



DEMOCRATIC REPUBLIC OF THE CONGO

SELECTED ISSUES

September 2019

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DEMOCRATIC REPUBLIC OF THE CONGO

SELECTED ISSUES

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Approved By
**The African
Department**

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GOVERNANCE AND CORRUPTION CHALLENGES¹

In line with the IMF's revised policy on governance, this note focuses on macro-critical issues related to governance and corruption in DRC.² Third-party indicators suggest that governance has been poor and corruption widespread in the country. Conducting an audit of the civil service and improving the transparency of its remuneration system, simplifying tax payment processes, and merging the activities of the numerous revenue agencies would boost public efficiency and improve the business environment. Contract enforcement and protection of property rights could be enhanced by insulating the courts from external influence.

A. Fiscal Management

The Budget Process

1. **The transparency of the budget process has improved relative to the early 2000s but there is scope for further improvement.** The International Budget Partnership's Open Budget Index, which evaluates budget process transparency, highlights a substantial improvement from a zero rating in 2006 to a rating comparable to the regional average in 2015.³ The government now publishes a budget summary and updates on budget revenue and expenditure execution. However, the Cours de Comptes, the government audit institution, does not publish its annual report. Public financial management (PFM) responsibilities in the DRC are split between the Ministry of Budget, the Ministry of Planning, the Ministry of Finance, and the Central Bank of Congo (BCC).
2. **Public participation and oversight have also improved over the past decade but remain limited.** The government engages with donors and civil society through 15 thematic groups, including one on public finances. The groups are supposed to meet regularly and be open to civil society, but meetings are not held on a regularly basis.
3. **Parliamentary oversight of the budget process has been weak.** Prior to 2019 when President Tshisekedi took office, the Executive and legislature were controlled by the same political party. The Court of Auditors assists the National Assembly in overseeing the executive and audits public expenditures, including those of the provinces, decentralized budget institutions, and state enterprises. However, the Court has no independent budget and lacks adequate financing. The Court's reports are listed but not published on its website. Moreover, the Court's recommendations are not followed by Parliament and sanctions are not enforced. A

¹ Prepared by Victor Davies based on the work of Nick Staines, former resident representative in Kinshasa. A multi-departmental team will undertake a governance assessment exercise later this year. The assessment will provide a more in-depth analysis of the issues raised in this paper and other issues.

² IMF 2017b and 2017c.

³ International Budget Partnership, 2017

Court of Auditors Law establishing the Court's independence, including financial, has been enacted. The Office of the Inspector General of Finance (IGF) has the authority to audit the executive accounts and impose administrative sanctions. It reports to the Ministry of Finance but is located in the Presidency.

4. **Lack of budget credibility undermines parliamentary oversight and allows for discretionary allocation of public resources.**⁴ Budget execution bears little relation to the approved budget because budget revenue projections—driven mainly by political pressures to accommodate higher spending—and expenditure projections have been overly optimistic. The 2011 Public Finance Law approved the introduction of Medium-Term Fiscal and Expenditure Sector Frameworks and the transition to program budgeting by 2018 to improve revenue and expenditure projections, but these have been delayed. The so-called Troika, comprising the Office of the Prime Minister, the Ministries of Finance and Budget, and the Central Bank, is tasked with monitoring budget implementation.

5. **Limited information on the budget annexes and special accounts and little or no oversight by the central government, Parliament, and civil society, create scope for corruption.** Together, these accounts represented about 15 percent of the overall 2018 budget. Budgets annexes cover some 800 institutions, mostly in health and tertiary education, that are legally separate from the central government. The government controls the administration of these institutions, but not their finances. They collect user fees to cover costs and receive transfers from the general budget to cover any deficit (see SIP on Poverty and Social Spending). The special Accounts cover the budgets for nine special funds, such as the Road Fund and the Industrial Development Fund.

6. **There are major gaps in the provision of financial statements.** An annual budget execution report is prepared but the central government and provincial governments do not publish annual financial statements. Weak provincial government capacity has been further exacerbated by the division of the then 11 former provinces into 26 in 2015. Also, state enterprises were converted to commercial entities in 2009, and are required under the OHADA Uniform Act to file their annual audited statements with the public registry. Whether state-owned enterprises, including commercial entities, are required to publish their financial statements, remains unclear.

Non-Resource Revenue Management

7. **Non-resource revenues, which form the bulk of budget revenues, are low compared to other SSA countries.** This is the result of constraints on administrative capacity, inappropriate tax policies, and governance issues. The lack of transparent procedures, and the multiplicity of contact points between tax payers and tax collectors in revenue collection, offers opportunities for corruption.

⁴ IMF, 2015a.

8. **Tax exemptions, under-declaration, and evasion are widespread.** A recent FAD TA report identified 140 exemptions, mostly in the mining sector, and estimated the foregone revenues from exemptions at 1.7 percent of GDP. These exemptions are granted under a set of 13 legislations, including the tax- and customs-code; the investment code, the 2002 Mining code; special mining conventions; as well as by administrative discretion. Also, the country's long, porous borders are difficult to monitor, facilitating tax and customs evasion. Excessive use of tax exemptions and a complex and fragmented tax code widen the gap between potential and actual revenue.

9. **The multiplicity of special taxes and fees, some accruing to special accounts outside the Treasury, generate opportunities for corruption and informalization of economic activity.** There are over 300 such taxes and fees, levied by a large number of agencies.

10. **The central government's single Treasury account at the BCC should facilitate the monitoring of public finances.** However, the central government also hold accounts in commercial banks. Treasury transactions in the fiscal and monetary accounts are not always consistent, making it difficult to reconcile central government fiscal accounts with monetary statistics. Furthermore, although provincial governments are required by law to hold their accounts at the BCC, they also hold accounts in and receive loans from commercial banks; these accounts are not identifiable in the monetary statistics.

Public Financial Management

11. **Despite some progress in strengthening public financial management, budget execution remains deficient.** The government has formalized the four stages of the expenditure chain and introduced budget commitment plans to align expenditures with revenues. Although fund transfers generally match budget appropriations, expenditure validation and payment orders are problematic and overdue payments are still common. Exceptional procedures are widely used, particularly following the recent crisis. They are required to go through the 4 stages of the expenditure chain and must be regularized within 48 hours, but this is often not the case. Furthermore, budget execution suffers from: (1) redundant and lengthy steps in budget execution processes, including various political interventions in the approval of commitments and payments; (2) abuse in the use of exceptional or emergency procedures; (3) excessive centralization of budget execution authority in the Ministry of Finance and the Ministry of Budget; and (4) inefficient use of public procurement procedures and entities, especially procurement units, that are not yet fully operational. According to the World Bank 2015 Public Expenditure Management and Financial Accountability Review (PEMFAR), the budget preparation process is strongly influenced by political considerations, often leading to the circumvention of instructions.

12. **The public procurement system was overhauled in 2010 and a Public Procurement Regulatory Authority established, but procurement practices remain weak.** The Public Procurement Law requires public contracts to be tendered, except in special circumstances. In theory, the procurement process is managed by the *Cellule de Gestion des Marches Publics*, but in

practice is managed by the Central Control Office, with deviations from public tender having to be approved by Director General for the Control of Public Contracts. The public tender requests and the results of the competitive process are required to be published but are not in practice. The law prescribes penalties against corruption, but this has failed to curb the practice.

13. **Until recently, about 60 percent of the general budget's spending passed through procurement channels.** Yet, only a small proportion passed through standard procedures, while the rest went through exceptional procedures or completely by-passed budgetary channels and were 'regularized' ex-post. The use of direct purchases, as opposed to public tenders, increased from 3 percent to 60 percent between 2013 and 2016.

14. **Low remuneration and weak institutional capacity undermine the civil service.** Currency depreciation and inflation have eroded 80 percent of the purchasing power of salaries and pensions of civil servants since 2015. The remuneration system is opaque, the exact number of civil servants is unknown, and many civil servants who have reached the age of retirement continue to work.

15. **Public services are inefficient and costly.** Health, education, water, and electricity services are underfunded. The health and education sectors rely heavily on user fees even though the central government pays the bulk of the salaries.

B. Central Bank Governance

16. **The BCC is nominally independent but has relied on budget transfers from the central government, undermining its independence.**⁵ The 2014 Financial Sector Stability Assessment noted that lack of operational independence constrained the BCC's ability to perform its functions. Notably, the Treasury has obtained direct advances from the BCC, contrary to the law. The recently approved Central Bank Law (December 2018) represents a step forward as it aims at reinforcing the BCC independence (including through a recapitalization) together with its accountability and transparency.

17. **Banking supervision and regulation capacity has been enhanced with Fund TA.** Regulations impose high penalties for non-compliance, but these are not applied consistently. The banking system is generally immune to overt political interference; however, some politically-connected banks sometimes get preferential treatment.

C. Market Regulation

18. **The economy is largely informalized and moderately regulated.** However, key sectors such as mining, banking, telecommunication, transport, and beverages, dominated by foreign interests and an important source of budget revenue, are subject to tighter controls.

⁵ The Government pays interest on a bond issued to the central bank, which has no fixed interest rate.

19. **The regulatory environment has improved over the last decade.** The 2015 World Bank Doing Business Report cited the DRC as one of the ten countries that had made the biggest advances. There are gaps between regulation and implementation, however. Entrenched vested interests benefiting from existing regulations and market distortions have resisted reforms.

20. **Regulation continues to weigh heavily on the cost of doing business.** DRC scores well below its regional peers on the World Bank Doing Business Indicators and the World Economic Forum Global Competitive Index. The Doing Business survey rates DRC well on starting a business, dealing with construction permits, and registering property, but not so well on protecting minority interests, paying taxes, trading across borders, and contract enforcement. Similarly, the World Economic Forum survey singles out the heavy burden of government regulations in DRC and the shortcomings of the legal framework to challenge regulations, as well as the burden of customs procedures and trade barriers.

21. **The rule of law is weak in DRC.** The Worldwide Governance Indicators rates the rule of law in the DRC well below its regional peers.⁶ Transparency International's Corruption Barometer and the World Bank Doing Business and Enterprise surveys all point to the judiciary as particularly corrupt. Private sector operatives have highlighted problems in the area of contract enforcement and property rights protection, and the lack of independence of the courts.

D. Combatting Corruption

22. **Despite the proclamation of a “zero tolerance” campaign toward corruption as early as in 2009 and the existence of anti-corruption laws, rampant corruption remains one of the DRC’s key problems.** Transparency and accountability are weak, including public procurement. Petty corruption is rampant – and in many cases the only means to survive for employees of the public administration – and largely considered normal by the population, despite a high level of frustration and a growing awareness of the severity of corruption.

23. **DRC is a signatory to various international conventions on corruption.** It became a signatory to the 2004 UN Convention Against Corruption (UNCAC) in 2010 but has yet to undergo a review of its implementation. In 2007, DRC ratified a protocol agreement with the Southern African Development Community (SADC) on Fighting Corruption.

24. **On the domestic level, the government has articulated a commitment to fighting corruption, launching several initiatives.** The Initiatives include the Observatory of the Code of Professional Ethics and the inclusive Anti-Corruption Pact in 2013.

25. **In relation to the anti-corruption framework, although some initial steps were made to establish an anti-corruption framework, it is not clear whether the legal and**

⁶ Use of perceptions-based indicators should be considered carefully, as they may reflect biases of respondents.

institutional framework is in line with the requirements of the UNCAC. Furthermore, the overall effectiveness of the framework is still weak. More precisely:

- **Anti-corruption policy and transposition of the UNCAC into domestic legislation:** In 2015, the position of Special Advisor reporting directly to the President was established. It is charged with developing strategies to promote good governance, fight corruption, and deter money laundering and the financing of terrorism, but no strategy has yet been formulated. DRC is yet to undergo the peer review against UNCAC, the first round of which will be focused on assessing DRC's compliance to Chapter III on the criminalization of corruption offenses and law enforcement and Chapter IV on international cooperation.
- **Declaration of assets:** The Constitution requires the President and political appointees to government to declare their assets to the Constitutional Court on entering and leaving office. It authorizes criminal prosecution for failure to do so. However, the disclosure is not made public and is not required for members of the legislature or the judiciary and other senior public officials at risk. It is not clear whether verification of the declarations and sanctions for non-compliance are properly conducted.
- **Prosecuting corruption:** DRC does not have an office dedicated to pursuing cases of corruption with sufficient autonomy to investigate and prosecute high-level cases. An office and a special advisor have recently been established to pursue corruption cases in the public service, but they lack independence and operational means. The level of enforcement against corruption is still low.

26. **Using anti-money laundering (AML) tools to tackle the proceeds of corruption.** Although some progress has been made, DRC should improve its AML/CFT framework informed by the upcoming mutual evaluation by Task Force on Money Laundering in Central Africa (GABAC) to help combat corruption and its proceeds. A 2014 draft AML/CFT assessment by the World Bank identified system-wide strategic deficiencies against the 2012 FATF standard. DRC became a member of the GABAC in late 2017 and a mutual evaluation of DRC's AML/CFT framework by the body is being finalized. The result of this exercise will help inform policy priorities in mobilizing the AML framework to help detect and deter acts of corruption, in particular, with respect to measures on politically exposed persons.

E. Some Recommendations

- **Budget process:** (i) Improve budget credibility by preparing supplementary budgets. (ii) Provide more information on the budget annexes and special annexes in the budget. (iii) Strengthen institutional oversight of public finances by granting the Court of Auditors and the Office of the Inspector General of Finance greater operational independence and adequate financial resources.
- **Strengthen revenue management** by rationalizing and merging revenue agencies and evaluating tax exemptions.

- **Public financial management:** (i) Restore normal public procurement and expenditure procedures. (ii) Expedite the transition to the Medium-Term Fiscal Framework, the Medium-Term Sector Expenditure Framework and Program Budgeting.
- **Improve the business environment** by simplifying tax payment procedures; and improving contract enforcement and the rule of law by insulating the courts from external influence.
- **State-owned enterprises:** require all state-owned enterprises, including commercial entities, to publish their financial statements

NATURAL RESOURCE MANAGEMENT¹

DRC remains one of the poorest countries in the world despite a large endowment of natural resources and has been prone to violent conflict over the years. The country lacks the critical institutions needed to ensure that natural resources promote sustainable inclusive growth. Increased transparency in their management and competitive bidding in the sale of assets and exploitation rights of state-owned enterprises would be key to reduce corruption and ensure that the state gets a fair share of the benefits.

A. Introduction

1. **DRC has a rich and diverse endowment of natural resources but remains poor and prone to conflict.** The country is the world's fifth largest copper producer and produces some sixty percent of the global output of cobalt. DRC is the fourth largest producer of diamonds in the world, and the largest tin producer. Gold, crude petroleum, zinc, and tin are also produced. Oil is also produced but the country remains a net importer. Ironically, DRC remains one of the poorest countries in the world. In 2014, 77 percent of the population lived below the poverty line of US\$1.90 (in purchasing power parity). The country ranked 176th out of 189 countries on the UNDP 2018 Human Development Index. DRC experienced state collapse in the 1990s, culminating in civil war from 1996 to 1997, and from 1998 to 2003. The two wars were fueled by the country's natural resources, drawing in neighboring countries. Rebellion currently affects the eastern and central regions, with about 5 million people internally displaced persons, the most in any country in the world.

2. **DRC's experience to date resonates with the natural resource curse thesis.** The thesis highlights the tendency for countries that are richly endowed with non-renewable natural resources to experience worse development outcomes than resource-poor countries. It pinpoints the following problems. First is corruption in the management of the resources, given the typically large rents. Second are overblown public expectations of the benefits and political pressures to spend the revenues—rather than save or invest them. Third, disputes over revenue allocation or the desire to appropriate the resources could trigger violent conflict. Fourth, some countries may simply lack the technical capacity to manage the resources. The powerful multinationals exploiting the resources often wield considerable advantage over the government in terms of expertise and access to information in the negotiation and implementation of contracts, and in dealing with complex natural resource taxation. DRC has experienced these problems. The country's sheer size—it is as large as Western Europe and is bordered by nine countries—and the diversity of the natural resources create additional challenges, necessitating a well-developed management machinery. The vast terrain also makes it difficult to police the resources and prevent smuggling.

¹ Prepared by Victor Davies.

3. **Some developing countries have managed their natural resources well, escaping the resource curse.** Botswana, the world's largest producer of diamonds, has been touted as the example par excellence. It went from being one of the 25 poorest countries in the world to becoming an upper-middle-income economy within thirty years (Meijia and Castel, 2012). Critical to this transformation was the fact that Botswana developed strong governance institutions before the resources were exploited. One specific policy it pursued was a fiscal rule that separates expenditures from revenues, shielding expenditures from fluctuations in diamond prices (Meijia and Castel, 2012).

B. Economic Contribution of Natural Resources

4. **Contribution to GDP and export earnings.** The contribution of natural resource extraction to GDP has been rising steadily from 11 percent in 2005-08 to 24 percent in 2012-13, and to 25-26 percent in 2014-17. Natural resources generate 95 percent of export earnings. Copper has accounted for over half of export earnings to date, followed by cobalt which now accounts for about a third. Natural resources account for about a third of government revenue. This figure excludes revenues generated by state-owned enterprises that do not pass through the Treasury.

5. **Fiscal revenue from natural resources has been modest in DRC relative to African peers.** It averaged 8.9 percent of commodity exports in DRC in 2014-17, compared with 17.5 percent among resource-intensive SSA countries—defined as countries for which natural resource exports make up at least 25 percent of commodity exports. DRC's aggregate domestic revenue-to-GDP ratio averaged 14 percent in 2012-15, compared with 20 percent in SSA as a whole.

6. **Artisanal mining is a major source of employment, especially for low-skilled labor.** The mining sector accounted for 10 percent of total employment in 2014. About a million artisanal miners are estimated to be employed in the mining of diamonds and gold (US Geological Survey 2014). Artisanal and small-scale miners are also involved in the production of copper and cobalt.

7. **Other benefits.** Mining regions and communities also benefit from infrastructure and social services—roads, schools, and hospitals—provided by mining companies.

C. Rules and Regulations

8. **The regime for mineral exploitation has seen various changes in the last three decades.** Prior to the mid-1990s, the exploitation of copper and cobalt was monopolized by the state-owned Générale des Carrières et des Mines (Gécamines). During the 1996-97 civil war, a rebel movement captured the copper belt region and began selling off the assets of Gécamines and awarding exploitation rights to private investors. To end this disorderly process, a new Mining Code was enacted in 2002, in a context of a country emerging from state collapse and civil war. The country was desperate to attract foreign investment and offered very generous

terms to entice investors to a high-risk environment. Exploitation rights were, in principle, issued on a liberal first-come, first-serve basis. The Code sought to liberalize the copper sector and create a level playing field for investors. It envisaged a uniform tax regime and a transparent process to secure mining permits. In reality, Gécamines became the private gatekeeper to exploitation rights to the copper and cobalt mines, exploiting a clause in the mining code that allows state-owned mining companies to retain their mining permits and sell them to other companies. Gécamines is now largely a junior partner in over 20 joint ventures with foreign companies. The production of copper and cobalt is now undertaken by nearly thirty companies. Gold and diamonds are mined by industrial and artisanal miners. A substantial proportion of their output is smuggled out of the country.

9. A revised mining code was introduced in June 2018, seeking to increase the benefits to the country. The following are the key elements of the revised code:

- **Higher taxes and royalties.** (i) Royalties on copper, cobalt, and gold increase from 2 to 3.5 percent; a new 10 percent royalty is imposed on “strategic minerals”. The designation of a mineral as “strategic” is arbitrarily determined by government decree, based on “economic context” and taking into account “critical” or “geostrategic” considerations. The base for computing royalty changes from net to gross revenue. (ii) The allocation of free shares to the state on new projects increases from 5 to 10 percent, with an additional 5 percent increase each time a license is renewed. (iii) Income tax remains unchanged at 30 percent. (iv) Elimination of the option for accelerated depreciation of 60 percent. (v) A tax of 0.3 percent of business turnover is imposed as contribution to local development.
- **A new 50 percent tax on so-called windfall profit.** Windfall profits are defined as profits realized when the price of the mineral resource is more than 25 percent higher than envisaged in the feasibility study.
- **The changes take immediate effect.** This breaches and eliminates the stability clause under the 2002 Mining Code, which protected existing mining companies from any changes to the fiscal regime for the 10 subsequent years, a generous provision.
- **Additional provisions to increase domestic content.** (i) At least 10 percent of the equity of any project must belong to Congolese nationals. (ii) Subcontractors must be Congolese, unless no local subcontractor is in a position to provide the desired good or service.
- **All export earnings in foreign currency should be repatriated to local banks once the investment is amortized** (60 percent of earnings should be repatriated before the investment is amortized).
- **Permit holders not to exceed a debt-to-equity ratio of 1.5.**

10. The revised Mining Code has its merits and flaws. The rates for royalties—except for strategic minerals—and the elimination of accelerated depreciation, are in line with standard

practice.² Terminating bilateral mining agreements outside the Mining Code would help create a more level-playing field for investment and reduce the incentive for rent-seeking and corruption. On the other hand, the windfall profit tax appears ambiguous. It is not clear how windfall profit would be distinguished from normal profit. The discretionary power to classify minerals as “strategic”, which carry the 10 percent royalty rate, would increase the risk and potential cost of investing in mining activity in DRC. The increase in the allocation of free shares to the state by five percent of total shares each time a license is renewed, would mean that, over time, the state would hold a large percentage of free shares in private mining projects. This would be excessive relative to international norms, serving as a strong deterrent to invest or renew mining licenses. The requirement to repatriate all foreign currency earnings once the investment is amortized would hinder profit repatriation, and thereby discourage investment. Lastly, the removal of the ten-year stability clause under the 2002 Mining Code raises legality and policy credibility issues.

11. **Mining companies have been critical of the revised Mining Code, claiming that it would deter investment.** They claim that they were not consulted during the revision process, and that the code could reduce fiscal revenues from natural resources, and threaten jobs, social programs, and infrastructure projects. They are also particularly concerned about the termination of the ten-year stability clause, which they perceive as a breach of a legally binding commitment. They have threatened recourse to international litigation.

12. **President Tshisekedi, inaugurated in January 2019, has endorsed the revised Mining Code.** Mr. Tshisekedi stated that his Government will continue to enforce the code while remaining open to dialogue with mining companies to hear their concerns.

D. Transparency and Accountability

13. **The degree of compliance with a 2011 decree requiring the government to publish all mining, oil, and forestry contracts remains unclear.** A Fund-supported Extended Credit Facility was suspended in 2012, and eventually discontinued, over the authorities’ failure to publish a mining contract. Environmental and social impact studies for mining projects have also not been published.

14. **DRC signed the Extractive Industries Transparency Initiative in 2008.** The EITI is a “global standard to promote the open and accountable management of oil, gas and mineral resources.” EITI requires mining companies operating in member countries to make public how much they pay in natural resource revenue and governments to also make public how much they receive. The last published report for the DRC was for 2016, published in 2018. The EITI reports show only a minor divergence between tax revenues paid by the resource sector and the amounts received by the Treasury. While reconciling payments made by mining companies and revenue received by government would help foster transparency, subsequent stages in managing the revenues remain weak—particularly at the provincial and local levels. Also, public enterprises generate substantial revenues that are not passed to the public treasury. These lie

² The elimination of accelerated depreciation had been recommended by the Fund’s Fiscal Affairs Department.

outside the EITI reconciliation exercises. Lastly, the EITI does not establish whether the government is receiving a fair share of the revenue from the exploitation of natural resources.

15. **The law only requires companies to disclose their legal owners, not their beneficial owners.** Requiring companies to disclose their beneficial owners can promote transparency and serve as a check against corruption and conflicts of interests. The 2015 EITI report for DRC states that more than half of private mining companies disclosed their beneficial owners.

16. **Civil society has raised concerns over the management of the state-owned Gécamines.** Such concerns include allegations of undervalued asset sales, outright failure to account for revenues, failure to publish contracts with joint-venture partners, political interference, and conflict of interest (Carter Center 2017, Global Witness, July 2017, Natural Resource Governance Institute 2015). Gécamines has refuted some of these allegations (Gécamines 2019), which, nevertheless, highlight the need for increased transparency and accountability in the management of state enterprises.

E. Revenue Management

17. **Institutional capacity to assess and collect resource revenue is weak.** The revenue agencies lack the skilled human and informational resources to monitor the activities of mining companies and deal with the complexities of natural resource taxation, especially where multinational corporations are involved.

18. **Revenue agencies are permitted by law to issue penalties and keep a portion of the fines for their own funding, an incentive for predatory behavior.** Penalties are sometimes imposed on spurious grounds and the fines can be considerable, running into hundreds of millions of dollars (Global Witness, 2017).

19. **The SICOMINES joint-venture project between the Government and a consortium of Chinese firms has been operating as a parallel revenue and spending structure, bypassing the budget.** The project involves a multi-billion dollar loan from the consortium for infrastructure and a signature bonus. The loan disbursement is made into SICOMINES' accounts, with SICOMINES then directly disbursing money for specific infrastructure projects. The loan is repayable with future copper and cobalt output from the project.

20. **Revenue sharing with the mining provinces has been problematic.** The 2018 Mining Code stipulates that the central government keeps 50 percent of royalties; 25 percent to the provincial administration where the project is located; 15 percent to the area where the mining takes place; and the remaining 10 percent to a mineral fund for future generations. Civil society organizations have stated in the past that the mining provinces were getting much less than the stipulated amounts under the 2002 Mining Code, prompting the provinces to impose their own taxes and charges. The 2018 Mining Code requires mining companies to pay revenues directly to provinces.

F. Peacebuilding and Conflict Prevention Initiatives

21. **In 2003 DRC joined the Kimberley diamond certification scheme (KPCS)**—an initiative that unites government, civil society, and the diamond industry to remove conflict diamonds from the global supply chain. The Kimberley Process Certification Scheme (KPCS) imposes extensive requirements (*) on its members to enable them to certify shipments of rough diamonds as 'conflict-free' and prevent conflict diamonds from entering the legitimate trade. Under the terms of the KPCS, participating states must meet 'minimum requirements' and must put in place national legislation and institutions; export, import and internal controls; and also commit to transparency and the exchange of statistical data. Participants can only legally trade with other participants who have also met the minimum requirements of the scheme, and international shipments of rough diamonds must be accompanied by a Kimberley Process certificate guaranteeing that they are conflict-free (<https://www.kimberleyprocess.com/en/about>).

G. Recommendations

22. **Increased transparency is critical for reducing corruption and improving governance of natural resources.** This can be achieved through the following;

- Full publication of all future mining contracts, and contracts signed since 2012; and timely publication of all future EITI reports.
- Active involvement of civil society in the management of the natural resources.

23. **A review of the management of the state-owned Gécamines is urgently needed.** The objective would be to enhance transparency and make the company commercially viable. A measurable milestone would be the timely publication of annual audited financial statements. An investigation into revenues that have not been properly accounted is warranted.

24. **A review the Sicomines model with a view to reinforcing transparency and parliamentary oversight is also needed.**

25. **Simplification of taxation and rationalization of revenue agencies would improve efficiency, oversight, and transparency:** There is a need to eliminate parallel state structures and centralize revenue collection. Discontinuing the practice of allowing revenue institutions to keep a share of the fines they levy, would remove the incentive for abusing the power to levy such fines.

26. **Adopting a fiscal guideline or rule based on the non-mineral balance** would help shield expenditures from fluctuations in natural resource prices and facilitate the building of buffers.

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POVERTY AND GOVERNMENT SOCIAL SPENDING¹

A. Update on Poverty and Vulnerability

1. **Poverty remains pervasive across all dimensions (Table 1).** The last household income and consumption survey, which took place in 2012, remains the main source of available data, though there have been other surveys related to social sectors. According to the data, out of the 83 million Congolese, 77 percent live below the poverty line of PPP\$1.9 a day (the SSA average is 43 percent); 90 percent of workers make less than PPP\$3.10 a day and are therefore working poor; and 42 percent of the population is in severe multidimensional poverty. These indicators are significantly worse than most countries in a group of peers.

2. **A high level of vulnerability suggests that poverty could continue to worsen.** Vulnerability refers to the risk of falling into poverty if identified events were to occur. There are many such events or potential occurrences in DRC including, to name a few, armed conflict, political crises, natural disasters, disagreements with neighbors (such as the one that resulted recently in the deportation of hundreds of thousands of Congolese from Angola), and epidemics. The number of Congolese vulnerable to multidimensional poverty is almost 18 percent. More than six million Congolese are either refugees or internally displaced and many are either poor or facing the risk of falling into poverty.

3. **The socio-political situation in the DRC contributes to creating more poverty.** The Ebola outbreak in the North-East shows no sign of abating. To the contrary, the lethality rate is picking up, as efforts to combat the disease are being thwarted by armed groups who routinely attack Ebola screening and treatment facilities. Cholera, which is endemic in many parts of the country, killed more people than Ebola in 2018. Hundreds of armed groups around the eastern border are disrupting economic activities and contributing to the increase in poverty and vulnerability in the affected communities. Millions of internally displaced and deported refugees are living in squalor under temporary shelters, breeding more poverty.

4. **Income and gender inequality in DRC worsen the poverty situation.** The Gini coefficient, at 42 percent, is relatively high, although not the highest among peer countries. However, the gender inequality index is the highest (Table 1), along with the gap between the human development index for males and females. Specific areas are particularly problematic. Sexual violence against women and girls in conflict-afflicted eastern regions of the country has reached epidemic proportion, famously leading to the activist doctor Denis Mukwege winning the 2018 Nobel peace prize for denouncing such abominations and for devoting his professional life (at a very high risk for his and his colleagues' lives) to assist the victims.

5. **Some of the social indicators reflect the high level of poverty and may reinforce poverty.** The rates of child mortality, lack of immunization, and child malnutrition and stunting in

¹ Prepared by Philippe Egoume with contributions from Emmanuel Gbadi and Yanki Kalfa.

DRC are among the highest compared to peer countries. Overall mortality attributable to polluted air and unsafe water and poor hygiene is also very high, as well as malaria incidence. On a brighter side, both inputs and outputs in the education sector appear to be within ranges in peers.

Table 1. Poverty, Vulnerability, Inequality, and Social Indicators in Selected Countries

| | DRC | Ethiopia | Nigeria | Kenya | Uganda | Botswana | Cambodia |
|--|-------|----------|---------|-------|--------|----------|----------|
| Poverty | | | | | | | |
| Working poor at PPP\$3.10 a day (% of total employment) | 90.5 | 51.5 | 71.7 | 26.8 | 52.4 | 21.2 | 46.4 |
| Multidimensional Poverty Index (MPI) | 0.378 | 0.49 | 0.294 | 0.179 | 0.279 | n.a | 0.158 |
| Population in multidimensional poverty, headcount (%) | 72.5 | 83.8 | 52 | 38.9 | 56.8 | n.a | 34.9 |
| Population in multidimensional poverty, headcount (thousands) (for the year of survey) | 53417 | 85834 | 99166 | 17890 | 23549 | n.a | 5328 |
| Population in multidimensional poverty, headcount (thousands) (projection for 2016) | 57050 | 85834 | 96623 | 18837 | 23549 | n.a | 5499 |
| Population in multidimensional poverty, intensity of deprivation (%) | 52.2 | 58.5 | 56.7 | 46 | 49.1 | n.a | 45.3 |
| Population in severe multidimensional poverty (%) | 42.2 | 61.8 | 32.7 | 13.4 | 25.4 | n.a | 12 |
| Population living below income poverty line, PPP \$1.90 a day (%) | 77.1 | 26.7 | 53.5 | n.a | 35.9 | n.a | n.a |
| Internet users, total (% of population) | 6.2 | 15.4 | 25.7 | 26 | 21.9 | 39.4 | 32.4 |
| Mobile phone subscriptions (per 100 people) | 36.7 | 50 | 83 | 80.4 | 55 | 146.2 | 126.3 |
| Vulnerability | | | | | | | |
| Population vulnerable to multidimensional poverty (%) | 17.7 | 8.7 | 16.9 | 34.7 | 23.9 | n.a | 21.1 |
| Vulnerable employment (% of total employment) | 53.5 | 88.2 | 80.4 | 54.3 | 74.5 | 15 | 51 |
| Homeless people due to natural disaster (average annual per million people) | 31 | 2 | 7 | 12 | 718 | 0 | 356 |
| Refugees by country of origin (thousands) | 611.9 | 87.5 | 216 | 7.6 | 6.4 | 0.3 | 12.2 |
| Young age (0-14) dependency ratio (per 100 people ages 15-64) | 91.3 | 72.5 | 82.6 | 71.2 | 95.2 | 48.6 | 48.6 |
| Inequality/Gender inequality | | | | | | | |
| Income inequality, Gini coefficient | 42.1 | 39.1 | 43 | 48.5 | 41 | 60.5 | n.a |
| Gender Inequality Index (GII) | 0.652 | 0.502 | n.a | 0.549 | 0.523 | 0.434 | 0.473 |
| Human Development Index (HDI), female | 0.42 | 0.424 | 0.494 | 0.568 | 0.475 | 0.707 | 0.553 |
| Human Development Index (HDI), male | 0.493 | 0.501 | 0.569 | 0.61 | 0.55 | 0.725 | 0.605 |
| Health | | | | | | | |
| Child malnutrition, stunting (moderate or severe) (% under age 5) | 42.7 | 38.4 | 43.6 | 26.2 | 28.9 | 31.4 | 32.4 |
| Infants lacking immunization, DPT (% of one-year-olds) | 18 | 15 | 51 | 7 | 5 | 2 | 6 |
| Infants lacking immunization, measles (% of one-year-olds) | 20 | 35 | 58 | 11 | 20 | 3 | 16 |
| Mortality rate, infant (per 1,000 live births) | 72 | 41 | 66.9 | 35.6 | 37.7 | 32.6 | 26.3 |
| Mortality rate, under-five (per 1,000 live births) | 94.3 | 58.4 | 104.3 | 49.2 | 53 | 40.6 | 30.6 |
| Malaria incidence (per 1,000 people at risk) | 291.9 | 53.1 | 349.6 | 85.3 | 187.2 | 2.4 | 8.9 |
| Mortality rate attributed to household and ambient air pollution (per 100,000 population) | 163.9 | 144.4 | 307.4 | 78.1 | 155.7 | 101.3 | 149.8 |
| Mortality rate attributed to unsafe water, sanitation and hygiene services (per 100,000 pop) | 59.8 | 43.7 | 68.6 | 51.2 | 31.6 | 11.8 | 6.5 |
| Education | | | | | | | |
| Expected years of schooling (years) | 9.8 | 8.5 | 10 | 12.1 | 11.6 | 12.6 | 11.7 |
| Gross enrolment ratio, primary (% of primary school-age population) | 108 | 102 | 94 | 105 | 100 | 105 | 110 |
| Literacy rate, adult (% ages 15 and older) | 77 | 39 | 51.1 | 78.7 | 70.2 | n.a | 73.9 |
| Population with at least some secondary education (% ages 25 and older) | 50.7 | 15.8 | n.a | 34.6 | 31.7 | 89.2 | 21.3 |
| Government social expenditures | | | | | | | |
| Current health expenditure (% of GDP) | 4.3 | 4 | 3.6 | 5.2 | 7.3 | 6 | 6 |
| Government expenditure on education (% of GDP) | 2.3 | 4.5 | n.a | 5.3 | 2.3 | n.a | 1.9 |
| Ratio of education and health expenditure to military expenditure | 5.1 | 10.6 | n.a | 8 | 5.4 | n.a | 4.8 |

Sources: UNDP Human Development Reports, 2018

B. Government Strategies and Policies to Tackle Extreme Poverty and Vulnerability

6. **The authorities have developed a national social protection policy (SPP) focusing on four dimensions of social protection.** The SPP dimensions include (1) access to health care through universal health coverage; (2) early childhood, with an emphasis on nutrition, health and education for children; (3) income security for people in difficult circumstances, especially the most vulnerable, and (4) old age, especially the elderly who are indigent. However, not all of these dimensions have been operationalized and only a few concrete programs have been implemented.

7. **The government has set up several social assistance mechanisms that are part of the SPP, which so far have benefited only a limited number of people.** These mechanisms include (i) social insurance, (ii) social safety nets, and (iii) social assistance programs.

- **Social insurance** schemes cover risks related to work and provide pensions for disability, old-age, and survivors as well as family allowances for the Katanga province.
- **Social safety net mechanisms** are non-contributory transfer programs (conditional or not) that aim to directly support the consumption of poor and vulnerable people as well as guarantee their access to essential social services.
- **Social assistance programs** promote investment in human capital. These programs support populations affected by shocks and aim at breaking the intergenerational cycle of poverty transmission.

8. **The main social safety net mechanisms provide conditional assistance or transfers.** These include exemptions from fees to access some health and education services, based on the “certificate of indigence,” issued by the Ministry of Social Affairs. Such certificates target vulnerable children and women, the elderly, internally displaced persons, and refugees. However, the program has been abused as well-to-do civil servants have had access to it. In 2013, the program covered around 5,604 people, 69 percent of them in Kinshasa. The administrative cost of US\$25 to US\$50 to obtain the certificate has essentially eliminated the vulnerable populations that the program was supposed to target. There is also a cash transfer program funded by DFID and administered by UNICEF that aims at providing vulnerable families affected by forced population movements with access to unconditional cash transfers. During the 17 months of program implementation, 23,534 families (117,670 people) have been assisted.

9. **The coordination of social protection activities needs to be strengthened.** Several organizations have been set up to coordinate social protection activities undertaken by different ministries. However, there is unnecessary redundancy which needs to be eliminated.

C. Assessment of DRC Government Expenditures

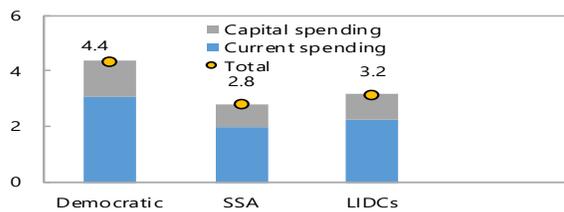
10. **DRC fares worse than peers in terms of spending efficiency.** This analysis is based on FAD’s Expenditure Assessment Tool (EAT).

11. **Total expenditures remain modest and current expenditure have increased more than investment in recent years.** Between 2004 and 2016 spending in DRC increased by 4.4 percent of GDP, more than in SSA, but the majority went to current spending. In 2016, current spending represented 65 percent of all spending, while capital expenditures amounted to 19 percent (73 percent and 27 percent in SSA, respectively). Data from 2015 shows that investment picked up since the early 2000s, but the stock of public capital in percent of GDP is just a little more than half the average of LIDCs.

12. **The wage bill in DRC has steadily grown from less than 1 percent of GDP in 2000 to around 5 percent of GDP in 2014.** While the wage bill in percent of GDP in the DRC is in the 10-percentile range of emerging and middle-income countries, it is close to the 90-percentile range in terms of percentage of public expenditures, with the compensation of government employees representing over one third of expenditures, against 28 percent in LICs. This also reflects the fact that DRC expenditures are relatively low as a result of limited government revenue.

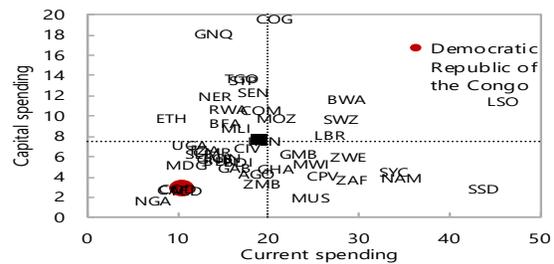
Figure 1. Government Spending and Economic Classification 1/

Change in Total Spending (in percent of GDP), 2004 - 2016



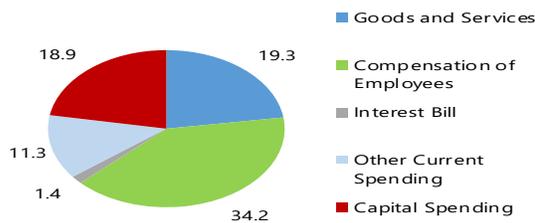
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Current and Capital Spending (in percent of GDP), 2016 2/



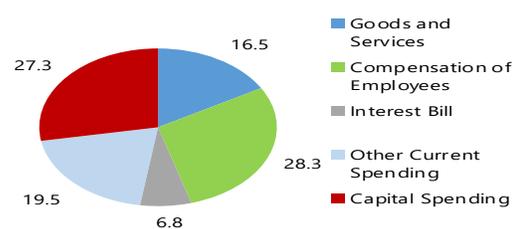
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Democratic Republic of the Congo -- Economic Classification (in percent of total), 2016



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SSA -- Economic Classification (in percent of total), 2016

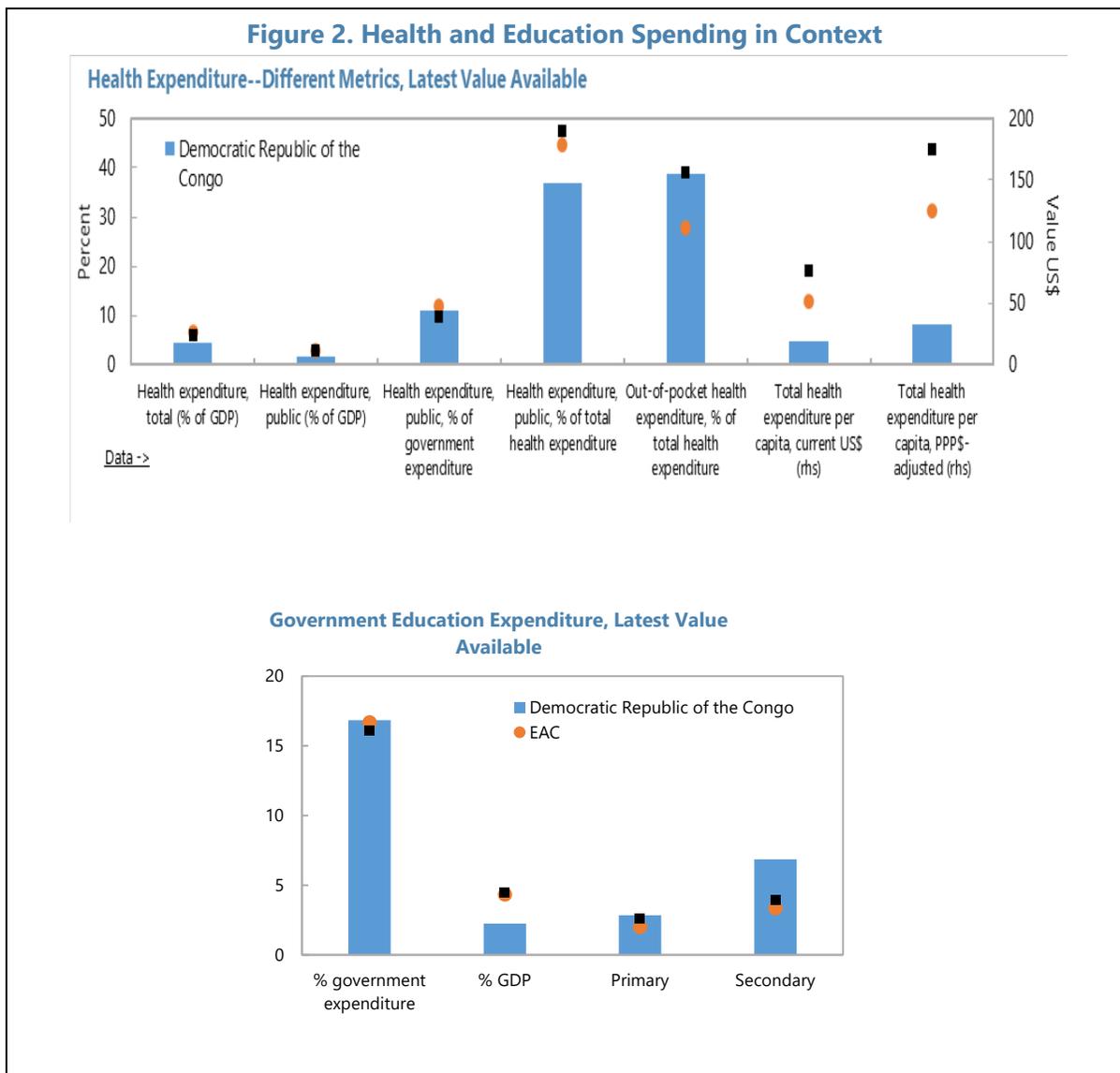


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Source: IMF FAD Expenditure Assessment Tool (EAT), World Economic Outlook.
 1/ Coverage refers to general government as per World Economic Outlook metadata.
 2/ Dashlines are the average of SSA.

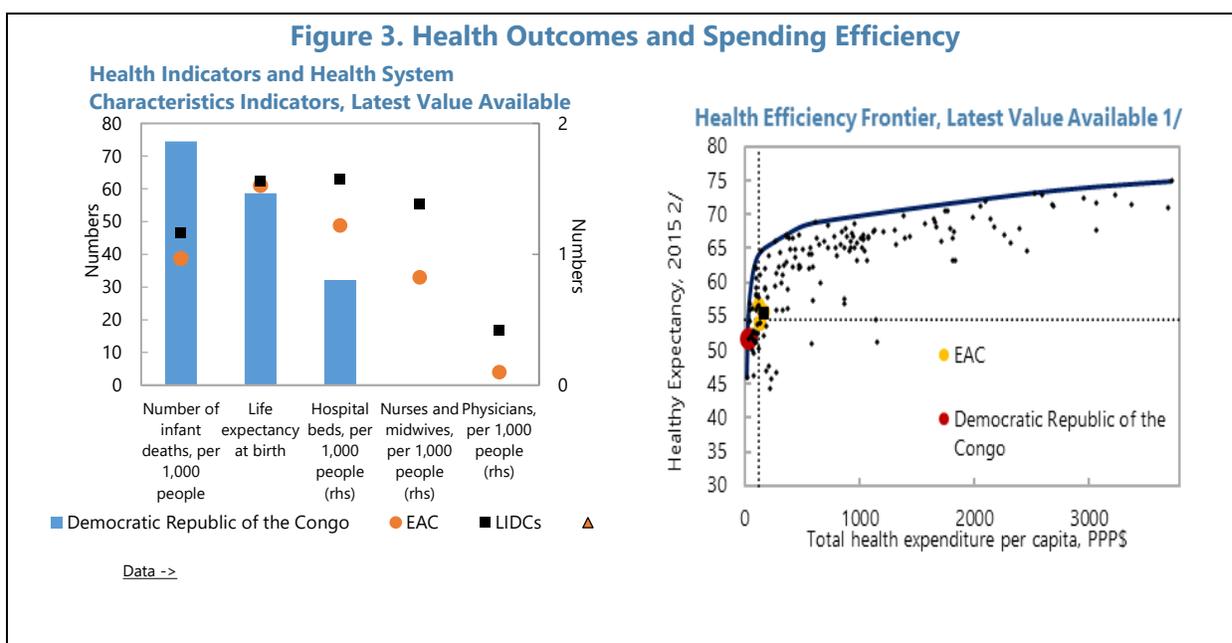
13. **DRC social spending is generally lower than peers.**

- **Health public spending** measured across a broad range of indicators is lower than the average for LICs, and out-of-pocket payments by households is higher than in other LICs (Figure 2).
- **DRC spending in education is comparable to other LICs in relative terms.** The DRC government devoted around 17 percent of its spending to education. But in percent of GDP, DRC lags comparators as it spends only around 2.5 percent of GDP against around 4.5 percent for the reference groups. In PPP terms, DRC government spending per student is just a few dollars in the primary and secondary education and a little less than US\$500 in the tertiary education. These levels are several multiple lower than the average in LICs.



14. **Health spending outcomes are weak, which given DRC’s low level of spending paradoxically would put DRC on the health efficiency frontier.**

- **Health outcomes are poor across the board, sometimes markedly weak compared to LIDCs, although not all the data monitored is available.** For instance, the number of infant deaths per 1,000 people in DRC is 72, against around 45 in LIDCs (Figure 3). DRC is located on the Southwest end of the efficiency frontier with low spending and low outcomes, implying that there is a degree of efficiency in utilizing scarce resources.
- **Budgetary allocations rarely reach reference hospitals, which then need to resort to service fees at levels that would price out the poorest and most vulnerable (DFID, 2018).** The lack of government oversight in the education of medical doctors expose patients to poor medical services and exaggerated drug prescriptions. The DFID study demonstrates that there is significant scope for improving the efficiency of health services and stresses the need for the government to devote more budgetary resources to health.
- **Regarding education, DRC actually has a higher teacher-student ratio per 100 compared to reference groups for both primary and secondary education.** In terms of outcomes, the adult literacy ratio at 77 percent is similar to reference groups.



D. Conclusions and Policy Recommendations

15. **Addressing DRC’s social development needs will require a complex set of policies and interventions.** For a start, bringing peace to conflict-afflicted parts of the country would help reduce poverty and vulnerability by boosting economic activity and employment. No intervention can succeed unless there is peace and stability, as demonstrated by the difficulty of

bringing medical assistance in some Ebola-afflicted areas. In that respect, policies should target the reduction of both poverty and vulnerability.

16. **There is an urgent need to increase government spending for social outlays**, which would require both mobilizing more revenue and prioritizing spending in social sectors. Given scarce resources, policies should focus on improving spending efficiency.

17. **Support efforts by civil society and social activists can hugely help and should be protected.** The inspiring story of Dr. Mukwege underlines the need to combat decisively violence against women and more generally make efforts to promote gender equality.

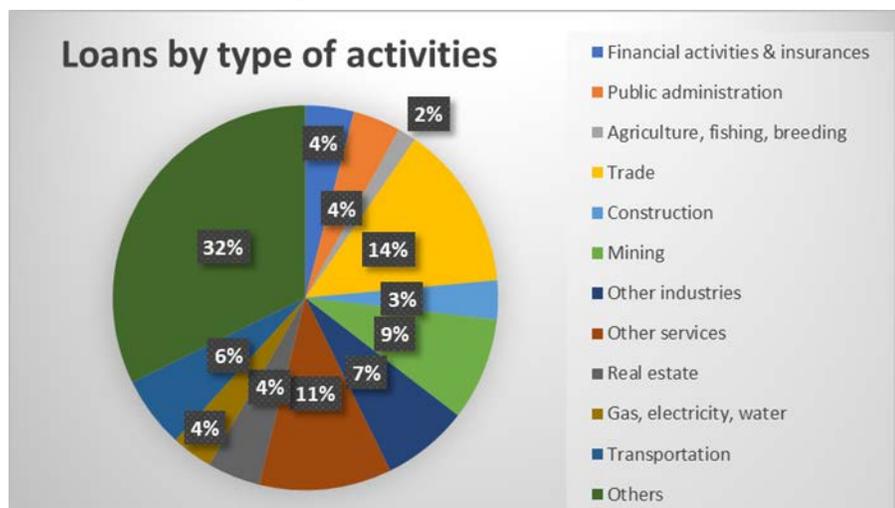
18. **Improving data quality and availability is critical to proper design and implement social programs.** In particular, household consumption and income surveys should be refreshed to get updated data; better data would help improve and support the targeting of government programs.

MACROFINANCIAL LINKAGES¹

A. Financial Sector Overview

1. **The financial sector of the Democratic Republic of the Congo (DRC) is shallow, underdeveloped, and dominated by banks.** The financial sector comprises 17 active licensed banks (including the BIAC currently under Central Bank of Congo (BCC) administration) with total assets of US\$5.3 billion (or 7 percent of GDP at end-2018). Banks can be classified in three groups: (i) 3 large banks (Rawbank, BCDC, and TMB), which dominate the sector with 49 percent of total assets, 53 percent of deposits, and 49 percent of loans; (ii) 4 medium size banks (Equity Bank, Ecobank, Afriland FB, and FBNBANK DRC) with 48 percent of total assets, 32 percent of deposits, and 31 percent of loans; and (iii) 10 small banks. One of the smallest banks, Advans Banque, applied to become a microfinance institution (MFI). The relatively large high number of lenders is due to loose banking regulations and relatively low minimum capital requirements. The competition is fierce, but many banks are poorly capitalized which leaves them vulnerable to shocks. Out of the 17 banks, 10 have met the capital requirements of US\$30 million, and the remaining 7 should comply before the end of the year. The minimum capital requirements will increase to US\$50 million at end-2020. Over 85 percent of loans and deposits are concentrated in the provinces of Haut-Katanga and Kinshasa.

2. **The financial sector is highly dollarized.** At end-2018, 90 percent of deposits were in US dollars. Banks' funding is mainly composed of sight deposits from the private sector (companies and households hold, respectively, 37 and 54 percent of total deposits). 94 percent of loans are also denominated in US dollars, with the largest share of clients being commercial entities (59 percent of total loans) mostly in the trade, services, and mining sectors.



3. **Non-bank financial institutions are numerous but represent only 5 percent of the banking system's assets.** They are a state insurance company (SONAs), the National Social Security Institute (INSS), 4 private insurance companies and 2 insurance brokers, 5 specialized institutions, 98

¹ Note prepared by Claire Gicquel.

microfinance intermediaries (cooperatives and MFIs) 83 financial messaging companies, and 32 forex exchange bureaus. There are no stock or debt capital markets in the DRC.

4. **Banks' activities are mostly characterized by transactions with correspondent banks abroad.** About 70 percent of the banking system's operations are with correspondent banks.

Correspondent transactions allow banks to conduct settlement of USD denominated transactions. These holdings of dollars in correspondent accounts are expensive for depositors as they are not remunerated and are subject to high transaction costs.

5. **Correspondent banks are few and represent an important vulnerability of the financial sector.**

Three banks serve as correspondent banks in principle, however Citibank is the only effective operator. The BCC has been facilitating operations to settle international transactions among local banks as using swift transfers could be time consuming and, consequently, avoiding international regulation. Some prominent Congolese nationals have been sanctioned by the USA and the EU, affecting negatively the country's image. Completing AML/CFT framework and adopting anti-corruption laws are crucial to avoid disruptions in the financial sector, limit transaction costs, and protect bank ratings.

6. **The banking regulatory framework is being strengthened.** A new Central Bank Law entered into force in January 2019. It enhanced the BCC functional and financial autonomy and strengthened its governance, transparency, and accountability frameworks. The Banking Law governing all credit institutions is being revised.

B. Key Macro-Financial Linkages

7. **The mining sector is a key driver of the country's economy as it represents the main source of growth.**

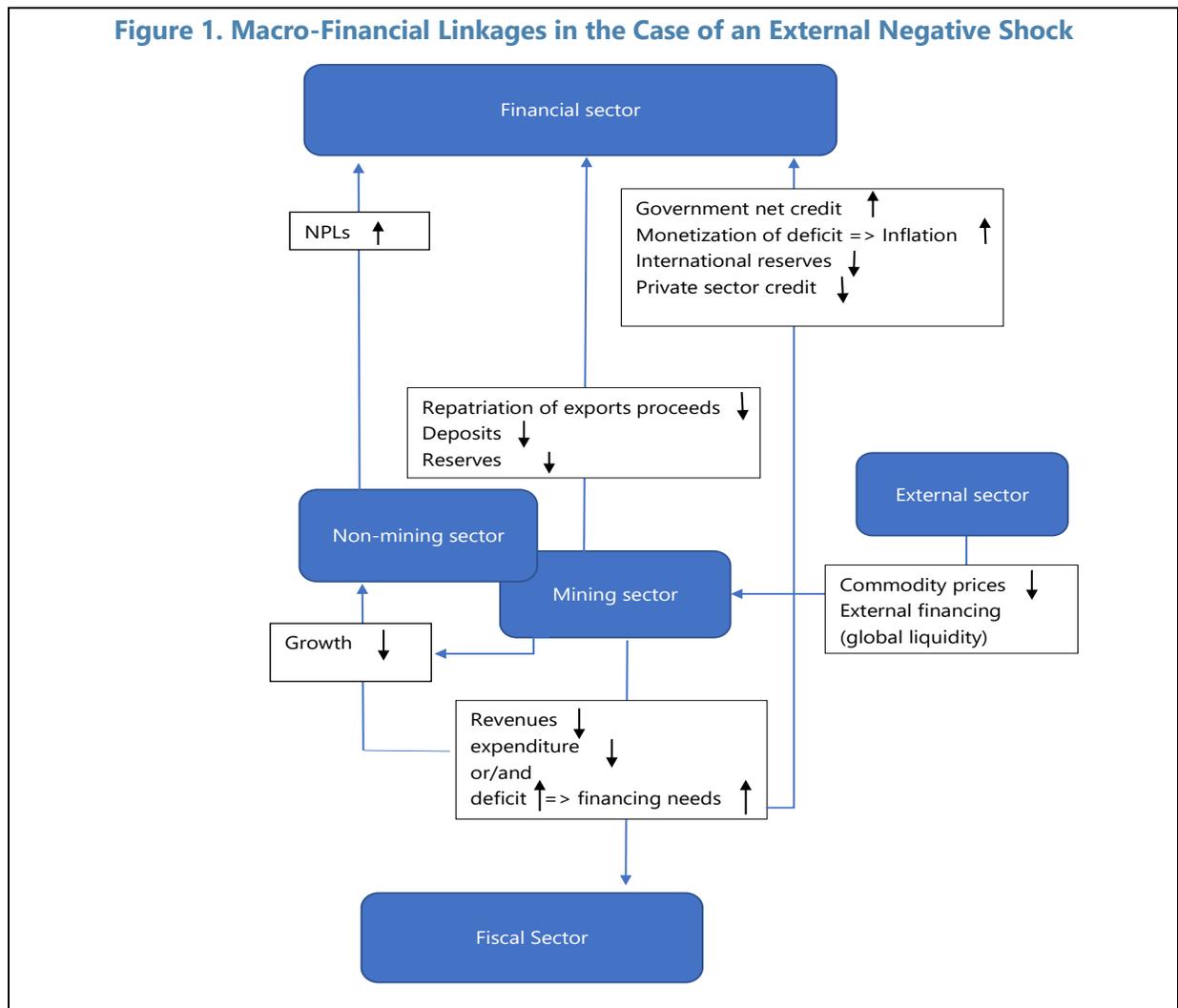
It represented about 10 percent of GDP and 94 percent of exports and contributed to 40 percent of GDP growth in 2018. The sector is composed by industrial mining dominated by foreign companies driving large scale mining and artisanal mining. Both industrial and artisanal mining employ officially only around 4 percent of Congolese workers. However, it is estimated that 10 million people depend directly or indirectly from the artisanal mining sector, or 12.5 percent of the total population. The sector is entirely dollarized and plays an essential role in ensuring the availability of foreign currency. While the 2002 Mining Code was designed to attract foreign investment, the 2018 Mining Code aims at increasing spillovers to the rest of the economy. To that effect, taxes and royalties increased, and the mandatory repatriation of export revenues was raised to 60 percent from 40 percent previously (see SIP on Natural Resource Management).

8. **The exposure to commodity price or production shocks has strong macro-financial implications.**

The recent commodity price shock illustrates well the vulnerabilities of the country and its financial system (Figure 1). Copper—accounting for 50 percent of exports—lost 45 percent of its value compared to 2011. The currency depreciated by a cumulative 71 percent, and inflation rose by 42 percent between 2015 and 2017. Fiscal revenues dropped by more than 2 percentage points of GDP as resource revenue accounts for about a quarter of fiscal revenues. Even with a drastic reduction of its expenditure levels, government deposits at the BCC were depleted, the rule of no

BCC financing of the budget was breached, and domestic arrears started to be accumulated. In that context, foreign reserves dropped below 3 weeks of imports.

9. **Given limited buffers and access to external financing, the government response to the shock affected the banking system in various ways.** The lower level of public spending hit the non-mining sector directly through economic agents depending on public contracts. This triggered lower growth in the non-mining sector and an increase in NPLs as public contracts did not materialize or obligations were not honored as the government accumulated domestic arrears. Net credit to the government by the banking system increased, as the government had limited means to finance its increased deficit, leading to a crowding out of credit to the private sector. Additionally, the fiscal deficit was monetized by the BCC which fueled inflation and led to a depreciation of the local currency. This affected the purchasing power of domestic economic agents and their capacity to repay bank loans and exposed banks to currency risks from a mismatch between assets and liabilities in foreign currency. The resulting and compounded increase in NPLs weakened the balance sheet of the banks.



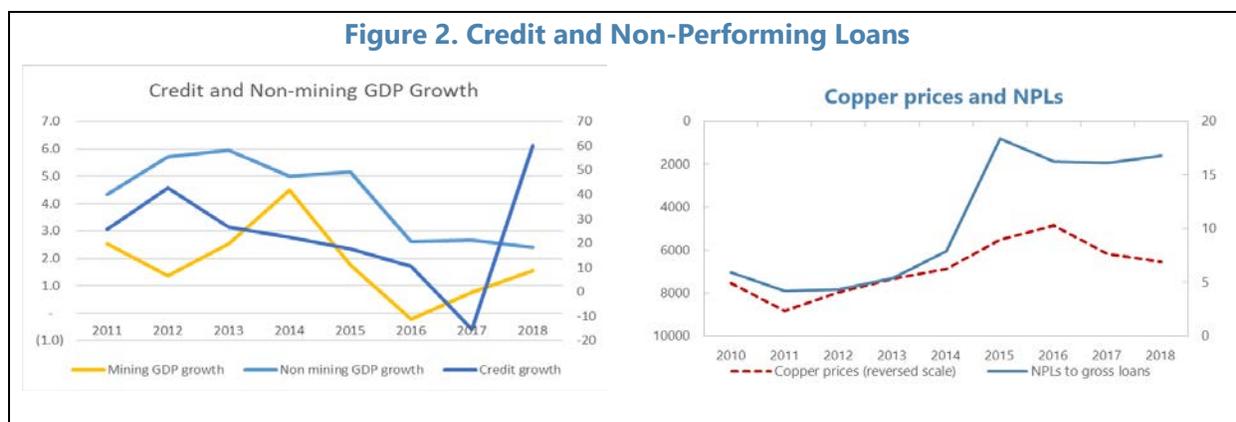
Text Table 1. Democratic Republic of the Congo: Selected Financial Soundness Indicators, 2014-19

| | 2014 | 2015 | 2016 | 2017 | 2018 | Mar-19 |
|--|--------|--------|--------|--------|--------|--------|
| Adequacy | | | | | | |
| Regulatory capital to risk-weighted assets | 23.7% | 20.4% | 9.0% | 16.0% | 14.2% | 14.8% |
| Asset quality | | | | | | |
| NPLs to gross loans | 7.9% | 18.3% | 18.1% | 16.1% | 16.8% | 16.0% |
| Earnings and profitability | | | | | | |
| Return on assets (net income/total assets) | 1.8% | 1.5% | -1.4% | -0.1% | 1.1% | 0.3% |
| Interest margin to gross income | 37.6% | 37.6% | 35.8% | 35.4% | 31.3% | 43.9% |
| Liquidity | | | | | | |
| Liquid assets/total deposits to short-term liabilities | 127.8% | 117.7% | 119.0% | 125.6% | 153.9% | 159.3% |
| Sensitivity to market risk | | | | | | |
| Foreign currency-denominated loans to total loans | 81.9% | 85.6% | 85.1% | 93.7% | 93.5% | 93.8% |

Source: Central Bank of the Democratic Republic of the Congo (BCC).

10. **Most financial soundness indicators deteriorated dramatically since 2014 (Text Table 1), showing the low resilience of the financial sector to external shocks.** Loans are mostly denominated in foreign currency (94 percent in 2018), but many borrowers' income is in local currency. As a result, employees that are paid in Congolese franc reportedly convert their salaries in foreign currency immediately to minimize exchange rate risk. NPLs reached almost 17 percent of total loans in 2018, up from 7 percent in 2014 as a result of the difficulties faced by domestic borrowers to reimburse their loans following a large exchange rate depreciation and a slowing economy. In addition, the accumulation of domestic arrears by the government worsened the situation of private suppliers depending on public contracts. The return on assets became negative during the crisis and capital adequacy ratios worsened. An increase in capital requirements, to be completed by 2020, is expected to reverse this. By contrast, liquidity ratios strengthened over this period, reflecting a more prudent attitude by banks.

11. **Direct credit risk to the mining sector appears limited.** Mining companies operating in the DRC are mostly foreign-owned and have limited borrowing from banks operating in the DRC. Loans from extractive industries represented only 8 percent of total loans as of January 2019, likely from the artisanal mining sector. Credit growth is correlated to the non-mining sector as most of the loans are concentrated in the trade sector, however, it seems that there is a strong correlation between the increase in NPLs and the fall in copper prices (Figure 2), which suggest a strong spillover of the mining industry to the rest of the economy and the banking system.



12. **Monetary policy has limited impact on the banking system as transmission channels are weak.** The share of transactions in local currency in the banking system is limited. Efforts to reduce dollarization stopped during the crisis and the authorities even asked mining companies to pay their taxes in foreign currency. The banks have ample liquidity in both local and foreign currency. The BCC has tried to mop up excess liquidity without much success. The increases in the policy rate and in the mandatory reserve requirement ratios had limited results. Issuance of BCC bonds would be a more effective instrument of monetary policy. However, the BCC is undercapitalized, which weakens its operational position and its ability to conduct an effective monetary policy.

13. **Financial inclusion is weak with a penetration rate of 6 percent, against the (already limited) SSA average of around 25 percent.** The DRC made considerable progress in account ownership, from less than 4 percent to a quarter of the population between 2011 and 2017. However, the country still lags its peers with 40 percent less account ownership than the average for the SSA region (Text Table 2). The difference in account ownership between men and women has been largely eliminated, and the country is performing better than the rest of the region in reducing that gender gap. Increasing financial inclusion would help increase the effectiveness of monetary policy.

Text Table 2. Account ownership at a financial institution or with a mobile-money-service provider

| | 2011 | | 2014 | | 2017 | |
|-----------------------------------|------|------|------|------|------|-----|
| | | | | | DRC | SSA |
| Percentage of population ages 15+ | 3.7 | 17.5 | 25.8 | 42.6 | | |
| Secondary education or more | 6.0 | 23.4 | 29.9 | 60.3 | | |
| Primary education or less | 1.0 | 7.7 | 17.8 | 30.7 | | |
| Male | 4.7 | 20.7 | 27.4 | 48.4 | | |
| Female | 2.8 | 14.3 | 24.2 | 36.9 | | |
| Richest 60% | 5.4 | 21.9 | 31.4 | 49.7 | | |
| Poorest 40% | 1.1 | 10.8 | 17.4 | 31.9 | | |

Source: The World Bank

14. **The microfinance sector could play a major role in supporting inclusive growth and reduce poverty.** It has been growing rapidly but remains underdeveloped, with US\$262 million in

assets in 2018 compared to US\$230 million in 2013. The sector is composed of 20 MFIs and 78 cooperatives and is concentrated in three provinces (North and South Kivu and Kinshasa). It operates under BCC regulation. The sector is largely focused on savings and loan services, with deposits and loans representing respectively US\$217 and US\$127 million in 2018 (compared to deposits of US\$162 million and loans of US\$118 million in 2013). The sector is highly concentrated (and unprofitable) with the three leading institutions that specialize in loans to micro, small, and medium enterprises accounting for 44.2 percent of the microfinance sector.

C. Conclusions and Policy Recommendations

15. **Financial stability depends on the country's ability to build buffers against external shocks and on an appropriate regulatory framework.** This would require a combination of appropriate policies.

- a. *Fiscal policy.* The DRC needs to strengthen its fiscal position and create fiscal space by increasing its low revenue mobilization levels. The new Mining Code should help to that effect, but efforts should also be accompanied by reforms in PFM. The government should also develop financing tools, such as bonds issuance in the domestic market to avoid having to access BCC credit.
- b. *Monetary policy.* The BCC needs to be recapitalized and rationalized to restore confidence in the local currency and ensure its operational effectiveness.
- c. *Financial sector.* The new Banking Law should be approved promptly to provide the BCC with the needed toolkit to supervise and resolve banks with problems. The authorities should continue to strengthen the preventive supervisory function and introduce a general framework for crisis prevention and management.

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