMF	
	OUTCOME 2: IMPROVEMENT OF JIRAMA'S ELECTRICITY GENERATION EFFICIENCY AND SERVICE QUALITY	Improvement of the generator availability rate	58% in 2015	75% at the end of 2017	JIRAMA's activity report	
		Reduction in the production cost per kWh	MGA 681/kWh in 2015	MGA 670/kWh in 2017	JIRAMA's activity report	
OUTPUTS	**COMPONENT I: IMPROVEMENT OF JIRAMA'S PERFORMANCE: IMPROVEMENT OF THE GOVERNANCE AND FINANCE MANAGEMENT FRAMEWORK**					
	OUTPUT I.1: JIRAMA'S GOVERNANCE IS IMPROVED	JIRAMA's new organization chart is adopted and managers recruited through a call for applications.	JIRAMA's current organization chart is not efficient (especially as concerns commercial management)	Adoption in November 2016 of JIRAMA's new organization chart by the JIRAMA Board of Directors. 100% of managers recruited through call for applications in 2017. Gender objective: at least 30% of women in JIRAMA's decision-making organs and at least 40% in other positions.	Copies of the minutes of JIRAMA's Board of Directors adopting and implementing the new organization chart	
		The decree on the fight against electricity sub-sector fraud is revised and adopted	The system of fighting electricity sub-sector fraud is inefficient	Adoption in 2016 by the Council of Ministers of a Decree to strengthen the fight against electricity sub-sector fraud	Copy of the Decree on the fight against electricity sub-sector fraud adopted in the Council of Ministers	

	OUTPUT I.2 : JIRAMA'S FINANCIAL MANAGEMENT IS IMPROVED	Performance contract between the State and JIRAMA established	Absence of a performance contract between the State and JIRAMA	Signing of a performance contract between the State and JIRAMA in 2017	Copy of the performance contract signed between the State and JIRAMA	
		Action plan for implementation of the recommendations of the audit report on the management of JIRAMA's contracts is adopted and implemented	Recommendations of the audit report on the management of JIRAMA's contracts not implemented	Adoption of the action plan by JIRAMA's Board of Directors in 2016 and implementation of 80% of the recommendations of the audit report on the management of JIRAMA's contracts in 2017	Report on implementation of the recommendations of the audit report on the management of JIRAMA's contracts	
	COMPONENT II: IMPROVEMENT OF JIRAMA'S PRODUCTION EFFICIENCY AND SERVICE QUALITY					
	OUTPUT II.1: JIRAMA'S ELECTRICITY GENERATION IS IMPROVED (INCREASED AND DIVERSIFIED)	Conversion of the operating mode of thermal generators from diesel into fuel oil conducted and operational	0 MW of capacity converted in 2015	80 MW of installed capacity converted from diesel into fuel oil in 2017	Copy of JIRAMA's contracts for the purchase of parts for diesel into fuel oil conversion	
		Draft revised electricity sub-sector law, including the promotion of renewable energies, adopted	The current electricity sub-sector law is ill-adapted	Adoption by the Council of Ministers, in 2017, of a draft revised electricity sub-sector law	Copy of the draft revised electricity sub-sector law	
	OUTPUT II.2: JIRAMA'S SERVICE QUALITY IS IMPROVED	JIRAMA's fuel security stock constituted for 15 days	No security stock to ensure generator operation	Availability of a fuel security stock to ensure 15 days of operation for JIRAMA's generators in 2017.	JIRAMA's operation and technical reports	
		Preventive maintenance programme for JIRAMA's production plants adopted and implemented	Inexistence of a preventive maintenance programme for JIRAMA's thermal park	Preventive maintenance programme prepared in 2016, implemented and deployed in the Company in 2017	Copy of the minutes of JIRAMA's Board of Directors adopting a preventive maintenance programme for the Company's thermal park	
KEY ACTIVITIES	COMPONENTS Component I: Improvement of JIRAMA's performance (governance and financial management) Component II: Improvement of JIRAMA's electricity generation efficiency and service quality				RESOURCES UA 13.77 million	

I. INTRODUCTION: THE PROPOSAL

1.1. **Management hereby submits this proposal to grant a UA 13.77 million loan from ADF resources to the Republic of Madagascar for use in financing the Energy Sector Reform Support Programme (PARSE).** This is a sector budget support operation to assist the Government in its effort to provide a lasting response to the electricity sub-sector crisis.

1.2. **The Programme aims to intervene in the National Water and Electricity Company (JIRAMA), with a view to improving its performance and service quality.** The programme will help address energy sector constraints in order to meet the challenge of improving efficiency in providing services. Furthermore, JIRAMA's consolidation will enable the State to reduce the subsidies granted to the Company, thus re-channelling its resources to other social sectors capable of generating inclusive and sustainable economic growth.

1.3. PARSE is consistent with the orientations of the 2015-2019 National Development Plan (PND), which aims to achieve sustainable and inclusive economic growth that can generate multiplier effects on the income level, the quality of life of the population and in line with sustainable development principles. Intervention through budget support is justified by the need to provide an urgent response to the crisis facing the electricity sub-sector by helping the country to implement a series of reforms.

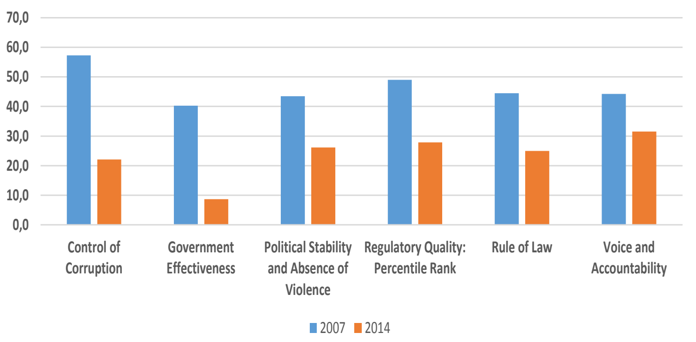
1.4. This is a single-tranche disbursement operation, but reform implementation covers the period 2016-2017. The priority reforms identified under this programme are the result of continuous dialogue with the Malagasy Government and development partners, which started in July 2016 and will continue throughout the programme's implementation up to December 2017. The programme's presentation to the Bank Board is subject to prior implementation of a number of reforms during the second half of 2016.

II. COUNTRY CONTEXT

2.1. Political Situation and Governance Context

2.1.1 After five years of political crisis (2009-2013), the Republic of Madagascar returned to constitutional order with the 2014 election of a new President, and the establishment of a new National Assembly. However, in 2015, this political stability was weakened by parliamentary motions to depose the President and motions of no-confidence on the Government. Although these motions did not succeed, they strained the political climate. The political situation has returned to normal in 2016. Divergences within the political class have helped to strengthen democracy, respect for freedoms and political rights. This recourse to political and constitutional mechanisms for inclusive political dialogue will enhance the political situation, necessary for development.

Figure 1: World Governance Indicators, World Bank (classification in percentile; high value = positive)



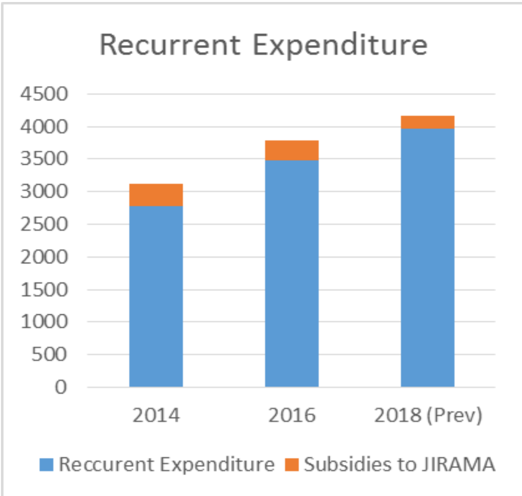
2.1.2 The 2009-2013 crisis affected key governance indicators in Madagascar. For instance, the country was ranked 29th out of 54 countries in the Mo Ibrahim Index in 2015, compared to the 9th position in 2009. Transparency International's corruption perception report ranked Madagascar 123rd out of 168 countries in 2015, with a 28/100 rating, 4 points down compared with the 32/100 rating recorded in 2012. Similarly, many governance indicators deteriorated during this crisis period, as shown in Figure 1 from a World Bank analysis. The country's poor governance also affects public companies, especially JIRAMA, which is unable to meet the population's electricity needs, and whose low performance hampers the improvement of the business climate. The situation is particularly worrying in terms of electricity connection.

According to the Doing Business report, to get connected to electricity in Madagascar, it takes 450 days and 6.2% of income per capita. Hence, the improvement of the electricity value chain is a major challenge for attracting private investors to the country. To promote good governance, economic recovery and the restoration of an attractive business climate, the Malagasy Government has committed to fight corruption at national level, through the implementation of the 2015-2025 National Anti-Corruption Strategy (SNLCC), officially launched in September 2015 by the President of the Republic. Furthermore, Madagascar regained membership of the Extractive Industries Transparency Initiative (EITI) in 2015. This has contributed to strengthening governance in the sector.

2.2. Recent Economic Trends, Macroeconomic and Budget Analysis

2.2.1 Madagascar's economic situation is characterized by renewed growth. After posting a 3.1% growth rate in 2015, medium-term prospects remain favourable (4.1% in 2016 and at least 4.5% from 2017). However, the progress made is still not enough to significantly reduce poverty. Inflationary pressures have been relatively contained in 2016, thanks to the prudent management policy implemented by the authorities. Thus, the average inflation rate should stand at below 7% in 2016. In addition, the economy remains highly vulnerable to declining commodity prices and climate shocks. The key drivers of the country's economic growth are agriculture, tourism, mining and the manufacturing sector. To consolidate the economic fundamentals, the Government concluded an SDR 220 million three-year Extended Credit Facility (ECF) with the IMF in July 2016.

2.2.2 Madagascar's public finance situation remains difficult in 2016. The tax revenue mobilization capacity is still weak, at 10.1% of GDP in 2015. Projections target 10.8% of GDP in 2016, which is still not enough to generate fiscal space favourable for strong and inclusive growth compared to Mauritius and the Seychelles (19% and 27.4% of GDP, respectively). For its part, public expenditure accounted for 15.5% of GDP in 2015, with a good proportion devoted to recurrent expenditure (at 12% of GDP in 2015). Although necessary to spur growth and create jobs, investment expenditure accounted for only 3.6% of GDP. The resulting overall budget balance deficit (commitments basis) is deteriorating: 3.3% of GDP in 2015, against 2.3% in 2014. In particular, Government should intensify reforms to strengthen public finance management (revenue recovery and public expenditure quality) and improve the business climate.



2.2.3 Provision has also been made to cap JIRIMA subsidies for 2016 at MGA 300 billion (USD 97 million), especially by settling part of fuel bills to oil distributors (subject of tripartite agreements) and payment of the Company's bills from generator providers. However, the expected increase in tax revenue in 2016 will not be sufficient to cover increased budget expenditure, thus preventing any improvement in public finances.

2.2.4 To rationalize public expenditure, the Government has committed to gradually reduce transfers to JIRAMA. This effort will be supported by implementing the Company's management improvement plan approved in February 2016, and the execution of PAGOSE project activities financed by the World Bank to the tune of USD 65 million. PAGOSE aims at: (i) improving the electricity sub-sector's planning and financial sustainability; (ii) enhancing JIRAMA's operational performance and governance; and (iii) investing in more reliable electricity.

2.2.5 Madagascar's total debt was estimated at USD 3.7 billion or 41% of GDP in 2015. According to the August 2016 IMF report, the external debt component contracted and guaranteed by the State (CGE) is expected to reach 30% of GDP by end-2016, while the domestic debt component should stand at 11% of GDP. According to this debt sustainability analysis, Madagascar's debt distress risk is deemed "moderate". Thus, the debt contracted and guaranteed by the State remains sustainable, although low mobilization of budget revenue, external exchange rate shocks and contingent liabilities related to public enterprises are still sources of vulnerability.

2.3. *Competitiveness of the Economy*

Table 1. Doing Business Indicators

Indicators	DB 2016	DB 2015	DB 2009
Starting a business	128	112	58
Dealing with construction permits	182	183	102
Getting electricity	188	188	
Registering property	161	162	145
Getting credit	167	180	172
Protecting investors	105	109	53
Paying taxes	76	72	92
Trading across borders	125	128	109
Enforcing contracts	153	153	153
Resolving insolvency	127	128	
OVERALL RANK	164	166	144
Source: Doing Business, www.doingbusiness.org			

Madagascar is among the group of African countries where doing business is difficult. The business climate deteriorated significantly during the 2009 to 2013 political crisis due mainly to the sharp decline in governance indicators. In such a context, the economy is characterized by the predominance of the "informal" sector. Thus, nearly half of the economy was informal in 2015. The private sector faces several constraints. In addition to fraud and unfair competition which hamper national manufacturing enterprises, the private sector also faces the challenges of access to credit (guarantee and costs), and lack of road and energy infrastructure, resulting in high factor costs. The sector also faces the low efficiency of the judicial system and institutional instability. The country was ranked 164th in terms of overall ease of doing business, out of 189 countries considered in the 2016 Doing Business Report, compared to the 144th position in the 2009 report.

2.4. *Energy Sector Review*

2.4.1 Energy sector institutions include: (i) the Ministry of Energy and Hydrocarbons (MEH) which prepares and coordinates the implementation of the policy applicable to electricity and hydrocarbons management; (ii) the National Water and Electricity Company (JIRAMA), responsible for operating the network; (iii) the Electricity Regulatory Authority (ORE) which, among other activities, analyses and publishes electricity tariffs; (iv) the Rural Electrification Development Agency (ADER), responsible for promoting and developing rural electrification both within interconnected networks and in off-grid centres and rural areas; and (v) private operators and license holders, who sign generator leasing contracts with MEH, the licensing authority.

2.4.2 With the State as single shareholder, JIRAMA faces serious difficulties and is currently unable to fulfil its basic missions of ensuring continued, reliable and sustainable energy supply, executing connection, minor and major extension works, and supplying stable and quality voltage. Its overall performance dropped from 75% in 2009 to 66% in 2015. JIRAMA has about 6 000 workers, 43% of whom are assigned to the electricity sector, 16% to the water sector and 41% to the two sectors; 20% of overall staff (about 1 200 workers) are management executives.

2.4.3 The Malagasy electricity network comprises three regions, each with interconnected networks (Antananarivo, Toamasina and Fianarantsoa), and 130 centres of off-grid networks. While the interconnected networks are served partly by hydropower plants, the off-grid centres are for the most part supplied by thermal generators. The electricity system's total installed capacity stood at 642 MW in 2015, including 315 MW generated solely by JIRAMA, which is the only distributor. In 2015, electricity generation rose to 1 542 GWh, including 1 077 GWh (70%) injected into interconnected networks. Of this, JIRIMA supplied 68.8% (1 061 GWh) and the private sector 31.2%. In 2015, the energy mix on the entire network stood at 60% for hydropower generation and 40% for thermal generation. While private generation is essentially thermal, JIRAMA's mix comprises 87.7% hydropower (930 GWh) and 22.3% thermal.

2.4.4 The energy sector situation is characterized by the low access rate to modern forms of energy and the massive use of biomass to meet the energy needs of the population. The national electricity access rate stands at 15% (57% in urban areas and 4% in rural areas). The sector is also marked by a steady increase in imports of petroleum products to meet road transport and power generation needs. While the country has huge hydropower (7 800 MW, only 1.6% harnessed), solar (2 000 kWh/m2/year) and wind (2 000 MW) potential, the thermal park generates 75% of the electricity. The low development of the renewable energy potential, particularly hydropower (only 128 MW), coupled with the sector's poor management, focused on emergency, explain the sub-sector's poor development level and the technical, financial (negative income entailing State subsidies to ensure fuel supply) and commercial (40% recovery rate) under-performance of the main operator, JIRAMA. To date, the Company does not have the necessary resources to constitute a fuel security stock or acquire spare parts for preventive maintenance of the production plants. Thus, service quality is affected by outages and long waiting times for new subscriber connections. To deal with these sector difficulties, the Malagasy Government took various measures: (i) granting of subsidy to JIRAMA for the purchase of fuel to operate thermal generators and another subsidy to rent generators from private operators ; (ii) the preparation of the 2014-2019 JIRAMA Recovery Plan; (iv) the establishment of a JIRAMA Reform Strategic Committee (bringing together the ministers in charge of finance, energy and hydrocarbons, water, the Governor of the Central Bank, the Adviser to the President of the Republic for Economic Affairs, the Director-General of the Treasury), to support the Company in its strategic orientations and decisions; (iii) the adoption of the National Development Plan which aims, among others, to "supply low-cost energy to support economic growth as well as sustainable and inclusive development"; and (iv) the approval by the Government of the New Electricity Policy (PNE 2015-2030) which aims, in the context of the electricity sub-sector, to "reach a 70% access rate to a modern source of energy by 2030, while increasing the renewable energy share in the energy mix to 85%".

2.5. Public Finance Management

2.5.1 Madagascar's public finance situation remains delicate; the reforms started after the crisis have not produced the expected results. The 2014 Public Expenditure and Financial Accountability (PEFA)[1] self-report recommendations stress the urgent need to strengthen public finance management. Nine performance indicators were revised downwards in the 2014 assessment compared to the 2008 report (just before the 2009 political crisis) (Technical Annex IV). Expenditure assessment reveals inconsistencies between budget forecasts (unchanged rating at D) and budget execution (drop from A to C+ in the rating), both in terms of amounts and their composition. At the level of the expenditure chain, the infra-annual budget execution profile is unbalanced, with most of the commitments being deferred to the end of the year. The application of the Organic Law on the Finance Act (LOLF) is not yet complete. Weaknesses in budget execution mechanisms make control difficult and affect public expenditure quality.

2.5.2 In light of the outcomes of the PEFA 2014 assessment, the Government adopted a Priority Action Plan (PAP) in October 2014, for the 2014-2015 public finance management (PFM) reforms. Among the progress made in PAP implementation, it is worth mentioning the census of public bodies; the preparation of Budget Review Acts for 2008 to 2014; the prioritization of public expenditure, including increased transparency and the gradual introduction of long-term budgeting; and the strengthening of procurement procedures. To take over from PAP, the Bank is providing support to the Malagasy Government through the PAGI project, to prepare a PFM reform strategy that will cover the 2016-2020 period. Thus, one of the main objectives of this new strategy will be to expand fiscal space, in order to increase the level and efficiency of pro-poor expenditure and economic growth through structuring public investments.

2.6. Inclusive Growth, Poverty Situation and Social Context

2.6.1 Although there is a gradual upturn in economic growth in the country, progress made is still not enough to significantly reduce poverty. Both poverty and inequalities have remained persistent in Madagascar. According to 2013 data, poverty affected more than 80.3% of the population, while the extreme poverty rate stood at 70.1%. The situation does not seem to have improved in recent years due mainly to recurrent food insecurity (87.9% overall incidence) and the country's high vulnerability to climate shocks (drought, floods and cyclones).

2.6.2 Furthermore, the impact of political and economic fragility has created social fault lines, by accentuating poverty and inequalities, especially between the rural area, on the one hand, and the urban area, on the other hand, leading to low access of rural dwellers to basic economic infrastructure (transport and energy). Madagascar is among the poorest countries in sub-Saharan Africa. The 2013 Human Development Report ranks the country 151st out of 186, with a human development index (HDI) of 0.483. In Madagascar, poverty is a major cross-cutting issue and touches all segments of the society. Given this situation, all the Millennium Development Goals (MDGs) have not been achieved in Madagascar.

[1] *Public Expenditure and Financial Accountability*

2.6.3 In addition, the economic, health and environmental consequences of lack of electricity access are dramatic: the dissemination of vaccines and the development of modern medicine are hampered for lack of refrigeration, and the massive use of wood as a source of domestic energy causes diseases from pollution of indoor air, and accelerates deforestation.

2.6.4 In terms of gender, inequalities remain. For instance, latest report indicates that Madagascar has a Global Gender Gap index of 0.698 (1 corresponds to gender equality) and was ranked 74th out of 145 countries in 2015. Nevertheless, despite a partial implementation of the 2000-2015 National Women's Promotion Policy and the 2004-2008 Gender and Development National Action Plan (PANAGED) due to the various crises that the country has gone through, progress has been made in terms of education (access to education is almost equal with a 0.9 rating). Women's participation in politics is still difficult, but in terms of participation in economic activities, Madagascar is ranked among the first 10 balanced countries (88% of women are economically active, compared to 91% of Malagasy men, although they are increasing engaged in informal activities). Madagascar's 2015-2019 National Development Plan has mainstreamed gender in the country's priority themes and strategic areas. Vulnerable segments in Madagascar, especially women and girls, will benefit from public investments in the social sectors that the programme intends to support. There is effective gender parity at the primary and secondary education level.

2.6.5 The country is also characterized by under-employment, especially among youths and women. Unemployment affects women more than men (1.5% and 1%, respectively). In 2012, six unemployed persons out of ten were women (58.5%). Furthermore, although the unemployment rate is relatively low (4.5% in the urban area and 1.1% in the rural area), more than 80% of workers have low-paid jobs (low salaries, insecure jobs, under-employment), whereas more than 400 000 youths enter the job market each year. The informal sector, whose productivity is still low, remains the main provider of low-paid jobs and without social security. In addition, poor energy supply service quality in urban centres makes this sector's actors highly vulnerable.

III. GOVERNMENT'S DEVELOPMENT PROGRAMME

3.1. Government's Overall Development Strategy and Medium-Term Reform Priorities

3.1.1 Malagasy authorities adopted the National Development Plan (PND) in 2015 for the period 2015-2019. This plan is the main reference framework for the country's development policy. The PND is based on five thrusts: (i) governance, the rule of law, security, decentralization, democracy and national solidarity; (ii) preservation of macroeconomic stability and support to development; (iii) inclusive growth and regional anchoring of development; (iv) adequate human capital for the development process; and (v) enhancing natural capital and building resilience to disaster risks. Thus, PARSE is based on the PND's first three (3) thrusts.

3.1.2 In addition, the Government has adopted *Madagascar's Letter of Energy Policy 2015-2030*, which aims to increase the household access rate to modern and affordable electricity from 15% to 70%, by massively harnessing renewable sources of energy to preserve the ecological heritage and participate in the global effort to fight climate change and its repercussions.

3.2. Obstacles to Implementing the National/Sector Development Programme

3.2.1 The electricity sub-sector is facing various challenges. The country's island situation (Madagascar is situated 1 200 km of the Mozambique coast) prevents it from benefiting from regional interconnections to cover its production deficits and reduce investment needs. The State's inadequate financial resources and the low tariffs make it impossible to mobilize the substantial capital needed to develop the huge hydropower potential. The repeated crises (2002, and then 2009 to 2013) seriously affected electricity sector governance. The sector reforms initiated at the beginning of 1999 to ensure its recovery and development did not bear fruit because the various instruments adopted for this purpose were not properly applied. Such instruments include the common provisions for granting authorizations and concessions to private companies, the specific provisions for tariff regulation, monitoring, control and sanctions against fraud provided for by Law No. 98-032 reforming the electricity sub-sector. This law aims to secure private sector investments to meet the minimum expectations of potential private investors, and sets out the guiding principles for determining electricity sales tariffs. Law No. 98-032 further institutes an independent regulatory organ, ORE, which still lacks the needed resources and autonomy to fully fulfil its mission.

3.2.2 JIRAMA has faced a series of difficulties in recent years due to lack of investments in production and distribution. Similarly, preventive equipment maintenance was not properly carried out due to lack of financial resources to acquire spare parts. These difficulties affected service quality and hampered the country's electrification. Madagascar's electricity access rate is extremely low (15%). JIRAMA is now unable to meet demand for new connections, due to lack of resources to acquire connection equipment: 26 000 customers are still waiting to be connected, since 2014. The distribution network is obsolete, marked by equipment capacity limits and untimely disruptions of electricity supply (more than 80% of distribution transformers are overloaded). Outages are recurrent due, on the one hand, to the unavailability of several thermal generators which, although accounting for 75% of installed capacity, were only able to supply 39% of electricity in 2015 as a result of breakdowns and, on the other hand, to fuel shortages. The thermal park is a heavy burden on JIRAMA's finances, with an excessive oil bill estimated at MGA 636 billion (USD 215 million) for 2016. To mitigate the impacts on consumers, the State intervenes massively by contributing to the fuel bill. This subsidy rose to about MGA 309 billion (USD 101 million) in 2015, constituting a huge burden on public finances. Revenue is clearly inadequate and JIRAMA is in a chronically poor financial situation. Electricity is sold at far below the cost price and revenue collection is uncertain. Low revenue collection is attributable to: (i) heavy network losses, since 37% of the energy produced is not billed (about 60% of these losses are estimated non-technical losses); and (ii) the low customer bill recovery rate, at only 40%. Consequently, JIRAMA's turnover (USD 155 million in 2015; USD 150 million in 2014; and USD 146 million in 2013) is not enough to cover operating expenses (USD 204 million in 2015; USD 198 million in 2014; and USD 185 million in 2013). In particular, debts owed to generator providers have continued to accumulate to reach USD 16 million as at 31 July 2016. To try to improve JIRAMA's financial situation, the Malagasy Government, based on an IMF recommendation, approved a 15% tariff increase in 2016, but this will not be enough to bridge the gap between the cost price and sales price of electricity.

3.2.3 The electricity sub-sector's poor performance is now one of the major handicaps to Madagascar's economic and social development. To remedy this situation, the Government revised Law No. 98-032 to include provisions relating to harnessing of renewable sources of energy by the private sector while taking measures to apply the provisions recommending the sector's autonomy and transparency. Thus, an audit of JIRAMA's energy supply contracts with private operators was conducted. This audit highlights the operator's alarming situation and considers most of the hired generators as second-hand units in a very bad state, running at only 42% of their capacity. It also specifies that out of the 77 contracts signed between JIRAMA and some twenty operators, 36 can be deemed suspected cases of procurement circumvention. None of the audit recommendations have so far been implemented.

3.2.4 JIRAMA's difficulties are due mainly to: (i) lack of appropriate maintenance of generation, transmission and distribution equipment; (ii) transmission and distribution equipment that operate below capacity for lack of investments; (iii) the high fuel budget due mainly to the specific consumptions of thermal generators that operate on diesel; (iv) the low bill recovery rate; (v) the low network output characterized by excessively high losses (technical and non-technical); and (vi) and governance problems. From the discussions with Malagasy authorities, it emerges, among others, that there is need to: (i) improve JIRAMA's operational and commercial performance, (ii) promote private investments in the production sector; (iii) improve conditions for electricity access for Malagasy households; and (iv) ensure good governance in JIRAMA's management.

3.3. Consultation and Participation Process

3.3.1 Programme design benefitted from wide consultations that involved various energy sector reform stakeholders. Thus, the Bank's programme preparation and appraisal missions held consultations with JIRAMA, the Ministry of Finance and Budget, the Ministry of Energy, the Ministry of Water, ADER, ORE, and representatives of civil society organizations working in the environmental, energy and consumer protection sectors. Consultations were also held with the sector's key technical and financial partners (IMF, World Bank, AFD, EU, and GIZ) to harmonize their interventions.

3.3.2 The participatory process will be sustained during programme implementation, by the Bank, other stakeholders and beneficiaries through: (i) meetings of the budget support group as part of assessing the performance of the country's development strategy; (ii) meetings within the framework of the Bank's strategic dialogue with authorities; and (iii) Bank supervision missions. Furthermore, the various stakeholders and beneficiary groups will be associated with the preparation of the completion report.

IV. BANK SUPPORT FOR THE GOVERNMENT STRATEGY

4.1. Linkage with the Bank Strategy

PARSE is aligned on the Bank's 2014-2016 Interim Country Strategy Paper (CSP) for Madagascar. This Interim CSP is based on two pillars: (i) enhancing governance; and (ii) development of rural and access infrastructure.

PARSE is also aligned on Pillar I of the Bank's 2014-2016 Interim CSP for Madagascar, namely "Enhancing governance". The programme is consistent with the Bank's Ten-Year Strategy (2013-2022) priorities, notably infrastructure development, private sector promotion and good governance, and addresses one of the Bank's High 5s: "Light up Africa". It is also aligned on Pillars I: "Public sector management and economic management" and Pillar II: "Sector governance" of the 2014-2018 Governance Action Plan (GAP II). Lastly, it is in line with the Bank's 2014-2019 Strategy for Addressing Fragility and Strengthening Resilience in Africa. PARSE will eventually help to implement the 2014-2018 Gender Strategy, "Investing in Gender Equality for Africa's Transformation", under Pillar 2, "Economic empowerment".

Table 2.
Linkage between the PND, CSP, New Deal on Energy for Africa and the Operation

<table>
<tr><th>2015 -2019

PND</th><th colspan="2">New Deal on Energy for Africa Strategy</th><th>2014-2016 Interim CSP</th><th>PARSE</th></tr>
<tr><td>Strategic objective:

"Create conditions for steady, shared and sustainable economic growth"</td><td colspan="2">Strategic objective:

"Contribute to transforming the energy sector in Africa to promote inclusive growth and the transition to green growth, through increased production, expanded access to energy, improved energy reliability and increased energy efficiency, while improving energy system sustainability"</td><td>Strategic objective:

"Contribute to the country's economic and social recovery, on an inclusive and sustainable basis"</td><td>Strategic objective:

"Improve energy sector performance to create conditions for inclusive economic growth"</td></tr>
<tr><td rowspan="2">Thrust I: Governance</td><td colspan="2">Principle IV: Support to African governments in their efforts to improve their policies, regulations and energy governance mechanisms.</td><td rowspan="2">Pillar I: "Enhancing governance"</td><td>Component I: "Improvement of JIRAMA's performance: (from governance to financial management)"</td></tr>
<tr><td>Theme I: Institution of a favourable environment framework for reforms</td><td>Theme II: Capacity building for electricity companies to ensure their success.</td><td>Component II: "Improvement of JIRAMA's production efficiency and service quality"</td></tr>
</table>

4.2. Compliance with Eligibility Criteria

Madagascar is one of the States in transition. In addition, Government's commitment to reduce poverty is reflected in the National Development Plan (PND), which covers the period 2015 -2019. With regard to macroeconomic stability, the country concluded a three-year programme on 27 July 2016, under the IMF's

Extended Credit Facility (ECF), for SDR 220 million. As concerns fiduciary assessment, an ORPF.2 review conducted in 2016 found the overall fiduciary risk substantial but with a positive trend since 2013, in terms of implementation of reforms to improve public finance management performance. With respect to political stability, the country is on a positive path towards strengthening its institutions.

4.3. Collaboration and Coordination with Other Partners

The programme was designed to complement the interventions of other donors within the Partnership Framework, for better effectiveness of support operations. Technical Annex III details partners' interventions. With the normalization of the political situation, technical and financial partners (TFP) launched the mechanism to coordinate their efforts in terms of political dialogue, and alignment and harmonization of their interventions. They coordinate their activities through sector and thematic groups: private sector, governance/budget support, rural development, environment, decentralization, transport, energy, education and health. The Bank is the leader of the "Drinking Water and Sanitation" and "Rural Development" consultation frameworks. It participates actively in budget support operations with the WB, EU, and AFD. Several programmes for the reform of the administration and public expenditure are awaited under the IMF's ECF: improvement of public expenditure management, increase in tax revenue, strengthening of the fight against corruption as well as JIRAMA's recovery. Thus, PARSE reforms were discussed with members of the Partnership Framework and chosen on the basis of comparative advantage and each stakeholder's value added, with a view to harmonization and complementarity, in accordance with the Paris Declaration and the Busan Principles on Aid Effectiveness.

4.4. Linkage with Other Bank Operations

4.4.1 The total portfolio financed by the Bank as at 31 August 2016 stands at UA 178.76 million for 10 projects. The portfolio covers five sectors (Agriculture 52.81%; Transport 32.56%; Governance 13.43%; Water and Sanitation 0.81%; and Health 0.4%). The active portfolio's overall disbursement rate, comprising 7 projects (UA 164.7 million), stands at 21.39% as at 31 August 2016 for an average age of 1.2 years. The portfolio's performance is deemed satisfactory, with a 2.75 rating on a scale of 1 to 4. The active portfolio contains no problem project.

4.4.2 PARSE is complementary to ongoing governance strengthening operations (PAGI and PARGE), in light of their objective of improving the creation of fiscal space that will enable the State to finance public investment projects, including energy projects. PARSE is also in line with the PAPI Project, which aims to improve private investment promotion in priority sectors (including energy) in Madagascar. In 2007, the Bank granted EUR 6 million financing to a private promoter to build a hydropower plant in Sahanivotry, through its private sector window. PARSE will help to create conditions that will enable JIRAMA to honour the terms of the contract to purchase electricity generated by the plant. In addition, it is linked to the ongoing feasibility study for the preparation of an electricity generation project in Nosy-be, financed by SEFA.

4.4.3 PARSE design took into account lessons learned from similar Bank operations in Madagascar, in this case the Poverty Reduction Budget Support Programme Phase II (PABRP - II) approved in 2008, the Economic Recovery Emergency Programme (PURE) approved in 2014 after the crisis, and the Economic Management Reform Support Programme (PARGE), approved in March 2016 and still in the implementation phase (the outcomes of these support operations are detailed in Technical Annex IV). Lessons from implementing these operations mostly concern: (i) the need for budget support operations to be backed by investment projects targeting the same priority areas; (ii) consideration of the political dimension of certain reforms by choosing only measures over which the Government has effective control; and (iii) the prioritization of structuring reforms, taking into account the country's fragile situation and the capacity of implementation structures. The identification of PARSE reforms took these lessons into account by targeting measures that will be backed by investment projects, and that are achievable on schedule, given their importance and lasting impact.

Table 3. Lessons from Previous Bank Operations in the Country

Key lessons learned	Measures taken to include the lessons in the programme
The need for budget support operations to be backed by investment projects targeting the same priority areas	Ongoing investment projects will support Malagasy authorities technically in implementing the reforms of this budget support operation. These are the PAGOSE project, financed by the World Bank, and the GIZ PRC-ELEC project
The consideration of the political dimension of certain reforms by choosing only measures over which the Government has effective control	The improvement of energy sector management is a priority for Malagasy authorities, and PARSE reforms help to achieve this objective.
The prioritization of structuring reforms by taking into account the country's fragile situation and the capacity of implementation structures	The choice of reforms was made by ensuring that their outcomes/impacts provide a lasting response to the electricity sub-sector crisis. PARSE lays emphasis on the effective operationalization of these reforms.

4.5. Analytical Work Underpinning the PBO

Programme design benefitted from the results of several analytical works carried out by various stakeholders, including: (i) JIRAMA's business plan; (ii) JIRAMA's recovery plan; (iii) the sector note of the PAGOSE project, financed by the World Bank; (iv) the New Energy Policy (NPE); (v) Analytical work behind the Bank's CSP 2017-2019; (vi) the audit report of JIRAMA's contracts; and (vii) Government's PND and PUP. The conclusions of these studies and reports helped to better identify the main causes of the problems plaguing the energy sector. These analyses all point to the need to improve JIRAMA's institutional and financial governance, to create conditions for the Company's streamlining and autonomy vis-à-vis the State.

V. THE PROPOSED PROGRAMME

5.1. Programme Goal and Objective

PARSE's main objective is to contribute to eliminating constraints to the electricity sub-sector's development in Madagascar, while creating favourable conditions for investment and inclusive growth. The specific objectives are to: (i) contribute to improving JIRAMA's performance (governance and financial management); and (ii) improve JIRAMA's production efficiency and service quality.

Bank support is also justified by the Malagasy Government's request, addressed to the Bank on 17 June 2016, to meet the urgent financial needs of the 2016 budget, whose deficit is estimated at USD 45 million. Coverage of this deficit was one of the key conditions that the Malagasy Government had to accept to conclude an agreement with the IMF under the Extended Credit Facility (ECF).

This programme is the first in a series of programmes that will support energy sector reform, especially under the Bank's next intervention strategy for Madagascar, covering the period 2017 - 2021.

5.2. Programme Components

PARSE is divided into two components: (i) Improvement of JIRAMA's governance framework and financial management; and (ii) Improvement of JIRAMA's production and service quality.

5.2.1. Component 1: Improvement of JIRAMA's Governance Framework and Financial Management

Issues and challenges

The electricity sub-sector's poor performance is one of the major handicaps to Madagascar's economic and social development. This is characterized by the low electricity access rate, poor service quality marked by recurrent outages, and JIRAMA's low technical, commercial and financial performance.

The electricity sub-sector is seriously handicapped by the State's (single shareholder) inadequate financial resources, as well as sector governance problems and abandonment of the recovery measures adopted at the beginning of the 2000s (particularly the termination of the management contract in 2009, which exhausted external concessional sources of financing and led to the abandonment of the sector's development plan). To address the production shortfall that emerged from this period, recourse was made to private operators through energy purchase contracts and rental of diesel plants and generators, without resorting to competition, in a context of increasing fuel prices. These decisions exacerbated JIRAMA's financial difficulties and led to the abandonment of preventive maintenance of the production plants, whereas the Company has the required technical competencies.

Recent measures adopted by the Government

To reform JIRAMA, the Government in 2015 conducted an audit of the Company's energy supply contracts with private producers. In this context, JIRAMA now publishes quarterly, on its website, certain data on ongoing contracts (the list of private operators that obtained these contracts as well as the current cost per kWh of each contract and the cost provided in the contract terms).

The Government has also prepared a sector performance improvement plan, finalization of which is planned for the coming weeks. This improvement plan provides for a new organization chart for JIRAMA and the strengthening of certain functions, including the commercial function. JIRAMA's management improvement plan also provides for the setting up of an integrated information system (human resources management, budget, accounting, procurement, inventory management, sales management, repairs management, geographic information system, telemetry system, etc.). Furthermore, the new anti-corruption law came into force in September 2016.

Programme activities

PARSE is expected to help address the deeper issues that hinder the electricity sub-sector's development. The Bank will also support Madagascar in implementing the following reforms: (i) the implementation of JIRAMA's new organization chart (which takes women's involvement into account); (ii) the establishment of a regulatory system to fight against electricity fraud, especially by adopting the related decree; (iii) the implementation of the performance contract between the State and JIRAMA, which specifies the two parties' commitments to improve the electricity sub-sector's situation through control of JIRAMA's costs, electricity development and sub-sector financial balance; and (iv) the implementation of the recommendations of the audit report on JIRAMA's contracts with private suppliers, to improve transparency and efficiency in the supply of goods and services to the Company. In this regard, **the adoption and operationalization of JIRAMA's management improvement plan, the adoption of the decree to fight against electricity fraud, the adoption of JIRAMA's new organization chart and the preparation of an action plan for implementation of the recommendations contained in the audit report on the Company's contracts (Delta Conseil)**, will be measures precedent that the Malagasy Government must fulfil before PARSE's presentation to the ADF Board of Directors. The implementation of all the measures under this programme component by the end of 2017, should help achieve the following results: (i) control of JIRAMA's costs and sub-sector financial balance, especially with the Company's recovery rate increasing from 40% in 2015 to 60% in 2016; (ii) improvement of JIRAMA's governance, especially by reducing the level of the balancing subsidy from MGA 309 billion in 2015 to MGA 250 billion in 2017, and reducing connection time for new electricity subscribers from an average of 450 days in 2015 to 350 days in 2017.

5.2.2. Component 2: Improvement of JIRAMA's Production and Service Quality.

Issues and challenges

Low development of the renewable energy potential, particularly hydropower (only 128 MW harnessed out of a 7 800 MW potential), coupled with poor sector management that focuses on emergency, largely explain the electricity sub-sector's poor development level and its under-performance. To remedy this situation, it is essential to create conditions for the restoration of sector planning, based on the development of renewable energies, while ensuring service quality commensurate with the efforts made by the State and JIRAMA customers, who will bear the unavoidable tariff adjustments. To this end, it is essential to improve electricity generation efficiency (by reducing costs) and service quality (by reducing outages).

The constraints to production activities caused by JIRAMA's poor financial situation, the signing of electricity purchase contracts and rental of plants and generators under non-optimum conditions (heterogeneous park, high rental and operating costs, performance below specifications, unfavourable or unapplied contractual clauses) must be eliminated. JIRAMA is now unable to constitute a fuel security stock to operate the plants or acquire spare parts for preventive maintenance of the thermal park, which leads to a spiral of increased operating expenses and deterioration in service quality marked by outages and long waiting time for new subscriber connections. Thus, fuel costs increased from 40 to 103% of the turnover between 2009 and 2014, before dropping slightly in 2015 (86%) following the fall of oil prices. The availability rate, measured by the ratio between the available capacity and the installed capacity, fell from 74% in 2009 to 61% in 2014, then further dropped to 55% in 2015.

Recent measures adopted by the Government

To remedy the electricity sub-sector situation, the Government embarked on the revision of Law No. 98-032 reforming the sector to include provisions on the harnessing of renewable sources of energy, while taking measures to apply the provisions recommending the sector's autonomy and transparency. More recently, the Government published the *'Letter of Energy Policy 2015-2030.* This document summarizes the main thrusts, objectives and strategies adopted to increase the household access rate to modern and affordable electricity from 15 to 70% by 2030, by massively harnessing renewable sources of energy to preserve ecological heritage and take part in the global effort to fight climate change and its repercussions. The new energy paper is based on five major thrusts: (i) enhancing natural capital and preserving the environment; (ii) access to sustainable energy for all, through the development of an electrification plan for rural, suburban and urban communities; (iii) ensuring the country's energy security and independence; (iv) adaptation and strengthening of the regulatory/institutional framework and the business environment; and (v) sustainable financing of energy needs.

The NPE "recommends a combination of technological approaches and methods that preserve and develop the country's natural energy resources, as well as an energy mix associating renewable energies, hydrocarbons and other thermal resources, by making the most of opportunities for extension and interconnection of networks and mini-grids, based on the principles of least cost and technological neutrality to achieve defined energy objectives".

The Government has also taken action to ensure continuity of services provided by JIRAMA, especially with the subsidization of fuel purchase and generator rental. The total amount of the subsidy provided for 2016 is capped at USD 300 million.

Programme activities

This second component aims to intervene at more technical levels to support measures that will have a direct impact on JIRAMA's production and service quality.

Although totalling about 40% of 2015 production, thermal generation absorbs a fuel bill of MGA 636 billion (USD 190 million at the December 2015 rate) for a turnover of USD 155 million, a situation that stifles any other effort elsewhere. The Bank has targeted reform measures aimed at securing thermal generation and reducing its cost. These reforms are also supported by the IMF, AFD and WB.

Under this component, the Bank will support Government's efforts to implement the following measures: (i) conversion of the operating mode of thermal generators from diesel into fuel oil (80 MW in 2017) to reduce fuel costs; (ii) institution of the revised electricity law to include the promotion of renewable energies (2017), with a view to developing national potential; (iii) constitution of a fuel security stock that can ensure continuity of service for 15 days (2017); (iv) implementation of a preventive maintenance programme for the thermal park to reduce fuel consumption and generator rental costs (2017), by improving the availability rate of the generating fleet. The implementation of these measures will eventually help to improve the quality of services provided by JIRAMA to its customers, especially by reducing outages. In this regard, a single measure precedent to presentation of the programme to the ADF Board of Directors was identified for this component, namely the **preparation of a preventive maintenance programme for the thermal park, including needs, programme financing arrangements and analysis of the financial impact of this maintenance on the reduction of fuel consumption and generator rental costs**. The implementation of all measures under this programme component by end-2017, should help achieve the following results: (i) improvement of electricity generation, with the availability rate rising from 58% in 2015 to 75% in 2017, as well as a slight decrease in the cost price per KWh; and (ii) creation of a favourable legal framework for the promotion of renewable energies to better develop the country's potential

5.3. Policy Dialogue

The programme's areas of intervention will be subject to continuous dialogue between the authorities, TFPs and the Bank. The dialogue on programme reforms, which started since July 2016, will continue during 2017 by laying emphasis on areas supported by the programme. The dialogue on supported reforms is taking place in a transparent manner with Malagasy authorities, and in a consultative and complementary manner with development partners in the areas of intervention within the Budget Support/Public Finance Partnership Framework. The dialogue will be backed by analytical work that will be produced through the World Bank-financed PAGOSE investment project, and the AfDB-financed PAPI and PAGI projects, including: (i) the JIRAMA management improvement plan to enhance the Company's governance; (ii) the revenue protection programme to reduce non-technical losses; (iii) the preparation of an investment needs plan to reduce technical losses and improve electricity generation; (iv) the preparation of the public finance management modernization strategy; and (v) the feasibility study for a PPP project in the energy sector and support for the completion of the transaction.

5.4. Loan-related Conditions

Following dialogue with the country's authorities, the Government committed to implement a set of measures, before presenting the programme to the Bank Group's Board of Directors. The structuring nature of these measures led to their selection. They are presented in Table 4 below.

Table 4: Measures Precedent

Measures precedent	Status Required factual elements
Component 1. Improvement of JIRAMA's performance (improvement of the governance and financial management framework)	
Adoption and operationalization of JIRAMA's management improvement plan	To be adopted before the end of October 2016
	Letter of the Minister of Finance and Budget forwarding the copy of the minutes of JIRAMA's Board of Directors adopting the management improvement plan
Adoption of the decree to fight against electricity fraud	To be adopted before the end of October 2016
	Letter of the Minister of Finance and Budget forwarding the copy of the minutes of JIRAMA's Board of Directors adopting the decree to fight against electricity fraud
Adoption of JIRAMA's new organization chart	To be adopted before the end of October 2016
	Letter of the Minister of Finance and Budget forwarding the copy of the minutes of JIRAMA's Board of Directors adopting the Company's new organization chart
Preparation of an action plan for implementation of the recommendations contained in the audit report on JIRAMA's contracts (Delta Conseil)	To be adopted before the end of October 2016
	Letter of the Minister of Finance and Budget forwarding the action plan for implementation of the recommendations contained in the audit report on JIRAMA's contracts (Delta Conseil)

Component 2: Improvement of JIRAMA's production efficiency and service quality	
Preparation of a preventive maintenance programme for the thermal park, including needs, programme financing arrangements and analysis of the financial impact of this maintenance on the reduction of fuel consumption and generator rental costs.	Programme prepared Letter of the Minister of Finance and Budget forwarding a preventive maintenance programme for the thermal park, including needs, programme financing arrangements and analysis of the financial impact of this maintenance on the reduction of fuel consumption and generator rental costs.

5.5. Application of Good Practice Principles on Conditionality

Good practice principles on conditionality were applied. Ownership results from consideration of national needs and alignment of the programme on the 2015-2019 PND and the 2015-2030 NPE. It also results from active collaboration between the Government of Madagascar and the Bank during programme design. Furthermore, the programme was prepared in close coordination with other TFPs, particularly the World Bank and GIZ, which intervene in the energy sector. The conditions precedent to the operation's disbursement will be reduced in number and will relate to key reform measures that are key to a gradual and lasting recovery of the electricity sub-sector. Lastly, the programme is aligned on the budget cycle of the Republic of Madagascar and will help reduce the country's financing need.

5.6. Financing Needs and Mechanisms

The resources of this operation are part of external financing that will help to fill the financing gap for 2016. The financing need (cash basis) for 2016 stands at 4.5% of GDP. Domestic financing corresponds to 1.6% of GDP and external financing accounts for 2.9% of GDP. In terms of external financing, 1.9% of GDP comes from budget support. PARSE, amounting to UA 13.77 million, is part of the additional budget support need of USD 45 million identified during ECF programme preparation. It is in this context that the Malagasy Government approached its technical and financial partners to bridge the gap and balance the 2016 State budget.

In this respect, the AfDB, through PARSE, will provide UA 13.77 million (USD 19 million); the World Bank committed to provide additional support of USD 15 million (which will bring its total budget support for 2016 to USD 65 million), while France committed to provide EUR 5 million (USD 5.5 million).

Table 5 : Projected Financing Needs and Sources

Financing needs and sources in MGA billion		
	2016	**2017**
Total revenue and grants	4 135	4 918
Tax revenue	*3 431*	*3 898*
Grants	*636*	*944*
Total expenditure and net loans	5 162	6 494
Budget balance (commitment)	-1 026	-1 576
Overall balance (cash)	-1 415	-1 811
Total financing including:	1 415	1 659
Domestic financing	500	399
External financing including:	915	1 261
Budget support	589	239
FINANCING GAP	0	-152
Source: MFB, IMF/ECF Programme		

5.7. Application of Bank Group Policy on Non-Concessional Debt Accumulation

PARSE will be financed by the remaining resources from Madagascar's country allocation, under ADF 13, which stands at UA 13.77 million, corresponding to UA 2.55 million under the remaining package of the 2016 Performance-Based Allocation (PBA) and UA 11.22 million from the balance of project cancellations. Thus, PARSE is consistent with the Bank's policy on non-concessional loans. Furthermore, it will be recalled that, within the framework of the three-year programme established under the Extended Credit Facility (ECF), Madagascar will benefit from a semi-concessional loan margin of USD 283 million between 2016 and 2017 as well as a non-concessional debt margin of USD 100 million, during the same period.

VI. PROGRAMME IMPLEMENTATION

6.1. Programme Beneficiaries

This programme, which aims to secure electricity supply and the energy sector's financial balance, will benefit the country's entire economy. The direct programme beneficiary is JIRAMA. The indirect beneficiaries are the people served with better quality electricity: households, whose living conditions will be improved, and socio-economic operators, whose activities will be more profitable. The final beneficiaries of the programme are the entire population, not just the 15% of the population that has access to electricity, but also those who, due to improved services, could be connected to the network.

6.2. Impact on Gender, the Poor and Vulnerable Groups

The implementation of programme reforms will help to improve the living conditions of the poor and vulnerable groups. PARSE envisages to have a favourable impact on the conditions of households in general, and those of women in particular. The programme will support structural reforms aimed at improving electricity supply, which will benefit vulnerable groups that lack the financial resources to acquire backup generators to ensure electricity supply during outages. By benefiting from public lighting, women will become more involved in income-generating activities, thus lightening their domestic chores. The programme will further contribute to business development by maintaining small- and medium-sized enterprises and informal sector activities.

6.3. Impact on the Environment and Climate Change

6.3.1 The programme is a budget support operation, which backs reforms that do not have any direct impact on the environment and climate change (Category III).

6.3.2 The programme might potentially have a negative impact on the environment, in that the urgent need to reduce electricity generation costs requires the conversion of plants, currently operating on diesel, into cheaper but more polluting fuel oil. However, this situation is temporary. The expected shift towards greater harnessing of renewable energies will ensure gradual abandonment of polluting sources of energy.

However, improved management of the electricity sub-sector will have positive impacts on efficient resource use. Measures taken to promote renewable energies will also favour the implementation of low-carbon energy operations.

6.3.3 Furthermore, the programme is unlikely to generate negative social impacts. The results expected from the programme even provides that the State budget, freed from the constraint of subsidizing JIRAMA, could be redirected towards basic social expenditure or investment projects that generate sustainable and inclusive growth.

In accordance with Integrated Safeguard System (ISS) requirements, PARSE does not require an environmental and social assessment.

6.4. Impact in Other Areas

The programme will have an impact in other areas, especially the increase in public resources allocated to social sectors. Being a budget support operation, PARSE will enable the State to have the necessary fiscal space to improve the delivery of essential social services to the population, particularly in hospitals, schools and businesses. This will have a positive impact on the quality of health and education for the population, and on job creation.

6.5. Implementation, Monitoring and Evaluation

PARSE implementation will be coordinated by the Ministry of Finance and Budget (MFB) through the Budget Support Monitoring Committee, placed under the supervision of the Secretariat General and the operational monitoring of the Department of Public Debt. This Committee, which is already in place and effective, will ensure the implementation of PARSE reforms by the Ministry of Energy and JIRAMA. The Committee will also be responsible for forwarding PARSE's progress reports and all evidence of reform achievements to the Bank.

The Bank will ensure programme monitoring and implementation by conducting supervision missions, and producing reports on implementation progress and results (IPRs), based on the programme logical framework. Monitoring will also be ensured in coordination with other TFPs of the "Budget Support and Public Finance" Group, within the framework of monitoring of the common performance matrix. Thus, the Bank's Field Office in Madagascar will play an important role in dialogue with authorities for PARSE monitoring.

At the end of the programme, a completion report will be produced jointly with the Government.

6.6. Financial Management and Disbursement

6.6.1. Country Fiduciary Risk Assessment

The assessment of Madagascar's public finance management systems deemed the overall fiduciary risk substantial, but with a positive trend since 2013 with regard to the implementation of reforms to improve public finance management performance. An audit of financial flows will be conducted by Madagascar's General State Inspectorate (IGE) at the end of the fiscal year. Audit reports will be shared with the Bank, with a view to monitoring the risk level. Furthermore, the Court of Auditors, through its control of the execution of Finance Acts, will provide its opinion on the Budget Review Act of the fiscal year concerned.

6.6.2. Financial Management and Disbursement Mechanisms

The proposed programme will be financed by a UA 13.77 million ADF loan, which will be disbursed in a single tranche, subject to fulfilment by the Borrower of the relevant general and specific conditions that will be mentioned in the loan agreement. The funds will be disbursed into a special account in the Central Bank of Madagascar, dedicated to receive the loan resources. The programme's presentation to the Board will be subject to implementation of the measures precedent presented in Table 4.

6.6.3. Procurement

The Bank recently assessed the country's procurement system, based on the OECD/CAD MAPS methodology and using indicators selected as critical for ensuring that the Bank's fiduciary obligations and standards are not compromised while using the country's procurement system. Despite a few divergences identified compared with international practices, Madagascar's public procurement framework would be adequate for effective use of Bank resources allocated through budget support. Reforms of the national procurement system were initiated by the Government, with the support of the Bank and other TFPs. Progress has been noted, starting with the ongoing updating of the public procurement code. Because of that, the Government carries out all procurement under the energy sector-based budget support programme, in accordance with the national law instituting the public procurement code.

VII. LEGAL INSTRUMENTS AND AUTHORITY

7.1. Legal Instrument

The legal instrument that will be used under this programme is the Loan Agreement between the Bank and the Government of Madagascar.

7.2. Conditions Associated with Bank Intervention

Conditions precedent to the programme's presentation to the Board: Based on dialogue with the Government, it was agreed that the latter should implement measures precedent to the programme's presentation to the Bank's Board of Directors. These conditions are indicated in the Table on Conditions Precedent (Table 4).

Conditions precedent to effectiveness of the Loan Agreement: Effectiveness of the Loan Agreement shall be subject to fulfilment by the Borrower, to the Fund's satisfaction, of the conditions set out in Section 12.01 of the General Conditions Applicable to AfDB Loan Agreements.

Conditions precedent to disbursement: In addition to effectiveness conditions, disbursement of the loan resources amounting to UA 13.77 million, shall be subject to the following condition: Provide evidence of the opening of a special account at the Central Bank of Madagascar (BCM), dedicated to receive the loan resources.

7.3. Compliance with Bank Group Policies

Prepared following an urgent request from Malagasy authorities, PARSE does not feature on the programming of the Bank's 2014-2016 Interim CSP for Madagascar. However, it is fully aligned on Pillar I: "Enhancing governance". The programme is also in line with the priorities under the Bank's Ten-Year Strategy (2013-2022), notably infrastructure development, private sector promotion and good governance, and meets one of the Bank's High 5s: "Light up Africa". It is also aligned on Pillar I: "Public sector management and economic management" and Pillar II: "Sector governance" of the 2014-2018 Governance Action Plan (GAP II), and is consistent with the Programme-based Support Operations Policy.

The Bank Group's main guidelines applied under this programme are those relating to loans to support the development budget in its regional member countries, defined in Document ADF/BD/WP/2003/182/Rev.2 of 28 April 2004. No waiver is requested in respect of Bank guidelines in this proposal.

VIII. RISK MANAGEMENT

The risks likely to affect programme implementation and mitigation measures are presented in Table 6 below:

Table 6: Risks and Mitigation Measures

Risks	Mitigation measures
The political and institutional risk that could affect the conduct of reforms	The ongoing political dialogue, with the international community's support
Macroeconomic instability	The partnership established among technical and financial partners around ongoing reforms as well as the IMF ECF
The weak institutional capacity to oversee and implement reforms as scheduled	The will of the State to work together with JIRAMA to come out quickly from this crisis. The implementation of the Bank's 2017-2019 strategy for Madagascar will provide more support for energy sector reforms and investments
Corruption	The continued implementation of reforms to fight corruption, especially with the gradual establishment of anti-corruption units in Ministries and institutions.

IX. RECOMMENDATION

It is recommended that the Board of Directors approve a loan of UA 13.77 million for the Republic of Madagascar, for use in financing the Energy Sector Reform Support Programme (PARSE).

Annex 1: Letter of Government Economic Policy

MINISTRY OF FINANCE
AND BUDGET
MINISTER

Antananarivo, 29 September 2016

THE MINISTER OF FINANCE AND BUDGET

To

THE RESIDENT REPRESENTATIVE OF THE
AFRICAN DEVELOPMENT BANK
ANTANANARIVO

Mr. Resident Representative,

Madagascar has continued implementing the National Development Plan (PND) and its Implementation Plan (PMO), in a bid to reduce poverty and establish inclusive and sustainable development. The thrusts of the Government's programme, presented before the National Assembly and the Senate, set objectives around three priority thrusts, namely: (i) enhancing governance and the rule of law, and establishment of equitable justice; (ii) economic recovery through the institution of a stable social and political environment, maintenance of macroeconomic stability and restoration of an attractive business climate; and (iii) extension of access to quality basic social services.

This Letter shows the Government's will to meet the challenges for medium-term economic development by strengthening tax and customs revenue performance, and optimizing resource allocation for sectors that have tangible impacts on the population (education, health, and infrastructure).

In the last two years, social indicators have not improved, despite Government's desire to promote human capital development and social protection mechanisms and systems. With a low Human Development Index of 0.510, Madagascar occupies the 154th position out of 188 countries in the United Nations 2015 Human Development Report and did not achieve the Millennium Development Goals by 2015.

The resumption of economic activities was still fragile in 2015 and performance, by sector of activity, remained mixed. They reflect prudent investment by operators in economic activities as well as limited supply. In addition, the volatility of nickel prices and the cyclone damage during the first quarter of 2015 worsened the situation. Economic growth reached only 3.1% compared to the 5% objective projected by the PND. The inflation rate was estimated at 7.6% end-2015.

Government's major economic and strategic orientations were aligned on the National Development Plan. The Government is determined to face the country's urgent economic and social challenges with the support of TFPs. The new agreement for Madagascar under the Extended Credit Facility (ECF), approved in July 2016 by the Executive Board of the International Monetary Fund (IMF), confirms the will to further support investments in infrastructure, the extension of access to education and health care, and the implementation of reforms to enhance economic and financial governance.

Concerning public finances, the tax burden rate stood at 10.1% for 2015. A decrease was noted relative to the objective set in the Initial Finance Act, due mainly to lower international oil prices and the volume of imports. Lack of dynamism in sectors of activity, inadequate means to limit fraud and tax evasion as well as the limited capacity of the current computer operating system, are the main obstacles to domestic resources recovery.

Public expenditure was estimated at 15.1% of GDP in 2015. Social sectors (health, education, social protection) remain a priority, despite the limited resources available to meet State needs. The operating and investment expenditure of four social ministries (Ministry of Water, Ministry of National Education, Ministry of Public

Health, and Ministry of Population) will be increased to reach 1.3% of GDP in 2019. This expenditure is estimated at 0.7% and 0.8% of GDP in 2015 and 2016.

Growth is expected to accelerate to reach 4.1% in 2016 and 4.5% in 2017. This expansion should help to reduce poverty and vulnerability under the combined effect of better governance and investment efforts. Economic growth will be driven mainly by sectors of activity related to infrastructure construction and public works, primary sector activities and free-zone industries.

The inflation rate for 2016 is estimated at 7.1% at the end of the period. The change in the consumer price index (CPI) will be more moderate because of the downturn in oil prices on the international market. Furthermore, the monetary policy in force will support the achievement of this objective.

Public finance strategies aim to preserve macro-economic stability, and will be based on support to socio-economic development as well as the practice of good governance. Budget policy has as objective to increase fiscal space, through the expansion of the tax base and the intensification of efforts focused on public expenditure efficiency. Thus, the net tax burden rate will stand at 10.8% in 2016 and 11% in 2017.

Public expenditure is estimated at 16.2% of GDP in 2016 and 18.3% in 2017. It will focus on activities contributing both to economic growth and the improvement of the people's standard of living, while aligning with the development priorities defined in the PND.

A recovery in total investments is expected. Capital expenditure will account for 5.3% of GDP in 2016, if estimated at 3.5% in 2015.

The Government committed to avoid accumulating domestic arrears and to clear the existing stock of arrears within a timeframe compatible with the Public Treasury's reimbursement capacity. An action plan with a schedule has already been established for the reimbursement (VAT, supplier debts) that will extend up to 2019. Negotiations have already started with debtors for the securitization of certain debts, in a bid to reduce State expenditure.

Public finance management reforms will increase public expenditure efficiency. The reform action plan will take into account the recommendations of the PEFA 2013 self-assessment, and reforms planned in the Extended Credit Facility (ECF) programme, approved in July 2016.

An annual 0.5 point increase in the tax burden rate will be fixed, to reach a tax burden rate of 12% in 2019. The Government will continue reforms to strengthen the performance of the tax and customs administration, with a view to establishing an efficient and equitable taxation system, while banking on the improvement and securitization of tax revenue.

The customs code has been revised to restrict the scope of application of the exemption regime. This will help to limit the effects of customs revenue decrease in the coming years, generated by the application of trade and regional treaties.

A modern customs system has been established for facilitation at the borders and the strengthening of ex-post control. Thus, the dematerialization of procedures will be strengthened. The customs administration has established a risk-based control mechanism for big importers. To this end, new conditions have been adopted for the benefit of the Accelerated Customs Clearance Procedure. A performance contract has been instituted for customs workers of the Toamasina Port, and will be extended to workers of other sites. That of the Anti-Fraud Service is planned for early 2017.

Furthermore, to ensure better budget transparency of tax exemptions, an inventory of tax expenditure will be conducted regularly, with systematic publication of a corresponding annual report.

To enhance rational public expenditure management, the Government has streamlined the management of pension accounts (CPR-CRCM) by replacing pensioner cards and physically identifying beneficiaries in the major urban centres. In this regard, pensioners have had to present themselves at the counters to obtain the new cards.

The drop in oil prices on the international market has helped to cut public expenditure by reducing fuel subsidies. The gap between the pump price and the reference price was eliminated, since October 2015. In March 2016, the Government introduced a monthly automatic adjustment mechanism for pump prices, based on world prices and exchange rate fluctuations.

Proactive measures have been taken by the Government to limit the transfer of expenses to JIRAMA. The latter was called upon to adjust electricity tariffs, ensure passage from diesel generators to more economical fuel oil generators, and prepare a new law to sanction electricity and water theft.

An ex-ante review by the National Contracts Commission (CNM), of all contracts to be concluded by JIRAMA in excess of predefined thresholds (MGA 80 million for supplies), is recommended. A ministerial order was signed to this effect on 31 March 2016 for State Corporations and Public Establishments benefiting from State financial assistance.

As part of the transparency policy, JIRAMA will publish quarterly statistics on the electricity cost per KWh, for each electricity supply contract in force.

The Government has strengthened trade justice by improving legal proceedings relating to commercial matters. A circular has been signed and published to this effect. To sustain these reforms and give them a legal framework, the civil procedure code will be revised to incorporate the contents of the circular.

To boost economic growth, the Government has committed to prioritize public investments in sectors that spur economic growth, notably infrastructure, agriculture, tourism, and the industrial and mining sectors. Recourse to support from TFPs as well as the promotion of public-private partnership (PPP) are necessary, considering the limited public resources.

The State has already confirmed its will to develop PPPs by instituting a relevant law, adopted and promulgated in February 2016. However, the law's application is not yet effective. In this respect, two decrees on procedures and institutions are currently being prepared for submission to the Council of Government.

To improve investment efficiency and impact, the Government will conduct a prioritization of investment projects by strengthening the mechanism for evaluation and selection of major projects.

At the micro-finance level, Government policy is voluntary and concerns both development and regulation. A regulatory framework has been established to ensure the development of micro-finance initiatives. A law on the activity and control of micro-finance institutions was adopted in September 2005 and is currently being revised. The relevant regulations will be adopted by the Banking and Financial Supervision Commission (CSBF).

The implementation of all the measures envisaged under the National Development Plan will enable the Government to attain its objectives, notably the achievement of high economic growth and poverty reduction. However, limited resources has led the Government to solicit financial support from the African Development Bank within the budget support framework.

MINISTERE DES FINANCES ET DU BUDGET

RAKOTOARIMANANA

Annex 2: Note on Relations with IMF

INTERNATIONAL MONETARY FUND
COMMUNICATIONS DEPARTMENT

Press Release No. 16/370
FOR IMMEDIATE RELEASE
28 July 2016

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$304.7 million Extended Credit Facility Arrangement for Madagascar

On July 27, 2016 the Executive Board of the International Monetary Fund (IMF) approved the equivalent of SDR 220 million (about US$304.7 million, or 180 percent of current quota) under a 40-month Extended Credit Facility (ECF) arrangement for Madagascar, to help reinforce macroeconomic stability and boost sustainable and inclusive growth.

Following the Board's decision, SDR 31.428 million (about US$43.5 million) is available for immediate disbursement; the remaining amount will be available in phases over the duration of the program, subject to semi-annual reviews.

The Executive Board was also informed about the Managing Director's approval of the first and final review under the six-month Staff-Monitored Program (SMP) covering the period from September 2015 up to the end of March 2016. During this time, the country built a satisfactory track record of sustained reforms, with progress in most areas.

Following the Board discussion, Mr. Mitsuhiro Furusawa, Deputy Managing Director and Acting Chair, made the following statement:

"The new arrangement for Madagascar under the Extended Credit Facility aims to reinforce macroeconomic stability and promote sustainable and inclusive growth. Weak revenue collections, substantial low-priority spending, and the need for strengthened economic governance all pose challenges to medium-term economic development. Against this background, rigorous and sustained reform implementation will be crucial.

"Rapid growth and sustained poverty reduction will require more investment in infrastructure and broader access to education and health care, in addition to structural reforms. It will be essential to increase tax revenue and to contain and then reduce lower-priority spending, including transfers to state-owned enterprises, such as the utility company JIRAMA. While substantial external borrowing is appropriate to finance development, debt sustainability must be preserved and the authorities should rely as much as possible on external grants and concessional financing.

"Reforms to strengthen governance are also central to the success of the economic program. Key actions include strengthening public financial management and procurement practices, increasing budget transparency, carefully managing the fiscal implications of Public Private Partnerships, and reinforcing the institutions and legal framework for combatting corruption.

"Creating a solid foundation for further financial deepening will be crucial for reinforcing economic growth and stability. This will require more frequent and deeper supervision of banks and nonbanks, establishment of a legal and operational framework for institutions in difficulty, and promotion of modern payment methods.

"The central bank has been strengthened by increased legal independence and growing international reserves. The authorities should remain vigilant about maintaining price stability, and continue to improve the operational framework for monetary policy implementation, including by establishing a well-functioning money market."

Recent Economic Developments

Hampered by fragile institutions, Madagascar is striving to recover from an extended political crisis and international isolation from 2009 to 2013. During this period, key social and developmental indicators deteriorated.

The recovery that began in 2014 has so far failed to gain much momentum due to key commodity prices falling, weather-related shocks, and deep-rooted structural weaknesses. GDP growth is now estimated at 3.1 percent in 2015, which is slightly lower than in 2014 and barely higher than population growth. Inflation fell back to 6.3 percent at end-May 2016 from 7.6 percent at end-December 2015, led by lower food and fuel prices.

Budget execution was challenging in 2015. Priority spending was squeezed by underperforming revenue collections, financing difficulties, and unexpected needs for transfers to state-owned enterprises and pensions. The fiscal deficit increased to 3.3 percent of GDP. Despite international headwinds, economic conditions are expected to improve in 2016 supported by country specific factors.

Performance Under the Staff-Monitored Program (SMP)

Macroeconomic performance was broadly satisfactory under the SMP, which ran from September 2015 to end-March 2016. Macroeconomic targets were met through end-March 2016, with the exception of the ceilings on net credit to government and new external payment arrears, due to technical difficulties in making payments. Tax revenue began to improve gradually, thanks to additional measures under the program, and priority social spending targets were met. A robust accumulation of foreign exchange reserves boosted external buffers.

Progress was also achieved on the structural front, including strengthened audits and controls for revenue collections; an automatic fuel pricing mechanism to avoid any fuel subsidies; the submission to Cabinet of a revised Central Bank Act, advancing a key institutional objective for macroeconomic stability; the Cabinet approval of a National Social Protection Policy; better transparency and functioning of the foreign exchange market; and a new database to enhance debt management capacity and transparency.

Program Summary

The government program, supported by the ECF, aims at reinforcing macroeconomic stability and promoting sustainable and inclusive growth. The program focuses on:

- **boosting prospects for inclusive growth** through improved access to education, health care, and social protection combined with enhanced infrastructure and private sector development;
- **creating fiscal space** through improved revenue generation and spending prioritization
- **reinforcing economic governance by strengthening public financial management** and intensifying anti-corruption measures; and
- **strengthening macroeconomic stability by bolstering central bank operations** and financial supervision. Reform implementation will benefit from a targeted program of capacity building and technical assistance.

Additional Background

The Republic of Madagascar, which became a member of the IMF on September 25, 1963, has an IMF quota of SDR 122.2 million.

For additional background information on the IMF and the Republic of Madagascar, see: www.imf.org/Madagascar

Annex 3: Matrix of Programme Measures

Measures Taken to Reform the Energy Sector	Programme Measures (PARSE)	Implementation Schedule	Results	Structures Responsible
A. Improvement of JIRAMA's governance framework and financial management				
Audit of JIRAMA's energy supply contracts with private operators	Implementation of the recommendations contained in the audit report on JIRAMA's contracts with private fuel suppliers	December 2017	Control of JIRAMA's costs, sub-sector financial balance and electricity development	JIRAMA
Quarterly publication of data on ongoing contracts on JIRIMA's website	Adoption of the decree on the fight against electricity fraud	October 2016	Control of JIRAMA's costs, sub-sector financial balance and electricity development	Ministry of Energy and Hydrocarbons
JIRAMA's performance improvement plan	Adoption of JIRAMA's new organization chart (which takes into account women's involvement) and its implementation	December 2017	Improvement of JIRAMA's governance	JIRAMA
	Adoption and implementation of the performance contract between the State and JIRAMA (performance contract) specifying the commitments of the two parties	December 2017	Control of JIRAMA's costs, sub-sector financial balance and electricity development	Ministry of Energy and Hydrocarbons
B. Improvement of JIRAMA's production efficiency and service quality				
Publication of 'Madagascar's Energy Policy Paper' 2015-2030	Conversion of the operating mode of thermal generators (80 MW) from diesel to fuel oil, to reduce fuel costs	December 2017	Improvement of electricity generation	JIRAMA
Subsidization of fuel purchase and generator rental capped at USD 300 million	Constitution of a fuel security stock to ensure continuity of service for 15 days	December 2017	Improvement of electricity generation	Ministry of Finance and Budget Ministry of Energy and Hydrocarbons
	Implementation of the preventive maintenance programme for the thermal park to reduce fuel consumption and generator rental costs	December 2017	Improvement of JIRAMA's service quality	Ministry of Finance and Budget Ministry of Energy and Hydrocarbons
Preparation of the draft revised electricity law, including the promotion of renewable energies	Adoption of the draft revised electricity law, including the promotion of renewable energies	December 2017	Promotion of renewable energies, with a view to developing national potential	Ministry of Energy and Hydrocarbons

Annex 4: Map of Madagascar