Ministry of Finance and Economic Planning

Rwanda Fiscal Risk Statement FY 2021/22

May 2021

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I. INTRODUCTION

The Government of Rwanda is publishing its second Fiscal Risk Statement (FRS) produced by the Ministry of Finance and Economic Planning (MINECOFIN). This is not only in line with global best practice but also a fulfilment of Rwanda's commitment with IMF and World Bank and a continuous East African Community Monetary Union requirement.

The publication of the annual FRS outlines risks with a fiscal impact stemming from various sources and the Government's mitigating measures to reduce the impact. This demonstrates the Government's commitment to uphold its main policy objectives of promoting economic development and social cohesion whilst maintaining macro-economic stability.

For the purpose of this paper, **fiscal risks refer to the possibility of deviations in fiscal variables from what was expected at the time of the budget or other forecasts**. Specifically stated, fiscal risks are developments that can cause public finance outcomes to deviate from what was expected at the time of the budget, or in other macroeconomic forecasts. Such risks include but are not limited to unforeseen spending pressures, revenue shortfalls, terms of trade shocks, exchange rate volatility, natural disasters, and calls on Government guarantees.

Table 1: Fiscal Risk Framework

Macroeconomic risks	• External risks • Macroeconomic shock simulation • Fiscal analysis: forecast performance
Specific risks and contingent liabilities	• Public Corporations • Public debt related risks • Government guarantees • Public Private Partnerships • Pension liabilities • Local Government • Financial sector • Natural disasters

The purpose of this statement is to identify the fiscal risks facing Rwanda, and outline steps to mitigate such risks where appropriate, as sound management of fiscal risks contributes to macroeconomic stability.

This FRS has been prepared against the background of the COVID-19 pandemic, which has significantly affected the world economy including Rwanda. In view of the uncertainty related to the evolution of the COVID-19 situation globally, the Government views **the combined level of fiscal risks as moderate.**

The Statement groups fiscal risks into two categories: macroeconomic and specific risks. These risks are discussed in the rest of the document.

Government intends to publish the Fiscal Risk Statement annually. Over the medium term, coverage of risks will be progressively expanded to cover a wider array of risks, including more details on contingent liabilities associated with public-private partnerships and legal claims.

II. MACROECONOMIC RISKS

1. Primary external risks

Rwanda's main macroeconomic risks are largely external, arising from global commodity price volatility, climate irregularities, and uncertainty about the level of external support commitments.

Global commodity price volatility creates significant uncertainty. Many raw materials and finished products used in Rwanda are imported from the region or further afield. Because Rwanda is landlocked, transport costs are generally high. Coffee, tea, and some minerals are important sources of foreign exchange, but these are also susceptible to global commodity fluctuation. At this time, prices projections for some key products are positive with coffee, cassiterite, coltan and wolfram at 6.3, 40.3, 32.1 and 32.1 percent increase for the year 2021.

The COVID-19 pandemic severely affected our export of services which declined by 49 percent in 2020 due to travel (-74 percent) and air transport (-50 percent) as air traffic was disrupted and events cancelled. Projections for 2021 are more positive with a 13 percent increase in export of services.

Climate fluctuations are a source of risk in Rwanda because most food is locally produced. Low rainfall or drought can significantly reduce agricultural production, with knock-on effects for employment and income in rural areas while heavy rains with ensuing floods have also been of concern recently.

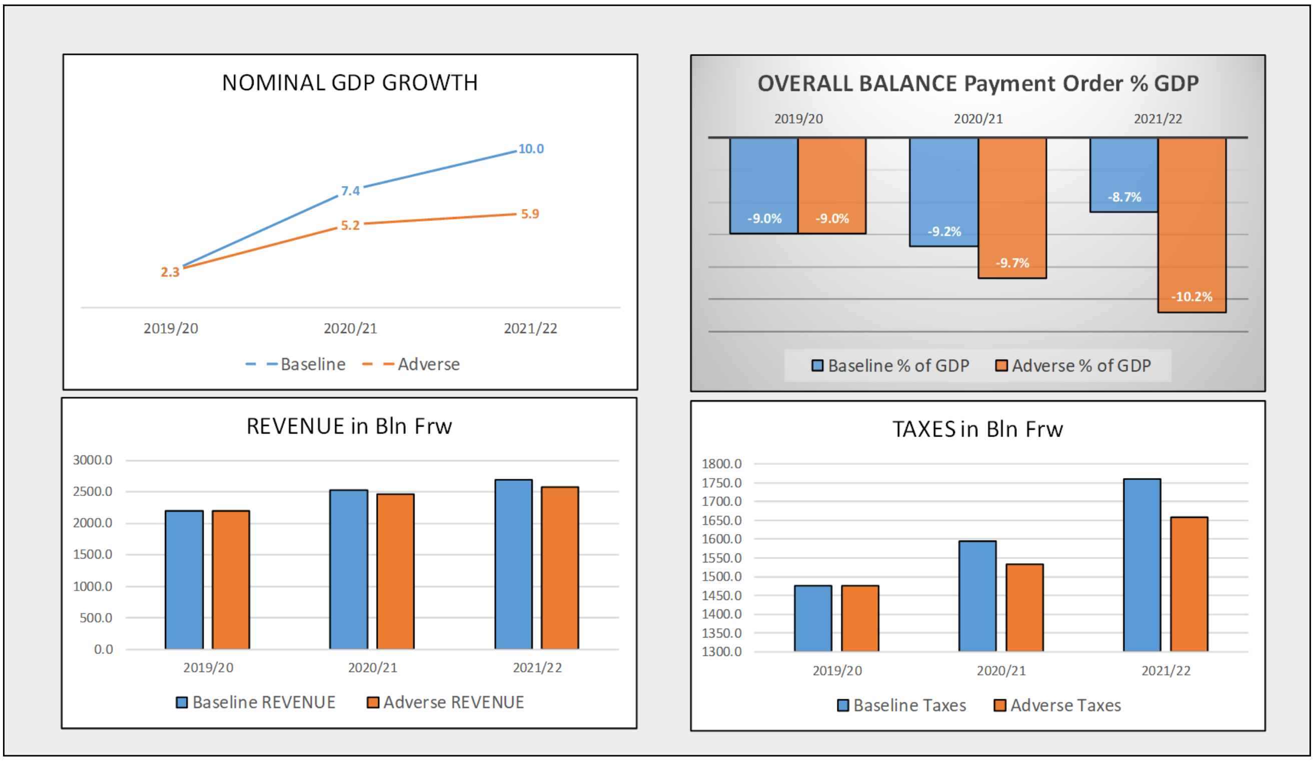
Unexpected foreign aid shortfalls can have a significant impact on budget implementation and economic growth in general. Delays in disbursements can create short-term funding gaps, and lead to pauses in development activity.

In the short run, the Government is committed to implementing its economic recovery plan to return to its pre-COVID-19 growth path, and prudent measures to manage these risks, improve the resilience of the economy, and maintain sustainable public finances. Tax compliance and administration measures will expand and diversify the revenue base in the medium-term, supported by revenue mobilization strategies under our forthcoming Medium-Term Revenue Strategy (MTRS-1) and increased expenditure prioritization.

2. Macroeconomic Shock Simulation

The adverse scenario shows a shock on nominal growth from the baseline of 10.0 percent to 5.9 percent. This is in line with a persistent COVID-19 impact or any unpredictable shock to the growth path. The shock magnitude is obtained from the standard deviation from a series of 10 years of growth. Keeping fixed public expenditure, the graphs below illustrate the effects of a reduction in real growth from 5.1 percent to 1 percent. Total revenue would drop by 107.7 billion Frw in 2021/22 compared to the baseline with 95 percent percent assigned to taxes which would reduce by 102.4. Taxes would go down from 1760.1 billion Frw in the baseline scenario to 1657.2 billion in the adverse scenario. Keeping expenditure constant, the overall deficit would worsen by 1.5 percentage points from 8.7 percent of GDP in the baseline to 10.2 percent of GDP in the adverse scenario. The below graph is just an illustration of the macroeconomic shock described above.

Figure 1: Macroeconomic shock illustration

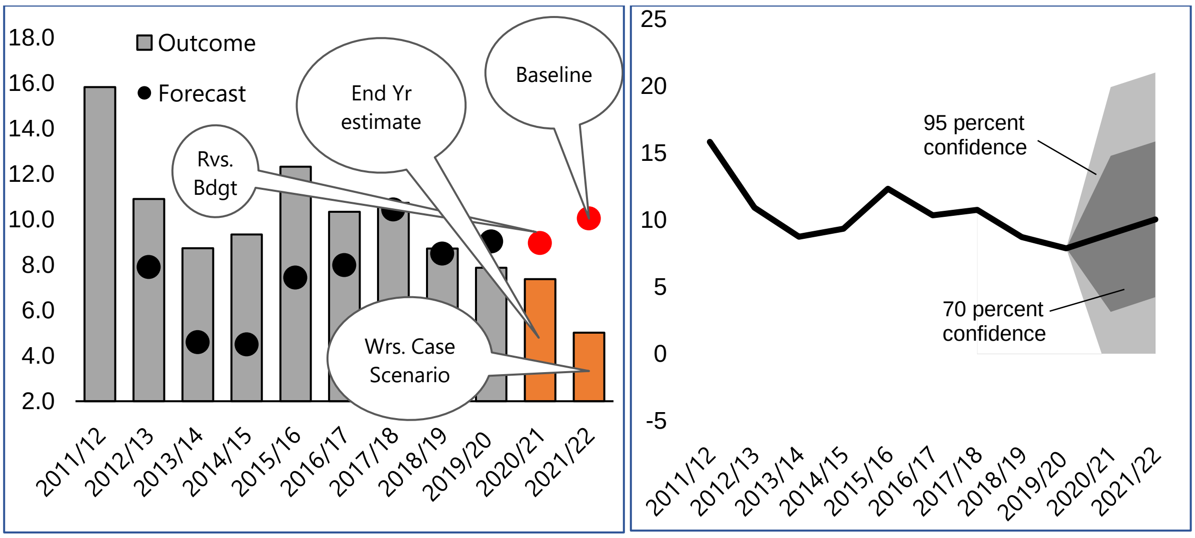


Source: MINECOFIN

3. Forecast performance

Forecast errors can be a source of fiscal risk. Revenue shortfalls against forecast, or expenditure overruns, can lead to unanticipated borrowing. This section reviews the performance of several key fiscal and macroeconomic forecasts. In general, forecast performance has been satisfactory over the past several years, with several notable exceptions.

Figure 2: Nominal GDP growth confidence intervals, forecast and outcome (percent)



Source: MINECOFIN

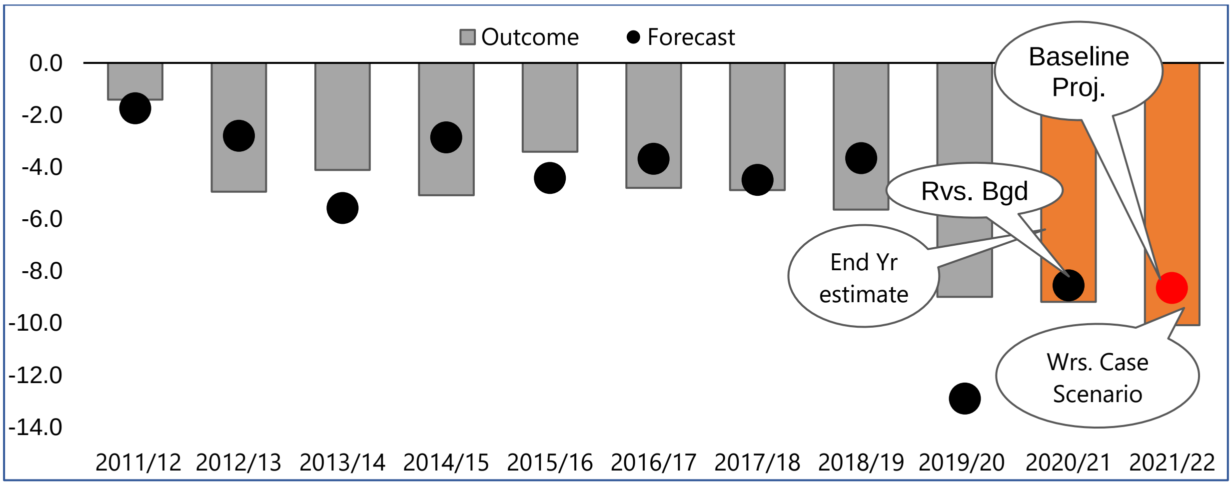
Nominal GDP

Based on historical forecast errors ie the difference between forecast and actual outturn, the nominal GDP outcome is usually higher than projected, and forecasting performance has been improving in recent years. There are two notable exception in FY 2019/20 and 2020/21 which can be explained by the COVID-19 pandemic shock on the economy. Nominal GDP growth forecasts for FY 2020/21 and FY 2021/22 are 9.0 and 10.0 respectively, expecting a gradual economic recovery, with a 70 percent probability (Figure 2) to be between 3.1 and 14.8 percent in FY 2020/21 and 4.2 and 15.9 percent in FY 2021/22,. The adverse scenario shows a shock on GDP leading to 5.0 percent growth in nominal GDP from 10.0 percent in the baseline in FY 2021/22. This would have a spill over effect to Government revenues and the rest of the economy.

Overall budget balance

We compare the overall fiscal deficit on cash basis to previous forecast. In 2016/17 and 2017/18, the budget deficit was slightly larger than forecast due to increased expenditure on new recruitment in the public service and advance payment for peacekeeping operations. From 2012/13 to 2014/15, volatility in foreign aid disbursements led to major deviations from the budget forecast.

Figure 3: Overall balance (cash basis) forecast and outcome (% of GDP)



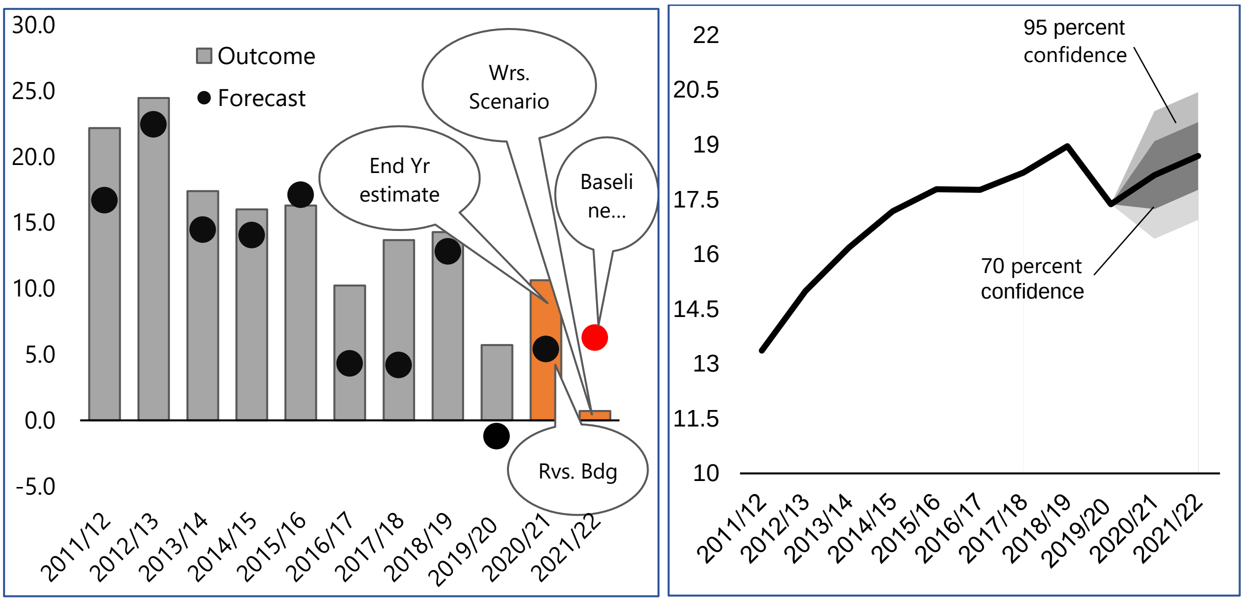
Source: MINECOFIN

The recent COVID-19 pandemic significantly impacted revenue collection and led to revenue losses. In addition, Government expenditure did not reduce since some urgent spending was needed in response to the pandemic in FY 2019/20, FY 2020/21 and FY 2021/22. These factors led to the fiscal deficit being significantly higher in FY 2019/20 and slightly higher for FY 2020/21. The adverse scenario shows a deterioration of the overall balance overall balance on cash basis from 8.7 percent of GDP projected in the baseline to 10.1 percent of GDP.

Revenue

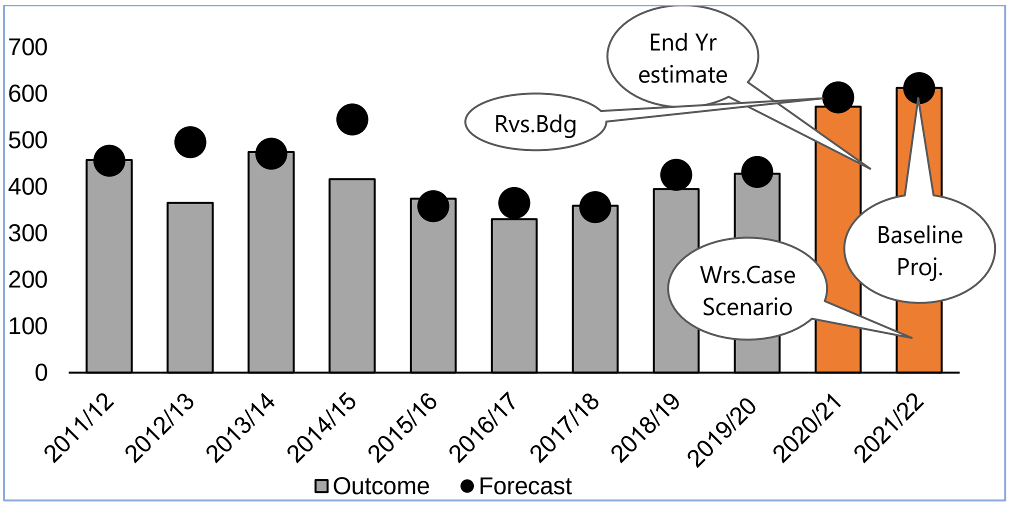
We measure domestic revenue as the sum of tax and non-tax revenue excluding grants. Tax revenues are highly sensitive to macroeconomic changes and effective revenue collection by the Rwanda Revenue Authority. MINECOFIN modelling suggests that for every percentage point increase in nominal GDP growth, tax revenue increases by 1.4 percent[1]. This highlights the importance of accurate macroeconomic forecasting in the budget process.

Figure 4: Revenue growth forecast and outcome



Source: MINECOFIN

Figure 5: Grants forecast and outcome (Rwf billions)



Source: MINECOFIN

Revenue forecasts, by and large accurate from 2012/13 to 2015/16, have become more pessimistic (Figure 4) since FY 2016/17. The better-than-expected revenue performance over the three years to FY 2018/19 is largely explained by administrative measures implemented by Rwanda Revenue Authority, combined with tax policy changes that generated additional revenue. For FY 2019/20 due to the uncertainty of COVID-19 pandemic, forecast revenue growth was revised down to -1.2 percent but the outcome registered growth of 5.7 percent reflecting the economic recovery after easing containment

[1] Pre-COVID estimate

measures such as total lockdown. Reimbursements from Rwanda's participation in United Nations peacekeeping operations have also been consistently higher than expected in the non-tax revenue performance.

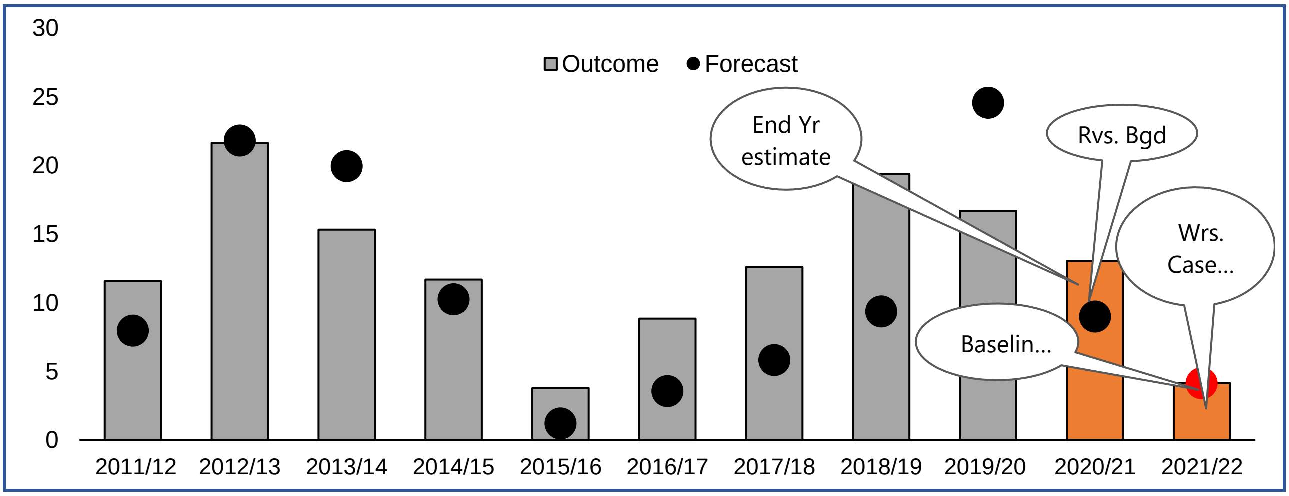
Revenue growth forecast for FY 2020/21 and FY 2021/22 result from the expected economic recovery. Figure 4 shows a confidence interval with 70 percent probability that the revenue-to-GDP ratio will be between 17.2 and 19.1 percent in FY 2020/21 and 17.8 and 19.6 percent in FY 2021/22. The adverse scenario of the COVID-19 shock to the economy may lead to only 0.7 percent growth in domestic revenue compared to 6.3 percent in the baseline.

Grant revenue forecasting has improved in recent years (Figure 5), following sharp deviations in 2012/13 and 2014/15.

Expenditure

Expenditure outcomes have been higher than forecast for the past 5 years except in FY 2019/20. This reflects unexpected expenditure on wages and salaries of some ministries and agencies due to the restructuring. Generally, exceptional expenditures include the costs of Rwanda's engagement in peacekeeping operations, the timing of which is difficult to predict. Lumpy project loan disbursements also increase the difficulty of capital expenditure projections.

Figure 6: Expenditure growth forecast and outcome (Percent)



Source: MINECOFIN

In FY2019/20, total expenditure and net lending at end June 2020 was lower by 205.3 billion Frw compared to projections, which anticipated an increase in spending due to COVID-19 on top of other spending in the budget that did not fully materialize. In fact, the total lockdown of the country and restrictions on movement including working from home led to underspending in all spending categories including delayed capital project implementation. COVID-19 related expenditure for the FY 2019/20, totalled to 109.1 billion Frw.

In FY 2020/21, spending is expected to be slightly higher due to higher COVID-19-related spending including vaccines. In FY 2021/22, expenditure is expected to continue to grow but at a lower pace than recently observed.

III. SPECIFIC RISKS AND CONTINGENT LIABILITIES

Contingent Liabilities are obligations that arise or are triggered by discrete but uncertain future events that may or may not occur in the future. Realisation of these risks may require the Government to make substantial and unexpected payments. Some of the following specific risks could present some contingent liabilities.

1. Public Corporations

Table 2: Public Corporations Classification

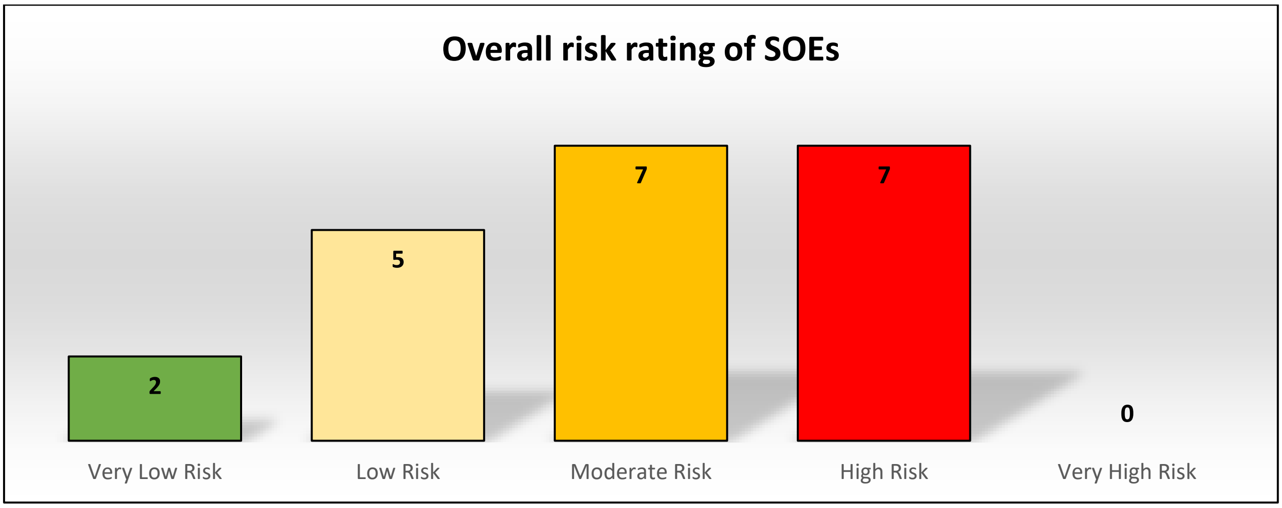
Non-Financial Public Corporations	***16***
Commercial State Owned Companies	13
Commercial Public Institutions	1
Commercial Special Purpose Vehicles	2
Financial Public Corporations	**7**
Commercial State Owned Companies	4
Commercial Public Institutions	1
Non Commercial Public Institution	2
Extra Budgetary Funds	**1**
Social Security Fund	**1**
Total	**25**

Source: MINECOFIN

There are 25 Public Corporations (PC), composed of seven financial and sixteen non-financial PCs. State Owned Companies or State Owned Enterprises (SOE) are 17, 13 non-financial and 4 financial. They serve to implement Government's socio-economic policies and strategies. Government business enterprises operate in different business sectors and are exposed to different kind of risks.

Health Check: General overview of PCs risk ratings

Figure 7: PC risk rating[2]



Source: MINECOFIN

[2] Out of the 21 PCs, 4 are financial public institutions.

Health check analysis of PCs helps to assess fiscal risk exposure of Government business enterprises by judging the financial performance and financial position of PCs to establish their financial health. The health check depicts a picture of Government investment risk exposure as a whole and analyses each individual enterprise. It is a dashboard that displays periodical analysis of the health of enterprises using financial ratios and economic indicators and signals risk exposure of individual companies as well as the aggregate picture.

The figure above displays the overall risk ratings. Each individual enterprise's risk exposure is rated against each type of risk (profitability, solvency and liquidity) and an overall risk is generated. 21 out of 25 PCs were assessed, the remaining 4 are quite new, the required information is not yet available to use the health check. Among twenty-one companies under scrutiny; two enterprises flagged very low risk, five enterprises flagged low risk, 7 enterprises flagged moderate risk and seven enterprises signposted high risk while none flagged very high risk.

It is important to highlight that the health check has demonstrated that the seven enterprises rated high risk are rated even very high risk against more than one type of scrutinized risks (liquidity risk, solvency risk and profitability risk). This implies that more in-depth scrutiny is needed in order to understand the underlying causes of risks in order to recommend proper remedy actions.

Health Check: Sectoral Analysis

At the sector level, losses and the accumulation of debt and liquidity challenges are concentrated in the transport and infrastructure sectors. Regarding infrastructure, losses are concentrated in utility companies: REG and WASAC.

Table 3: SOE Sectoral analysis

		Profitability		**Liquidity**		**Solvency**	
Sector	**SOE**	Return on Assets	Return on Equity	Current Ratio	Quick Ratio	Debt to Assets	Debt to Equity
Transportation		10.23	(3.75)	0.42	0.41	0.76	3.09
Infrastructure/Utility	REG	1.47	(76.54)	1.02	0.67	0.97	32.14
	WASAC	0.00	(6.79)	1.30	1.11	0.61	1.55

Source: MINECOFIN

Health Check: Quasi-fiscal activities

Table 4: PCs with quasi-fiscal activities (billion Frw)

		2016	**2017**	**2018**	**2019**	**2020**
Rwanda Energy Group	Total Revenue	176.7	132.2	130.8	148.9	150.6
	Government Grants Received	110.5	47.3	34.1	39.9	31.9
	GoR Contribution (%)	**62.5%**	**35.8%**	**26.0%**	**26.8%**	**21.2%**
Water and Sanitation Corporation	Total Revenue	27.3	26.6	41.8	30.7	35.8
	Government Grants Received	10.7	10.4	25.7	10.4	13.9
	GoR Contribution (%)	**39.2%**	**39.0%**	**61.5%**	**33.8%**	**38.8%**
Rwandair	Total Revenue	123.0	188.9	159.4	334.1	299.4
	Government Grants Received	43.1	82.6	97.0	131.2	132.3
	GoR Contribution (%)	**35.0%**	**43.7%**	**60.9%**	**39.3%**	**44.2%**
Aggregate	Total Revenue	462.0	458.5	488.0	923.9	1,090.0

	Government Grants Received	121.9	63.9	65.4	181.9	179.4
	GoR Contribution (%)	**26.4%**	**13.9%**	**13.4%**	**19.7%**	**16.5%**

Source: MINECOFIN

Rwanda Energy Group, Rwandair and Water and Sanitation Corporation lead in receiving Government subsidies due to the importance of the activities they execute for public interest at a price below the market price and/or for implementing Government objectives. It is evident that these enterprises would not cover their operational costs without Government support.

2. Public debt related risks

This section analyses four major risks associated with Rwanda's public debt portfolio, as well as the corresponding mitigating measures[3]. The main risks include: (1) refinancing risk, (2) interest rate risk, (3) foreign currency risk, (4) as well as risks associated with Debt Sustainability.

Sustainability Risk: Rwanda's public debt levels remain sustainable despite shift from low to Moderate risk of external and overall debt distress. The main sustainability risk associated with Rwanda's debt portfolio is the approaching repayment of the 2023 Eurobond of $400 million, for which the Government is currently exploring options that will help to mitigate the refinancing risk of a bullet payment in 2023. In addition, the cost of public debt portfolio keeps on increasing as result of higher domestic financing especially issuance of Government securities to cater for the fiscal gap. However, this is in line with Rwanda's debt strategy of developing a strong domestic capital market that favor the issuance of long-term securities in replacement of short-term securities in order to increase the average time to maturity of the public debt portfolio.

Refinancing Risk: Rwanda's debt portfolio refinancing risk is associated with sharp repayment profile that indicates a high liquidity risk over the next four years, mainly due to the repayment pressure from existing commercial debts and debt maturing in one year. However, this will gradually reduce with the Government strategy of lengthening external maturity profile and development of capital market that favor issuance of long-term securities in replacement of short-term securities.

Interest rate risk: The public debt portfolio is still entirely dominated by external loans with fixed interest rates. While the country is graduating from highly concessional lending sources, the portfolio could be subject to more variable interest rates, which could increase the risk and complexity of the debt portfolio. In addition, higher domestic public debt stock is re-fixed within same fiscal year, exposing the domestic debt portfolio to significant interest rate risk.

Foreign Currency risk: The overall Public debt portfolio is dominated by foreign currency denominated debt, exposing the debt portfolio to higher exchange rate risk. However, this will gradually reduce with liability management strategies being currently applied.

[3] An in-depth analysis of debt risks and associated mitigating measures, is found in the annual debt strategy document produced by the Debt Management Directorate in MINECOFIN .

(https://www.minecofin.gov.rw/1/publications/reports?tx_filelist_filelist%5Baction%5D=list&tx_filelist_filelist%5Bcontroller%5D=File&tx_filelist_filelist%5Bpath%5D=%2Fuser_upload%2FMinecofin%2FPublications%2FREPORTS%2FChief_Economist%2FDebt_Management%2F&cHash=c740c1b388f07e75324a50971292037b)

3. Government guarantees on loans from public corporations

To help public corporations and selected joint ventures attract private investment in infrastructure and enable them to borrow at affordable interest rates, the government issues guarantees. These guarantees commit the government to cover the debt obligations of borrowers in the event of loan default. Rwanda's current guarantee portfolio stands at FRW 396.7 billion, equivalent to 4.1 percent of GDP, of which FRW 209.0 billion is domestic and USD 193.0 million is external. The guarantees issued to six entities, are shown in Table 4.

Table 5: Government guarantees as of December 2020

STATE OWNED ENTREPRISES EXTERNAL DEBT STOCK (USD million)			
Entity	Guaranteed Amount at end December, 2020	EOP Echange rate	Billion FRW
Rwandair	35.8		
Ultimate Concept Ltd (UCL)	90		
Bugesera Airport Company (BAC)	38.6		
New Holizon Ltd	28.6		
	193.0	972.5	**187.7**
STATE OWNED ENTREPRISES DOMESTIC DEBT STOCK (FRW billion)			
Entity	Guaranteed Amount at end December, 2020		
Ultimate Concept Ltd (UCL)	15.4		
EWASA	16.0		
SONARWA	4.6		
Bugesera Airport Company (BAC)	113.0		
UCL BK Refinancing	46.0		
New Holizon Ltd	14.0		
	209.0		**396.7**
Norminal GDP			9746.0
Guarantees % of GDP			**4.1**

Source: MINECOFIN

A call on guarantees would result in the commitment of fiscal resources by Government. This risk is deemed to be low. Guarantee requests are subjected to strict assessments by the Debt Directorate within MINECOFIN. Government expects public corporations to be well run and financially sustainable, and closely monitors the financial performance of guarantee recipients.

4. Public Private Partnerships (PPPs)

Public private partnerships (PPPs) are where Government enters into some form of contractual arrangement with one or more private sector partners for the for the development or management of a public asset or service, where the private party bears significant risk and responsibility as well and is remunerated through performance or use of the asset/service.

PPP sector in Rwanda

To date, the Government have signed 58 PPP agreements with a total project value of approximately USD 1,816 million (around 1,823 billion Frw or 17.5 percent of GDP). Around 93 percent by both number and project value are in the energy sector, with the rest spread across various other sectors. 52 percent of the total projects by number are operational (21 percent by project value) and the rest are at various stages of implementation including negotiation and construction. Table 10 provides further detail on PPPs by sector and status.

Table 6: Ongoing PPPs in Rwanda by sector and status

Ongoing PPPs	Number	Project Value (USD million)
Energy Sector	54	1685.6
Operational	*27*	*280.2*
Other Stages	*27*	*1405.5*
Other Sectors	4	130.3
Operational	*3*	*107.9*
Other Stages	*1*	*-22.4*
Total	58	1816
Operational	*30*	*388*
Other Stages	*28*	*1383*

Source: RDB

Risks associated with PPPs

While PPPs can be a useful method for delivering infrastructure and services, they may expose the Government to various risks, depending on the exact structure of the PPP contractual arrangement. Well-designed PPPs allocate risks to those parties best able to manage particular risks effectively. Types of risks associated with PPPs include governance, construction, demand, operational and performance, financial risks, and risks associated with changes in law, renegotiation and contract termination.

Table 7: Explicit Contingent Liabilities (Guarantees Provided)

Project	Project Value (USD MM)	Estimated Total Annual Cost of Guarantee (USD MM)
Energy Sector PPPs		
Operational	126.6	33.6
Under Construction	480.9	118.4
Other Sectors PPPs		
Operational	70.5	12.4

Source: RDB
NB: Estimated total annual cost of the guarantee is the amount Government would have to pay for all annual energy produced in case the utility company failed to pay.

We track three main categories of explicit contingent liabilities:[4]

- Loan guarantees, whereby the Government guarantees loans made to a company in the furtherance of a specific project.

[4] Planned Government expenditure under a PPP is not ‘contingent’ (eg. an offtake) but is instead budgeted for by the relevant contracting authority. This type of expected expenditure does not fall within the scope of the explicit contingent liability categories tracked here.

- Demand/revenue guarantees in a PPP contract whereby the Government guarantees to the investor a baseline level of income as a hedge against a shortfall in private sector demand.
- Payment guarantees to the project company in case the utility companies fail to fulfil their payment obligations.

To date, the Government has not provided guarantees on loans or demand/revenue with respect to PPPs. All the guarantees provided so far fall under the category of payment guarantees and none of the guarantees have been called on so far. Table 9 shows the maximum potential explicit contingent liabilities associated with the guarantees issued to date.

5. Pension liabilities

Pension benefits play an important role in securing and improving the livelihoods of retirees and their dependents. The Rwanda Social Security Board (RSSB) administers the country's social security plan. The RSSB pension covers all formal-sector employees in the public and private sectors. It is a defined benefit scheme is paid to beneficiaries when they become eligible.

As shown in the table below, pension contributions well as benefit paid have increased for last five years.

Table 8: Pension contribution vs Benefits

Pension contributions vs benefit (millions)					
	2016	**2017**	**2018**	**2019**	**2020**
Contributions	74,695	74,897	83,344	94,371	102,178
Benefits paid	15,992	18,155	21,537	27,594	30,468
Incremental Contribution vs benefit payout (growth rates)					
	2016	**2017**	**2018**	**2019**	**2020**
Contributions	22.2%	0.3%	11.3%	13.2%	8.3%
Benefits paid	5.9%	13.5%	18.6%	28.1%	10.4%

Source: RSSB

However, it is noticeable that benefits payout is increasing more than contributions. This implies that the pension liability is increasing too.

6. Local Government

Local Government plays an important role in providing essential social and economic services, and Government considers local financial management capacity when assessing fiscal risk. In recent years, financial management and reporting capacity at district Government level has improved. As of April 2021, 1,031 local Government entities have enrolled on Government's integrated financial management and information system (IFMIS), up from 1,022 a year earlier, this represents added coverage of new district hospitals and health centers to use IFMIS, with schools using SDMS as a schools specialized component of IFMIS. There has also been further recruitment of hands-on specialists support to build financial management capacity in local Government.

As the table above shows, the percentage of local Government budgets contributed by central Government has stabilized at about 80 percent between FY 2013/14 and FY 2018/19, raising to 86 percent in FY 2019/20 and FY 2020/21. There has also been noticeable growth in own revenues, own-revenue generation capacity in local Government is expected to continue to increase, thereby reducing pressure from demands on national funds. Nevertheless, local Government funding of infrastructure projects is still inadequate and the Central Government has in past years provided additional budget support to local Governments to help fund local Government priorities and also mobilized funds from external funders to help bridge the gap in project funding capacity.

Table 9: Trend of local Government budget composition[5]

Designation	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
District Ownrevenues (Taxes & Fees)	37	40	46	49	53	64	74	87
Transfers from CG	279	310	327	343	348	391	450	546
External Grants	30	24	28	43	23	45	0	0
Total District Budget	**346**	**374**	**401**	**435**	**424**	**500**	**524**	**633**
% of Own revenues to the LG Budget	11	11	11	11	13	13	14	14
% of CG Transfers to the LG Budget	81	83	82	79	82	78	86	86
% of External Grants to the LG Budget	9	6	7	10	5	9	0	0

Source: MINECOFIN

7. Financial sector

The financial sector remains sound and stable, despite the challenges caused by the COVID-19 pandemic, and there are low risks of any financial crisis in the near-term to medium-term. All financial sub-sectors (Banks, insurance and microfinance) held adequate buffers of liquidity and capital capable as at end December 2020 (Table 1; Table 2 & Table 3). Non-performing loans are expected to edge-up in 2021 as payment moratorium expires on restructured loans and this will increase provisional expenses and compress profits across the financial sector. As at end December 2020, total outstanding loans restructured due to COVID-19 amounted to Frw 799.9 billion (i.e., 31.7 percent of total loans). Despite these asset quality challenges, the significant liquidity and capital buffers provide comfort that the sector is capable of absorbing losses on a going concern basis and without need for fiscal bail out. The National Bank of Rwanda (NBR) stress test performed in January 2021 indicated that banks continue to meet regulatory capital requirements, even under adverse shocks.

The recent regulatory reforms implemented by the NBR will continue to support resiliency of the financial sector in the near-term and medium-term. Since 2018, the NBR gradually adopted Basel II and III standards regulatory standards: it adopted a supervisory framework for Domestic Systemically Important Banks (D-SIBs) including introducing a capital surcharge for D-SIBs and additional supervisory requirements; introduced the capital conservation buffer; introduced the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) liquidity standards. Further to this NBR established critical financial safety nets like Deposit Guarantee Fund (DGF) and liquidity assistance facility to support in crisis management and resolution.

Table 10: Financial Soundness Indicators (Banking Sector) - In Percent

Indicators	Dec-16	Dec-17	Dec-18	Dec-19	Dec-20

[5] From FY 2019/20 external grants have been merged with Transfers from Central Government.

Total CAR (min 15 %)	21.9	21.4	25.5	24.1	21.1
NPLs Ratio	7.6	7.6	6.4	4.9	4.5
Provisions / NPLs	42.7	46.7	68.2	81.5	106.4
Return on Average Assets	1.7	1.1	1.9	2.2	2
Return on Average Equity	8.8	6.2	11.2	12.5	11.8
LCR (min 100%)	-	-	299	215	254.7
NSFR (min 100%)	-	-	222	111	161.4
FX Exposure/Core Capital (± 20%)	-7	-7.8	-5.6	-4.8	-4.4

Source: NBR

Table 11: Financial Soundness Indicators (Microfinance Sector) - In Percent

Indicators	**Dec-16**	**Dec-17**	**Dec-18**	**Dec-19**	**Dec-20**
Capital Adequacy Ratio (%)	35.2	35.8	35.1	35.7	36.0
NPLs Ratio (%)	9.0	8.2	6.5	5.7	6.7
ROA (%)	4.4	1.0	2.6	3.8	3.0
ROE (%)	13.7	2.9	7.7	10.7	8.2
Liquidity Ratio (%)	88.8	102.0	100.3	100.4	101.5

Source: NBR

Table 12: Financial Soundness Indictors (Insurance Sector) - In Percent

Indicators	**Prudential**	**Private Insurers**			**Public Insurers**		
	Benchmark	**Dec-18**	**Dec-19**	**Dec-20**	**Dec-18**	**Dec-19**	**Dec-20**
Solvency margin	Min 100%	165	170	114	2,265	2,426	2,496
Combined ratio	Max 90%	108	105	106	65	63	65
ROE	Min 16%	13	11	14	13	12	12
ROA	Min 4%	4	4	4	13	12	12
Liquidity ratio	Min.120%	134	130	134	3,982	4,636	3,984

Source: NBR

8. Natural disasters

Rwanda is highly dependent on its diverse ecosystems to sustain its population and support economic growth. The country is prone to storms, landslides, and floods, and 55 percent of total land area is at risk of soil erosion. On average, five districts per year face serious natural disasters, but in 2016 and 2018 the spread and severity of floods and landslides rose well above average, with over 2 million people affected, and negative consequences for agriculture, trade, and industry.

Disasters invariably require significant emergency management and longer-term responses. By disrupting normal business activities, they can also reduce revenue collection. Tourism is the country's largest source of foreign exchange, and disaster pose particular risks to wildlife tourism.

The number of events classified as natural disasters increased in recent years killing 134 people in 2019 and 298 people in 2020 while the number of people injured was 271 in 2019 and 414 in 2020. These events destroyed 5,691 houses in 2019 and 8,098 houses in 2020 and damaged 10,610 Ha of crops in 2019 and 4,662 Ha of crops in 2020.

Government scaled up its response for disaster management with a budget increasing from Frw 21.4 billion in FY 2016/17 to 44.8 billion in FY 2019/20.

Table 13: Natural disasters in 2019 and 2020

Event	2019				2020			
	Deaths	Injured	Houses Damaged	Damages in crops Ha.	Deaths	Injured	Houses Damaged	Damages in crops Ha.
Fire	1	23	56	76	1	9	84	-
Floods	30	12	89	2,891	62	5	178	2,993
Hailstorm	-	-	48	1,181	-	-	-	215
House collapse	7	26	15	-				
Landslides	13	21	113	477	125	63	1,643	180
Lightning	52	111	4	-	46	182	11	-
Mine disaster	23	4	-	-	19	9	-	-
Rainstorms	8	71	4,769	5,876	45	144	5,948	1,265
Wildfire					-	-	-	9
Windstorm	-	3	597	110	-	2	234	-
TOTAL	**134**	**271**	**5,691**	**10,610**	**298**	**414**	**8,098**	**4,662**

Source: Ministry in charge of Emergency Management (MINEMA)

Table 14: Budget for natural disasters

Bln Frw	2016/17	2017/18	2018/19	2019/20
Budget Commitments for Disaster management activities	21.4	36.0	53.7	44.8

Source: MINECOFIN

IV. MITIGATION MEASURES

Mitigation measures in case of a Macroeconomic shock

The macroeconomic shock described above may would lead to public finance challenges as domestic revenue would fall by Frw 107.7 bln or 1 percent of GDP. To maintain critical expenditure for economic recovery, Government would have to bridge this financing gap by contracting additional debt giving priority to concessional external borrowing and domestic borrowing.

Government mitigation measures for SOEs

Table 15: Government mitigation measures for SOEs

Source of Risk	Likelihood of occurrence	Mitigation/policy measure
Poor performance: high operational costs and Loan servicing costs	**Medium:** inherent risk associated to business management	- Reviewing business strategy to improve performance - Ensure proper accounting and financial reporting to enhance performance monitoring. - Regular SOEs stress check to establish the reason behind poor performance

Source of Risk	Likelihood of occurrence	Mitigation/policy measure
		- Ensuring appointment of right persons for SOEs directors and management
Gearing: Equity finance is low compared to high debt finance	**High:** enterprises financing that does not reflect their capital requirement and expansion/Growth plan**.**	- Sustainable funding strategy of SOEs - Viable business and strategic plan
Poor working capital: Lack of short term resources for day-to-day operations	**High**	- Ensuring availability of adequate working capital at every stage of growth - Consistency capacity building of SOEs Boards and management to enhance management operational efficiency
Uncompensated quasi fiscal operations: The need to comply with Government policy requirement for WASAC and REG to provide Water and electricity based on set tariffs put the companies at risk.	**High**: Grants and subsidies not likely to fully compensate the costs incurred by the enterprises	GoR, REG and WASAC to undertake a full review of the quasi fiscal operations and ensure that non-commercial activities are being sufficiently compensated for.

Management of public debt related risks

The Government is currently exploring options that will help to mitigate the refinancing risk of the USD 400 mln Eurobond bullet payment in 2023. To address the refinancing risk, the Government strategy is to lengthen external maturity profile and develop of capital market that favor issuance of long-term securities in replacement of short-term securities. The Government will also continue to maximize concessional borrowing, with non-concessional borrowing limited to cases where grants or concessional resources are unavailable.

Management of Government guarantees

A call on guarantees would result in the commitment of fiscal resources by Government. This risk is deemed to be low. Guarantee requests are subjected to strict assessments by the Debt Directorate within MINECOFIN. Government expects public corporations to be well run and financially sustainable, and closely monitors the financial performance of guarantee recipients. Over the past five years, there have been only one call on Government guarantees.

Management of PPP Risks

To support management of the risks associated with PPPs, in Rwanda these arrangements are anchored in a strong regulatory & institutional framework to ensure efficient and transparent processes. The framework comprehensively defines the entire PPP process, including project preparation & appraisal, project identification & selection, feasibility studies and PPP procurement. This ensures clarity, transparency consistency and efficiency in the process. Assessment and management of fiscal risks associated with PPPs is an area of ongoing work.

Management of pension liabilities

The Rwanda Social Security Board (RSSB) will continue to monitor contribution and benefits paid trend. It is ready to face the payment of any liability that may occur in due time.

Management of local Government risks

Government will continue supporting local Government to increase its own revenue. For this, implementation of the new law determining the sources of revenue and property of decentralized entities will help.

NBR mitigation measures for the financial sector

NBR will continue to closely monitor risks to the financial sector and is confident that the sector will remain resilient through 2021. The level of NPLs and provisions for bad debts are likely to increase during 2021 with an expected negative impact on profitability and capital buffers for banks and MFIs, while the upsurge of premium receivables and policy restructuring is likely to remain as a key challenge of the insurance sector and affect the growth of premiums and liquidity positions. However, to monitor and address risks to the financial sector, NBR will conduct a systematic review of credit risk across all institutions based on offsite supervision and onsite visits. Supervision will focus on investigating the proper implementation of the guidelines on credit reliefs, including scrutinizing banks' assessment of borrowers' likeliness to pay and examining whether they are implementing proper classification and timely recognition and provisioning of problem loans. With regards to insurance sector, monitoring of premium receivables will be key priority with the purpose of engaging insurers to have clear timeline of for premium receivable recovery.

Mitigation measures for natural disasters

As natural disasters remain one of the major source of fiscal risks, the Government's disaster risk financing has led to the formulation of recovery needs estimates that intends to address the four levels of disaster risk financing namely agriculture, housing, infrastructure and environment as well as strengthen disaster preparedness and management. Building on lessons learnt over the past several years, the Government has shifted to a more proactive approach. The country has strengthened the institutional, legal and coordination framework for disaster risk management.

V. CONCLUSION

Rwanda's second fiscal risk statement outlines a range of risks. In the current covid-19 situation, the **Government assesses the general level of fiscal risk as moderate**, and has put in place mitigation measures across a range of risks.

The Government of the Republic of Rwanda is aware of the current economic crisis resulting from the COVID-19 outbreak. However, due to external uncertainty beyond control, risks remain on the scale of the general economic impact. Government will continue to monitor and control regularly the fiscal impact to mitigate the fiscal risk. Future statements will expand the range of risks assessed.