



# WEST AFRICAN ECONOMIC AND MONETARY UNION (WAEMU)

## Staff Report on Common Policies for Member Countries

April 2013

This staff report on discussions with regional institutions of the West African Economic and Monetary Union (WAEMU) was prepared by a staff team of the International Monetary Fund in the context of the periodic regional surveillance of the WAEMU. The regional perspective of such discussions is intended to strengthen the bilateral discussions that the IMF holds with the members in the region under Article IV of the IMF's Articles of Agreement. The following documents have been released and are included in the package:

- **Staff Report** on Common Policies for Member Countries, prepared by a staff team of the IMF, following discussions with regional institutions that ended on January 25, 2013. Based on information available at the time of these discussions, the staff report was completed on March 8, 2013. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- **Supplement on Financial Depth and Macro-Stability**
- **Public Information Notice (PIN)** summarizing the views of the Executive Board as expressed during its March 25, 2013 discussion of the staff report.
- **Executive Director's Statement**

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# WEST AFRICAN ECONOMIC AND MONETARY UNION (WAEMU)

## STAFF REPORT ON COMMON POLICIES FOR MEMBER COUNTRIES

March 8, 2013

### KEY ISSUES

**Context.** The region faced new political and security challenges in 2012. Military coups occurred in Guinea-Bissau and Mali, and the northern part of Mali was taken over by terrorist groups. However, area-wide growth is estimated to have exceeded 5.5 percent in 2012, driven by the post-crisis recovery in Côte d'Ivoire and a rebound in agriculture, and is expected to remain robust in 2013. Inflation would remain moderate. The consultation focused on the appropriate mix of macroeconomic policies, including in response to the risks to the regional outlook; improving the effectiveness of policies and the stability of the Union through better coordination, financial deepening and stability; and accelerating growth through deeper integration.

#### Key policy recommendations:

- **Policy mix.** Fiscal consolidation is warranted in countries with higher deficits, in light of the projected high growth and the need to reconstitute policy buffers. The modest easing of monetary policy has been appropriate, taking into account the benign outlook for inflation. Official reserves remain adequate.
- **Fiscal policy coordination.** More coordination is needed to safeguard the stability of the Union. Convergence criteria on public debt and the fiscal deficit need to be reconsidered and implementation of the framework needs to be strengthened to improve adherence and traction.
- **Financial sector.** Further development and strengthening are desirable to boost investment and growth. Completing reforms of the interbank and government debt markets is a priority. Bank supervision and regulation, and crisis prevention and resolution frameworks need to be strengthened.
- **Growth.** Reinvigorating the regional integration agenda would strengthen competitiveness, raise potential growth, and boost employment.

Approved By  
**Roger Nord and Peter Allum**

Discussions were held January 14-25, 2013 with the regional central bank (Banque Centrale des Etats d’Afrique de l’Ouest, BCEAO), the Banking Commission, and the WAEMU Commission. Discussions with the West African Development Bank were conducted by the resident representative in Togo. The staff team comprised Mr. Joly (head), Messrs. Kireyev and Hitaj, Mesdames Kolerus and Zdzienicka (all AFR), Mr. Imam (MCM), and Mr. Bernard (AFRITAC West). The mission was assisted by Ms. Fichera and Messrs. Camard, Keller, and Le Hen (resident representatives). Mr. Nord joined the team in Dakar. Mr. Allé (OED) and World Bank staff participated in the discussions. Other contributors include Edison Narvaez, Doug Shapiro and Monica Snyder (all AFR).

WAEMU countries are Benin, Burkina Faso, Côte d’Ivoire, Guinea Bissau, Mali, Niger, Senegal, and Togo.

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## INTRODUCTION

**1. The WAEMU faced new political and security challenges in 2012.** Military coups occurred in Guinea-Bissau and Mali and caused economic disruption in these countries. The northern part of Mali was taken over by terrorist groups, which led to large refugee flows to neighboring countries and triggered a military intervention to restore territorial integrity. On the upside, the sociopolitical situation in Côte d'Ivoire improved significantly, and a peaceful and democratic changeover took place in Senegal.

**2. Regional policies last year have been broadly in line with the 2012 consultation's recommendations, although reform implementation has been somewhat slower than expected.** This is the case in the financial sector (e.g., the launch of key reforms to deepen the interbank market has been delayed to 2013) and in the area of regional integration (reflecting the security situation in Mali). Macroeconomic policies at the country level have also been consistent with Fund advice, generally in the context of Fund-supported programs.

## RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

**3. Regional economic activity rebounded in 2012.** After a large decline in 2011 to about 1 percent because of the drought in the Sahel and the post-electoral crisis in Côte d'Ivoire, regional growth is estimated to have reached 5.8 percent in 2012. Growth was driven mainly by the post-crisis recovery in Côte d'Ivoire, the rebound of agricultural production in a number of countries, and the start of oil production in Niger. A few countries faced inflationary pressures, mainly on domestic prices for food and petroleum products. Nevertheless, average regional inflation remained low, at about 2.5 percent (Figure 1).

**4. The area-wide fiscal deficit stabilized around 4 percent of GDP in 2012, while the overall debt situation improved thanks to debt relief to Côte d'Ivoire** (Figure 2). Compared with 2011, fiscal deficits increased in Burkina Faso, Niger, and Togo, stabilized in Côte d'Ivoire, and decreased in the other countries. With Côte d'Ivoire reaching the HIPC Initiative's completion point in 2012, all WAEMU countries have benefited from substantial relief on their external debt. The average nominal debt for the region now stands at about 40 percent of GDP. All countries have public debt ratios substantially below the 70 percent of GDP ceiling set by the regional surveillance framework; they also have low or moderate ratings for the risk of debt distress according to recent debt sustainability analyses (DSAs), reflecting prudent fiscal policies and sustained growth (Appendix I). Countries have tended to re-accumulate debt in the wake of debt relief, but generally in line with expectations and there has been no indication of a major deterioration of the debt sustainability outlook in the WAEMU. However, the composition of financing has changed, with increasing reliance on domestic debt with higher interest rates and shorter maturities to supplement concessional external financing, which raises new debt management challenges. This trend is likely to continue as aid prospects are not favorable.

**Figure 1. Recent Economic Developments 2007–2012<sup>1</sup>**

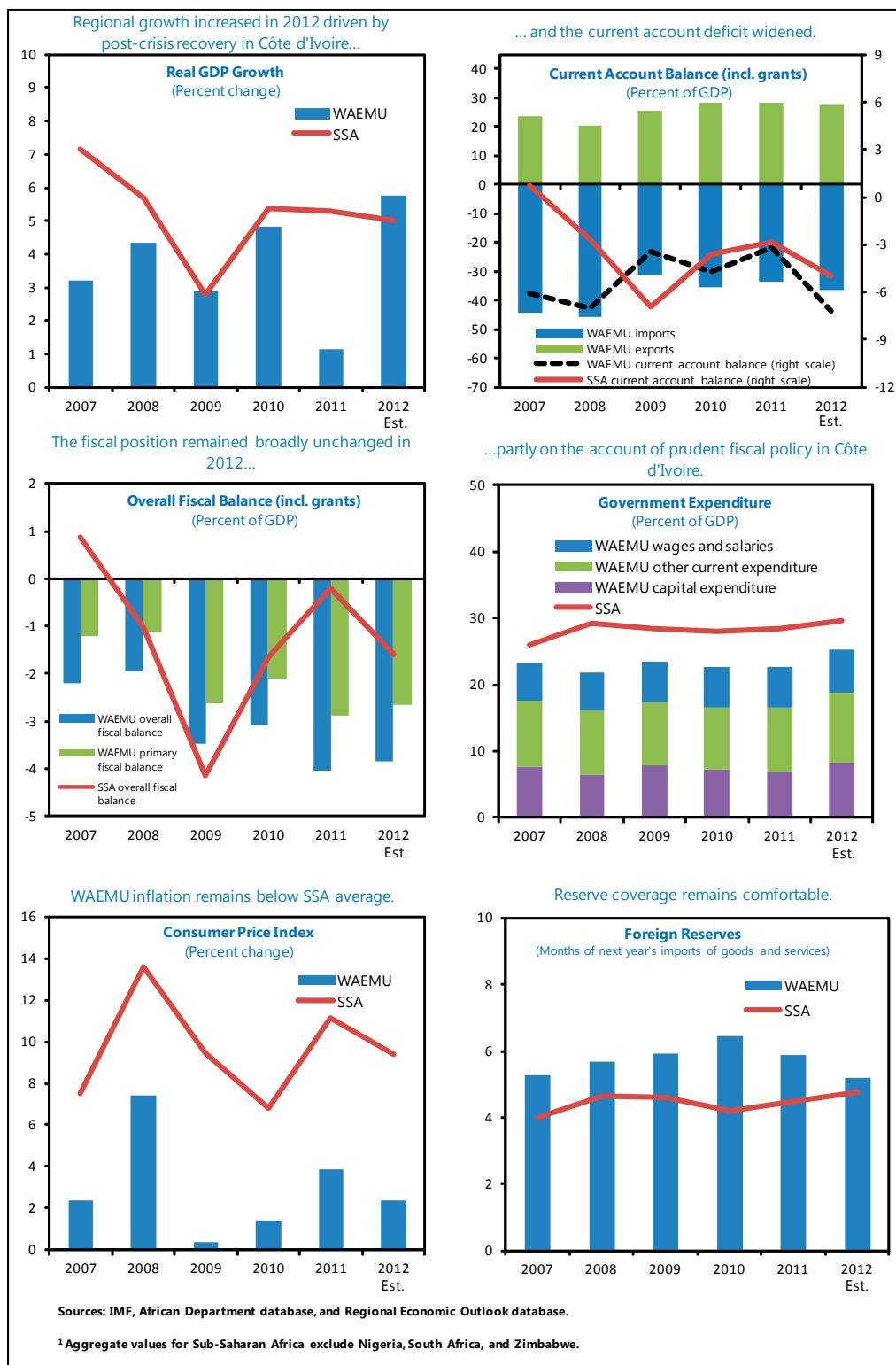
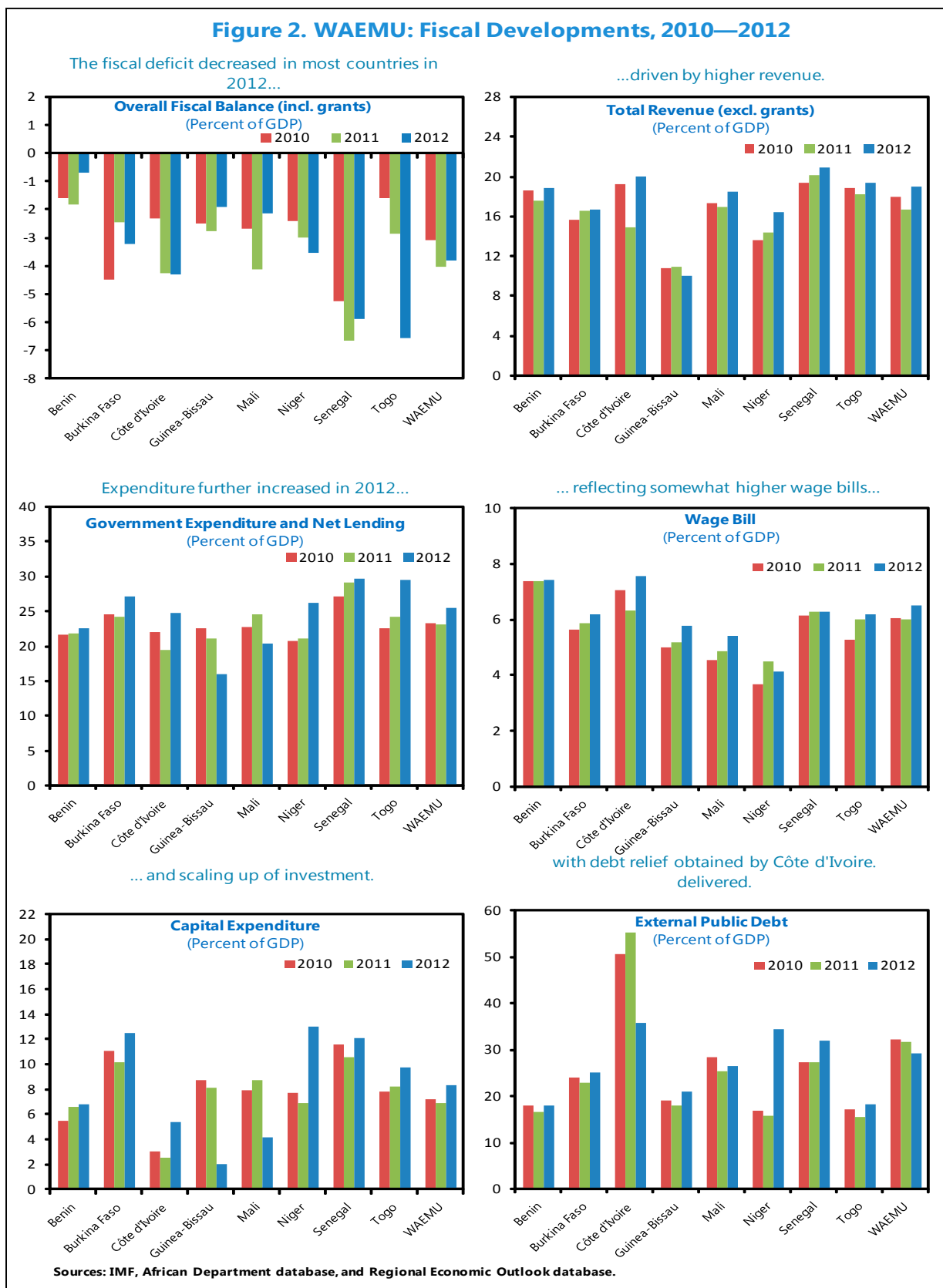


Figure 2. Fiscal Developments, 2010–2012



**5. Monetary policy was eased modestly in 2012.** Despite relatively strong growth of credit to the private sector and government, money growth remained moderate in 2012 (at about 8 percent year on year) because of a significant contraction in net foreign assets (NFA). In a context of continued moderate inflation and a sharp contraction in autonomous factors of bank liquidity (related, to a large extent, to the evolution of NFA) leading to pressures on interest rates, the BCEAO injected substantial amounts of liquidity to banks which has stabilized excess reserves. It also cut the policy rates by 25 basis points to respectively 3 and 4 percent and lowered the reserve requirement ratio to from 7 to 5 percent (Figure 3).

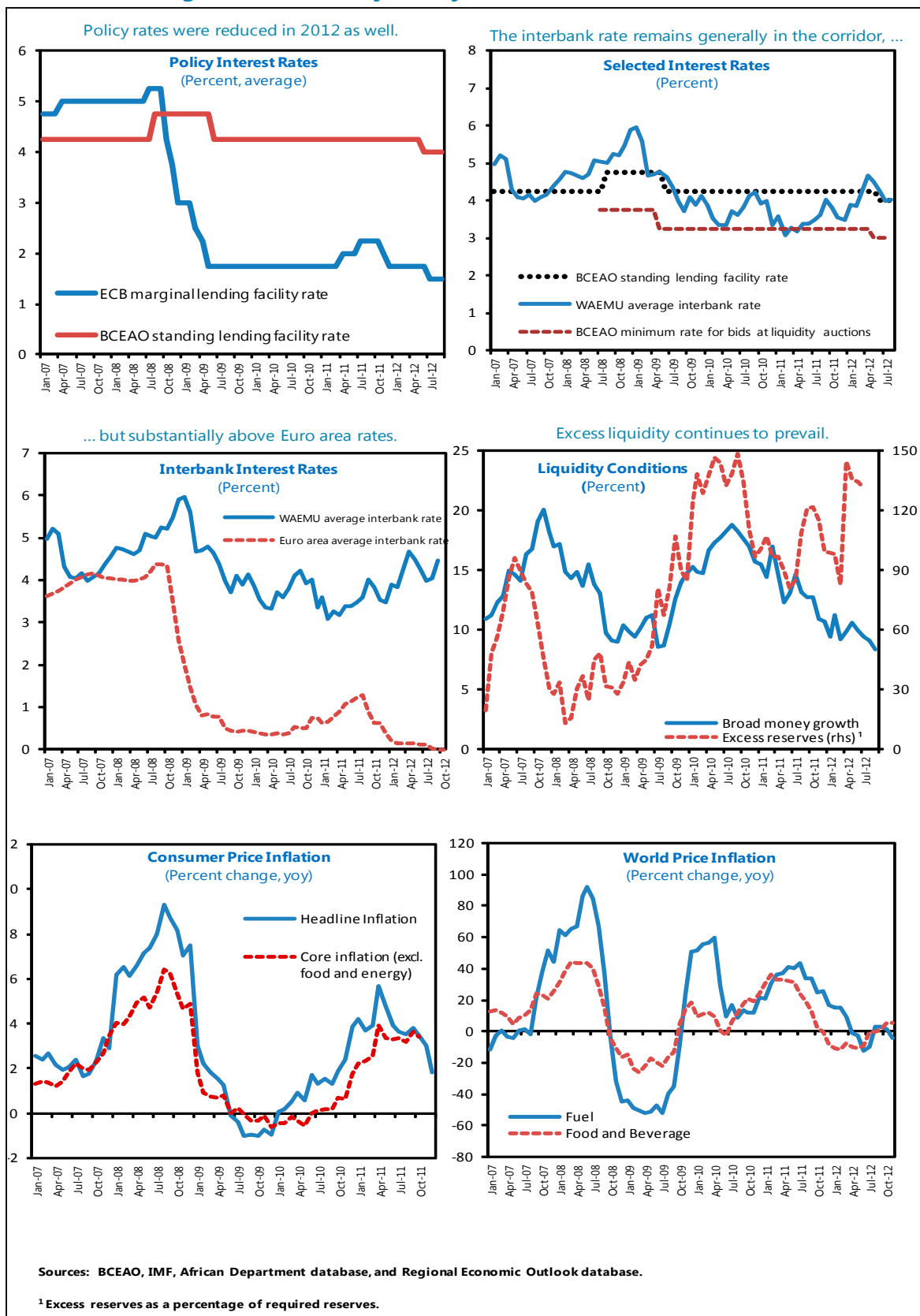
**6. The region's current account deficit widened significantly in 2012.** This outcome reflects a number of exceptional factors, such as higher imports of intermediate and capital goods by Côte d'Ivoire related to reconstruction efforts, Burkina Faso and Niger for mining and hydrocarbon projects, higher food imports to make up for the impact of the 2011 drought, and unfavorable terms of trade. The higher current account deficit, combined with temporary delays in repatriating export proceeds (mostly by Côte d'Ivoire), led to a deficit in the overall balance of payments and a decline of official reserves. Nevertheless, at about 5 months of regional imports and 98 percent of short-term domestic liabilities, reserves remain adequate. Updated staff estimates indicate that the level of the real effective exchange rate is broadly in line with the region's fundamentals (Appendix II).

**7. Growth is expected to remain robust in 2013 and the medium term, at about 6 percent** (Figure 4). It will be driven this year by a large increase in public investment and crowding in of private investment in post-crisis Côte d'Ivoire, continued mining and hydrocarbon sector investment in Burkina Faso and Niger, infrastructure investment in Senegal, and a further recovery in agriculture. Growth would remain high in the medium term under the assumption of full implementation of growth-enhancing policies, including policies aimed at closing the region's infrastructure gaps. Inflation would remain below 3 percent. The current account deficit is projected to remain large in 2013, but would gradually decline in the medium term as Côte d'Ivoire's reconstruction needs subside.

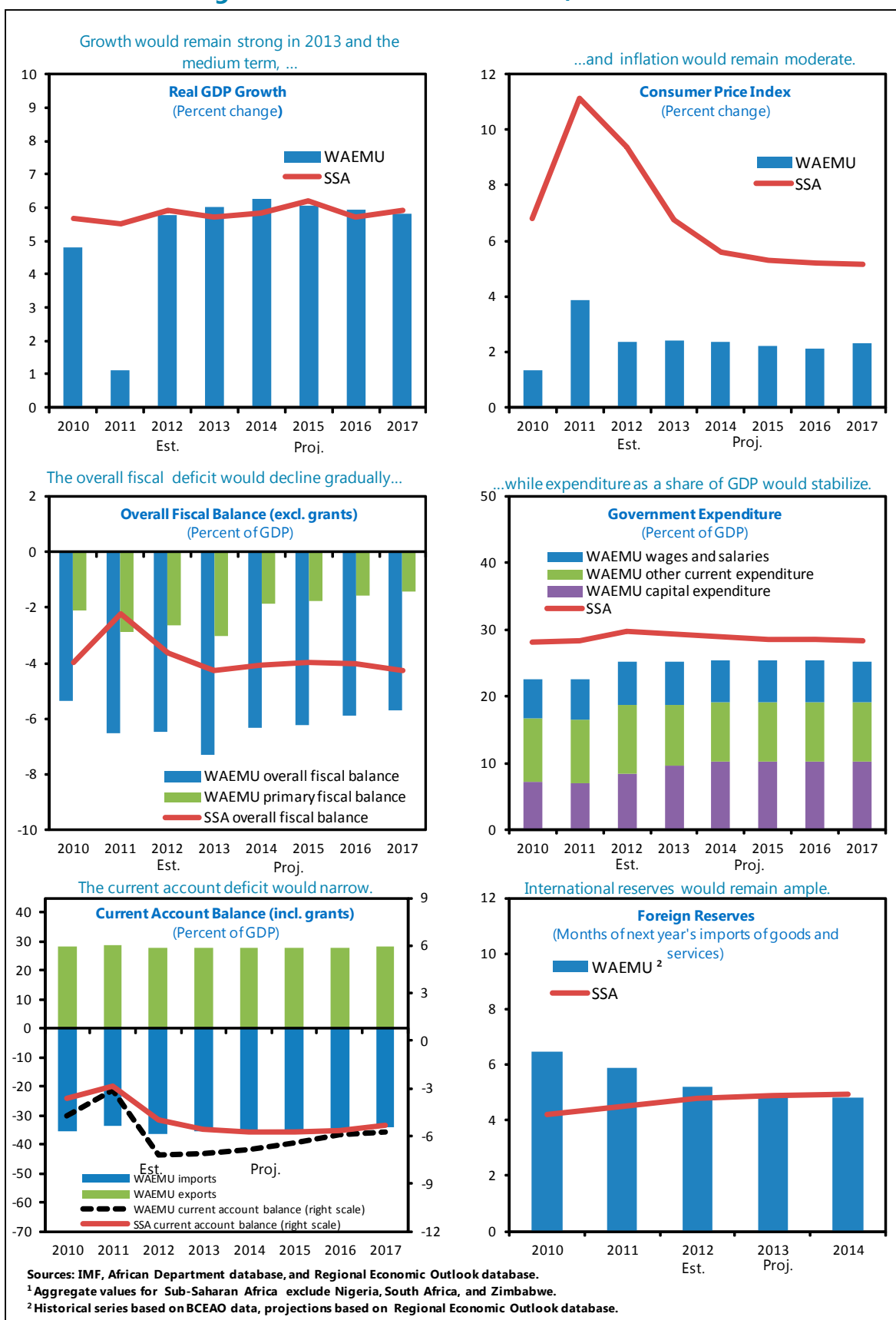
**8. The outlook is subject to a number of downside risks** (Risk Assessment Matrix). The economic impact on other countries of the crises in Mali and Guinea-Bissau has been moderate so far because of limited interconnectedness in the region (Appendix III). While the situation in Mali is evolving towards restoration of territorial integrity, the region may face broader political stability and security issues if terrorist activity were to spread and the perception of insecurity extended to neighboring countries, with a negative impact on public finances, risk perception by investors, and ultimately growth. Another downside risk is whether public policies needed to reach the projected growth rates, which are high by historical standards, will be fully implemented. Failure in this area would reduce significantly growth prospects with implications for poverty reduction and fiscal sustainability as suggested by recent DSAs (see Figure 5). The main risks related to the international environment include a possible intensification of the euro area crisis, which could affect exports, remittances, foreign direct investment, and official assistance. WAEMU countries also remain vulnerable to negative shocks to international food and fuel prices.



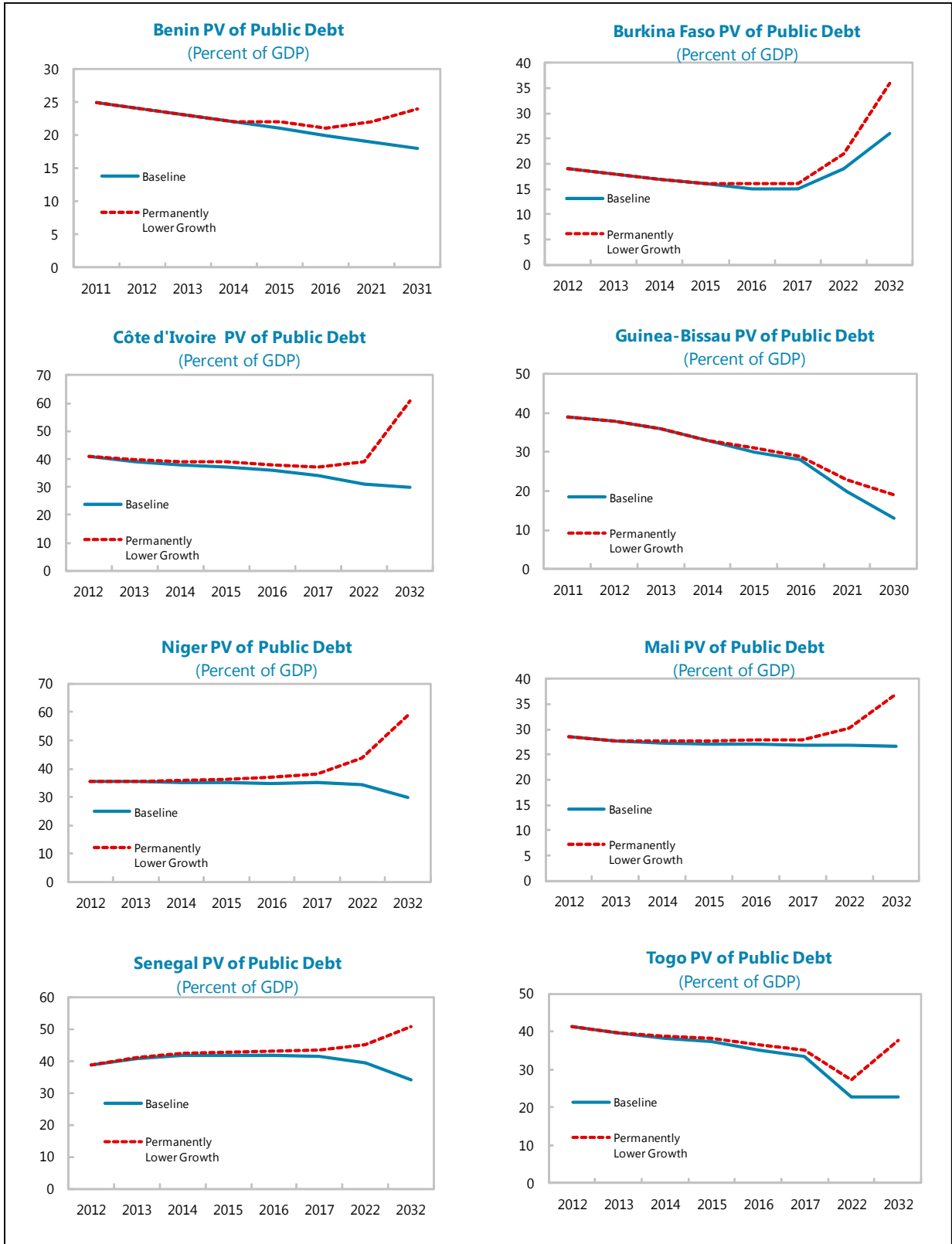
**Figure 3. Monetary Policy and Inflation, 2007–2012**



**Figure 4. Medium Term Outlook, 2010–2017<sup>1</sup>**



**Figure 5. Sensitivity of Public Debt to Lower Growth**



## WAEMU: Risk Assessment Matrix

| Source of risks  | Overall level of concern   |  |
|--|--|--|
|  | Relative likelihood  | Impact if realized   |
| <b>Short-term risks</b>  |  |  |
| <b>Global risks:</b><br><b>(i) stalled or incomplete delivery of Euro area policy commitments</b><br><b>(ii) deeper than expected slowdown in emerging economies (EMs)</b> | <b>Medium for EA/medium for EMs</b> <ul style="list-style-type: none"> <li>• WAEMU is exposed to the euro area through trade, worker remittances, foreign direct investment, and aid.</li> <li>• WAEMU is also increasingly exposed to China, India and other emerging countries.</li> </ul>   | <b>Medium</b> <ul style="list-style-type: none"> <li>• A 1 percentage point decline in growth in EA may translate into a 0.5 percent decline in the WAEMU growth rate. Impact could be larger if EMs slow down significantly too.</li> <li>• Social programs and infrastructure investment may be affected by reduced aid. Large projects financed by emerging creditors may be delayed.</li> </ul> <b>Policy recommendation</b> <ul style="list-style-type: none"> <li>• If shock is temporary, let automatic stabilizers play where financing is available; monetary policy could also be loosened.</li> </ul> |
| <b>Global risk</b><br><b>Oil price shock</b>   | <b>Low</b> <ul style="list-style-type: none"> <li>• Poor harvest in North America and Australia has produced an increase in prices for imported food.</li> <li>• Geopolitical risks in the Middle East can lead to an increase in oil prices.</li> </ul>   | <b>Medium</b> <ul style="list-style-type: none"> <li>• Support may be needed from the authorities, impacting the budgets of WAEMU countries.</li> </ul> <b>Policy recommendation</b> <ul style="list-style-type: none"> <li>• Domestic prices should reflect changes in international prices. Assist most vulnerable people through targeted transfers.</li> </ul>   |
| <b>Regional risk:</b><br><b>Spillovers from continued instability in the region</b>  | <b>Medium</b> <ul style="list-style-type: none"> <li>• Terrorism in Northern Mali (which might spread) could affect the perception of insecurity in the region</li> <li>• Higher risk perception by investors</li> </ul>   | <b>Medium</b> <ul style="list-style-type: none"> <li>• Negative impact on investment and growth.</li> <li>• Additional security-related expenditure may affect fiscal consolidation efforts.</li> </ul> <b>Policy recommendation</b> <ul style="list-style-type: none"> <li>• Security-related expenditure may need to be accommodated and financed through savings on non-priority expenditure.</li> </ul>  |
| <b>Regional risk:</b><br><b>Food price shock</b>   | <b>Low</b><br>Periodic droughts in the Sahel region may affect prices for locally produced food.   | <b>Medium</b> <ul style="list-style-type: none"> <li>• Food insecurity for vulnerable people, increased need for international humanitarian assistance. Support may be needed from the authorities, impacting the budgets of WAEMU countries.</li> </ul> <b>Policy recommendation</b> <ul style="list-style-type: none"> <li>• Domestic prices should reflect changes in international prices. Assist most vulnerable people through targeted transfers.</li> </ul>  |
| <b>Medium-term risks</b>   |  |  |
| <b>Domestic risk:</b><br><b>Delays in key growth-enhancing reforms (e.g., higher public investment, higher public spending efficiency)</b>                                 | <b>Medium</b> <ul style="list-style-type: none"> <li>• Absence of public expenditure reform and financing constraints could affect key public investments, and more generally the efficiency of government spending.</li> <li>• Insufficient progress in financial deepening, non-price competitiveness, and quality of institutions and governance could constrain growth.</li> </ul> | <b>Medium</b> <ul style="list-style-type: none"> <li>• Insufficient fiscal consolidation could affect medium-term sustainability.</li> <li>• Growth remains slow and poverty reduction is curbed. Lower growth would further affect fiscal sustainability.</li> </ul> <b>Policy recommendation</b> <ul style="list-style-type: none"> <li>• Keep reform momentum and avoid policy slippages.</li> </ul>  |

## IMPROVING EFFECTIVENESS OF POLICIES THROUGH BETTER COORDINATION

### A. Macroeconomic Policy Mix in 2013

**9. Fiscal consolidation is expected in 2013 in countries with higher deficits.** In Burkina Faso, Côte d'Ivoire, Senegal and Togo overall fiscal deficits are projected to decrease, while they would remain broadly stable at relatively low levels in Benin, Guinea Bissau, and Mali. Only Niger would record a large increase in its fiscal deficit, reflecting spending related to a new large project in the hydrocarbon sector. The area-wide deficit would remain broadly unchanged at about 4 percent of GDP in 2013; excluding Niger, it would decrease.

#### Staff's advice

**10. The current macroeconomic policy mix is appropriate, but the authorities should stand ready to respond to possible adverse developments.** The planned fiscal consolidation in the countries with higher deficits is warranted given the projected high growth. In the medium term, these countries should continue reducing their fiscal deficits, which would preserve debt sustainability and reconstitute fiscal space needed for countercyclical policy. This will require additional efforts on revenue mobilization and improving the quality of public spending. The monetary policy stance has been adequate too, taking into account the outlook for inflation, which remains largely determined by non-monetary factors (e.g., exchange rate fluctuations, terms of trade, shocks affecting agricultural production), and the constraints imposed by a shallow financial system. Should downside risks materialize, automatic stabilizers (i.e., higher deficits driven by lower tax receipts) could be left to operate where financing is available, and monetary policy could be loosened. Country debt management should be strengthened to address risks arising from higher recourse to market financing. More coordination in this area would reduce rollover risk.

**11. The effectiveness of monetary policy can be improved through a range of measures.** The BCEAO should continue strengthening inflation and liquidity forecasting. Further analysis of the monetary policy transmission channels is also desirable, as is better coordination with governments, which will facilitate liquidity management. Improving the quality, availability, and timeliness of macroeconomic and financial information would also facilitate the conduct of monetary policy. However, in the absence of more developed financial markets, the transmission of monetary policy signals remains weak. Only the bank lending channel is relatively active, while the interest rate and the asset price channels remain constrained by the shallowness of the financial system. The development of the interbank and the government debt markets therefore remains critical for strengthening the effectiveness of monetary policy. More developed financial markets would also allow banks to trade liquidity more actively, limiting the need for liquidity injections by the BCEAO and allowing for the emergence of an interbank rate that would provide highly valuable information for the conduct of monetary policy.

## Authorities' views

**12. The authorities broadly agreed with the assessment of the policy mix.** They stressed that member countries were facing large public investment requirements to reduce infrastructure gaps and improve the provision of social services. Addressing these needs, while preserving fiscal sustainability, would require expenditure rationalization. Monetary policy's best contribution to a growth-friendly environment would be to ensure macroeconomic stability.

**13. The BCEAO was confident that major reforms to deepen the interbank market would be launched by mid-2013.** These reforms include the introduction of collateralized operations (repos) to address the reluctance of liquid banks to lend to illiquid ones; the rollout of an electronic platform to auction and trade liquidity and government paper ("application Trésor"); and the introduction of primary dealers, which should accelerate the development of the secondary government debt market. The BCEAO also stressed that the imminent establishment of a regional debt agency, with the main mission to advise treasuries, improve issuance coordination, and contribute to the development of the government debt market, would facilitate liquidity management.

## B. Responding to Shocks While Preserving Sustainability

**14. Observance of the key fiscal convergence criterion remains limited, suggesting a need to reconsider the regional surveillance framework.** The criterion on the basic fiscal balance was missed by 5 of the 8 countries in 2012, and is likely to be missed again in 2013 by the largest two economies (Côte d'Ivoire and Senegal). This criterion has rarely been met by a majority of member countries, raising the question of its relevance and credibility. Following debt relief, the debt criterion is now met by all countries (Text Table 1).

**Text Table 1. WAEMU: Number of Countries Not Observing Convergence Criteria, 2009–2012**

|  | 2009 | 2010 | 2011 | 2012<br>Est. |
|--|------|------|------|--------------|
| <b>First-order criteria</b>  |      |      |      |              |
| Basic fiscal balance/GDP ( $\geq 0$ percent) <sup>1</sup>  | 6    | 3    | 6    | 5            |
| Average consumer price inflation ( $\leq 3$ percent)   | 0    | 1    | 5    | 4            |
| Total debt/GDP ( $\leq 70$ percent)  | 2    | 0    | 1    | 0            |
| Change in domestic arrears ( $\leq 0$ )  | 0    | 0    | 0    | 0            |
| Change in external arrears ( $\leq 0$ )  | 2    | 0    | 1    | 1            |
| <b>Second-order criteria</b>   |      |      |      |              |
| Wages and salaries/tax revenue ( $\leq 35$ percent)  | 5    | 4    | 5    | 6            |
| Capital expenditure domestically financed/tax revenue ( $\geq 20$ percent)   | 3    | 4    | 2    | 2            |
| External current account balance, excluding grants/GDP ( $\geq -5$ percent)  | 7    | 6    | 7    | 7            |
| Tax revenue/GDP ( $\geq 17$ percent)   | 7    | 7    | 7    | 5            |
| Sources: WAEMU; Central Bank of West African States (BCEAO); and staff estimates.  |      |      |      |              |
| <sup>1</sup> Total fiscal revenues, excluding grants, minus total expenditures excluding foreign-financed investment expenditure. From 2009, total fiscal revenues plus budget support grants plus counterpart of HIPC/MDRI-related spending for both current and capital spending less current expenditure and capital expenditure financed by own resources. |      |      |      |              |

**15. The frequency and asymmetry of shocks in the region are still high.** Business cycle synchronization within the WAEMU and between the WAEMU and the euro area remains limited (Appendix IV). Nevertheless, WAEMU countries are highly susceptible to various exogenous shocks, many of them asymmetric. Staff analysis suggests that shock absorption—the smoothing of the impact of GDP fluctuations on consumption—has been much more limited than in other monetary areas. The limited scope for, and effectiveness of, monetary policy suggest that fiscal policy has in principle an important role to play in addressing both symmetric and asymmetric shocks.

#### **Staff's advice**

**16. Preserving debt sustainability and the stability of the Union in the medium term will require better coordination of fiscal policies.** The experience of the euro area has shown that fiscal discipline in each member of a monetary union is critical for the stability of the union. At the same time, this discipline could be weakened by externalities, such as a non-credible no-bailout commitment. Staff analysis suggests that market discipline is limited in the WAEMU, and while it may improve with the development of the market, is likely to remain insufficient in the next few years (Appendix V). A strengthening of the regional surveillance framework is therefore desirable. Any new or modified rules should be relevant to the overarching objective—preserving the stability of the Union. They should be also easy to interpret, implement, and monitor, given administrative and technical capacity limitations.

**17. Both the design of the main convergence criteria and their enforcement could be reconsidered.** The criterion on nominal public debt could be lowered to reduce the risk of debt distress. Based on recent empirical research by the IMF and the World Bank, a threshold closer to 50 percent of GDP applied to a comprehensive definition of public debt would seem more appropriate. This threshold should be seen as a ceiling, not as an optimal debt level. A criterion on the overall fiscal deficit would allow better control of debt accumulation than the current basic balance, which excludes foreign-financed capital expenditure.<sup>1</sup> The ceiling for the deficit would need to be consistent with preserving fiscal sustainability, while leaving room for countercyclical policies. It should also take into account that the timing of some expenditures, such as donor-financed projects, is not entirely within the control of the authorities. While a cyclically-adjusted balance has been introduced in the euro area surveillance framework, its use in the WAEMU seems premature given data limitations and difficulties in identifying clearly cycles. However, even better designed rules may not lead to expected outcomes if they are not properly implemented. A first step should be a strengthening of the monitoring, and increased transparency and dissemination of regional and national fiscal outcomes.

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<sup>1</sup> The basic fiscal balance could continue to be monitored for analytical purposes.

## Authorities' views

**18. The WAEMU Commission agreed that a comprehensive review of the regional surveillance framework was needed.** Convergence is unlikely to be achieved by the (several times postponed) deadline of end-2013. The Commission will shortly launch a comprehensive study on the surveillance framework and desirable reforms, which is expected to be ready before end-2013. It expressed interest in continuing the close dialogue with staff on these issues.

## C. Other Areas for Policy Coordination

**19. Transposition of the WAEMU directives on national public financial management is lagging.** The directives harmonize the rules for the preparation, submission, approval, execution, budget control, and encourage efficient and transparent management of public finances in all countries of the Union. To date, only Senegal has completed the transposition of all directives. Staff and the regional authorities agreed that national authorities should complete transposition as soon as possible and start working on implementation.

**20. Further coordination of tax policies is desirable to increase revenue and reduce tax competition.** Staff and the WAEMU Commission saw scope for further coordination in the following areas: the introduction of a unified methodology for the assessment of tax expenditure; a strengthening of the surveillance of countries' compliance with WAEMU directives; implementation of the VAT (to better ensure neutrality) and corporate income tax; tax incentives for investment; mining taxation; the transition to a tax system less dependent on customs duties; and the implications for tax harmonization efforts of extending the common external tariff to ECOWAS. The WAEMU Commission will benefit from IMF TA in some of these areas. Work on taxation and pricing of petroleum products should also be pursued in a coordinated manner at the regional level.

**21. Information quality and availability need to improve.** Efforts at all levels to improve data quality, coverage, and timeliness should continue. The data should be widely shared at the national and regional levels between the authorities and with the public. This is critical for the design and effective implementation of national and regional policies, and more generally for the efficient functioning of markets. Staff welcomes the recent strengthening of the mechanism to monitor annually implementation of regional policies at the national level and encourages publication of its results.



## DEEPENING AND STRENGTHENING THE FINANCIAL SECTOR

**22. The financial system in the WAEMU remains largely bank-based.**<sup>2</sup> The regional interbank, debt, and equity markets are underdeveloped, with the exception of the market for government debt, which has expanded fast recently. Microfinance has developed quickly too in some countries and helped improve financial inclusion, but the sector remains small compared to banking. On average, the banking system is liquid and well capitalized, although the situation varies substantially across banks and countries (Figure 6). Lending concentration is high in all countries of the region, and quality of assets, as reflected in high gross NPLs, represent the main risk. The exposure of banks to WAEMU sovereigns has increased rapidly, with the development of the regional market; their broader exposure to the public sectors is also substantial. Compliance with prudential norms remains low for a number of ratios, and some of these norms are not in line with international standards. The interconnection between the various segments of the financial system is low but increasing.

**23. Financial depth has increased in recent years but remains low.** A benchmarking exercise conducted on the countries of the region suggests that the limited depth of the banking system reflects these countries' structural characteristics, while financial markets look particularly underdeveloped from this perspective (Figure 7). Further development of the financial sector would facilitate the financing of growth, improve financial inclusion and the ability of firms and households to cope with a volatile environment, and increase the effectiveness of macroeconomic policies (Box 1).

### Staff's advice

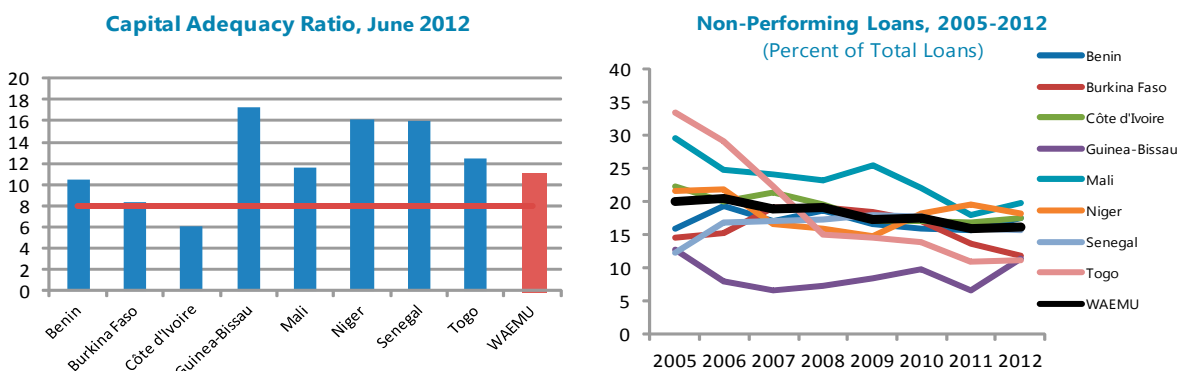
**24. Further development of the financial sector requires resolute action on several fronts.** As pilot studies on Benin and Senegal have shown, obstacles to financial development include insufficient transparency and informational asymmetries, weak business environment and legal and judicial frameworks, unfavorable taxation regimes for financial operations, regulatory and supervision issues (including issues related to the division of responsibilities in a monetary union) and lack of financial skills. Staff urged the authorities to complete ongoing reforms to develop the interbank market and deepen the market for government debt (above), but also encouraged them to avoid distortions (e.g., in terms of taxation), which would affect the development of private debt and equity markets. Staff welcomed the authorities' efforts to reduce information asymmetries (e.g., through the planned creation of credit and guarantee bureaus) and to facilitate access to, and lower transaction costs on, the regional stock exchange (e.g., through the introduction of ratings, the reduction of various fees and the planned new market for small and medium sized companies).

<sup>2</sup> An overview of the WAEMU's financial system and issues was produced in the context of the pilot on strengthening financial sector surveillance in LICs. More detailed analysis can be found in Supplement 1. Similar reports were produced for Benin (IMF Country Report No 13/9) and Senegal (IMF Country Report No 12/337).

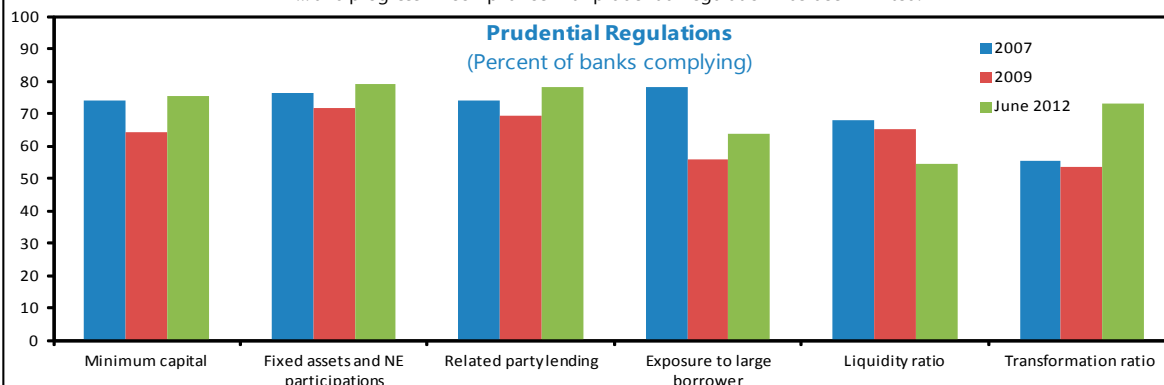
**Figure 6. Financial Soundness**

Although the banking sector appears well capitalized overall, banks in Côte d'Ivoire are significantly undercapitalized on average.

Non performing loans are high albeit trending downwards for some countries...



... and progress in compliance with prudential regulation has been limited.



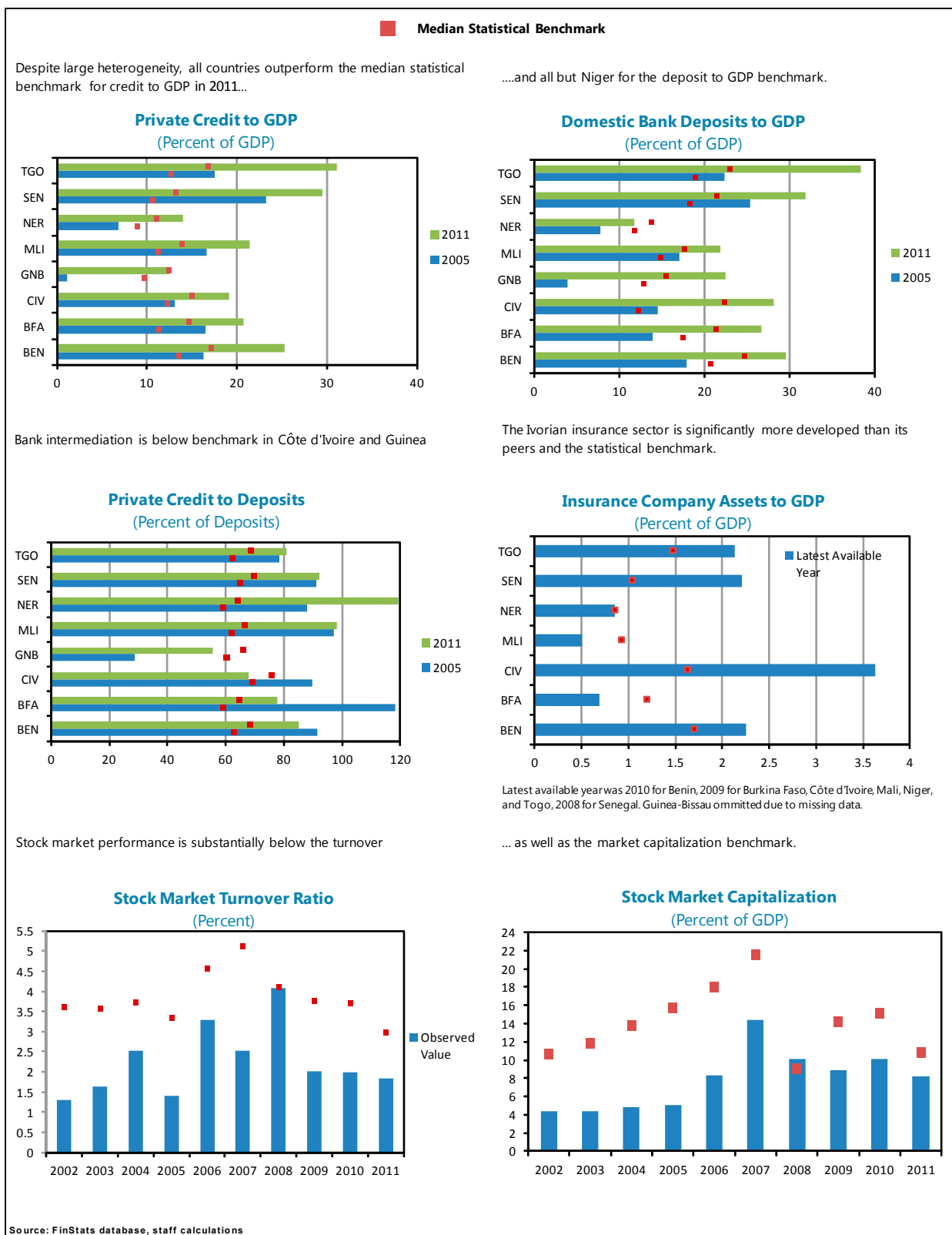
**Respect of Prudential Norms by Country, end-June 2012**

| Number of Banks per country | Solvency Ratios |                                    | Other Prudential Ratios    |                    |                       |                           |                 |
|-----------------------------|-----------------|------------------------------------|----------------------------|--------------------|-----------------------|---------------------------|-----------------|
|                             | Capital ratio   | Fixed assets and NE participations | Exposure to large borrower | Concentration risk | Related Party Lending | Transformation ratio >50% | Liquidity ratio |
| Benin (12)                  | 10              | 9                                  | 5                          | 10                 | 9                     | 5                         | 7               |
| Burkina (12)                | 9               | 10                                 | 6                          | 10                 | 11                    | 10                        | 7               |
| Côte d'Ivoire (23)          | 13              | 16                                 | 12                         | 16                 | 16                    | 11                        | 18              |
| Guinea Bissau (4)           | 3               | 3                                  | 3                          | 3                  | 3                     | 2                         | 1               |
| Mali (13)                   | 12              | 11                                 | 9                          | 12                 | 10                    | 7                         | 5               |
| Niger (10)                  | 7               | 8                                  | 8                          | 8                  | 8                     | 5                         | 3               |
| Senegal (19)                | 16              | 18                                 | 14                         | 18                 | 16                    | 8                         | 10              |
| Togo (12)                   | 9               | 8                                  | 10                         | 9                  | 9                     | 4                         | 6               |
| WAEMU (105)                 | 79              | 86                                 | 65                         | 87                 | 82                    | 52                        | 57              |

Sources: BCEAO, IMF, African Department database, and Regional Economic Outlook database.

Note: The transformation ratio (stable resources/M&L term loans) was lowered from 75 percent to 50 percent early 2013, the data reported for 2012 takes the 50 percent into account.

**Figure 7. Selected Indicators on Financial Sector Depth**



### BOX . FINANCIAL SYSTEM SHALLOWSNESS AND MACROECONOMIC POLICIES

The pilots on strengthened financial sector surveillance showed that the limited development of the financial system is a constraint on the scope for, and effectiveness of, macroeconomic policies.

#### Constraints on fiscal policies.

- *Limited scope for counter-cyclical fiscal policies.* While the regional market has developed substantially, there are limits to the amounts governments can raise on it. This is a significant constraint since fiscal policy is the main instrument to address asymmetric shocks, which are frequent in the region.
- *High liquidity (rollover) risks.* As most public debt is short-term, it needs to be regularly rolled over, which may be challenging in certain circumstances. Senegal faced such difficulties ahead of the 2012 presidential election. This situation also reflects the fact that the investor base—composed mainly of banks—is relatively narrow.
- *High borrowing cost,* because of low liquidity and limited economies of scale. For instance, the yield at issuance for Senegalese bonds with maturities of three to five years was in the 7–9 percent range in the first half of 2012, while average inflation was around 2 percent.
- *Limited scope for investment financing,* as governments cannot easily raise long-term financing.

**Constraints on monetary policy.** In a currency area, monetary policy is generally better suited to address symmetric shocks. Under the fixed exchange rate arrangement, the BCEAO has some scope for active monetary policy in the short-to-medium term, as capital mobility is limited. However, the transmission of monetary policy is hampered by the limited depth of financial markets, which affects the effectiveness of most channels of transmission, and the absence of the exchange rate channel given the fixed exchange rate regime.

- *The bank lending channel* seems the only relatively effective transmission channel. Changes in the BCEAO policy rates do affect credit to the private sector, although the impact is more limited than in countries with more developed financial systems (Appendix IV).
- *The interest rate channel* seems largely ineffective. There is little evidence of a statistically significant impact of policy rates changes or liquidity injections on the short-term T-bill and the interbank market rates. This could reflect the limited development of the interbank market, the absence of a secondary government debt market, and large excess liquidity.
- *The asset price channel* is constrained by the limited development of financial markets.

**25. Development of the financial sector and strengthening of its supervision should go together.** Strengthened bank supervision is needed for earlier identification of risks and increased compliance with prudential norms. The emergence of regional banking groups requires the development of supervision on a consolidated basis and strengthening of cooperation with banking supervisors in countries where these groups operate. The increasing exposure of banks to sovereigns is also a risk which needs to be recognized, including through a non-zero weight on government paper in capital adequacy calculations. Micro-prudential regulation should be revised to bring certain prudential standards closer to international best practice, for example on risk concentration, classification of claims and provisioning, while taking into account the regional context.

**26. The financial crisis prevention and management framework could also be strengthened.** Crisis prevention requires greater transparency, including through the regular and timely compilation and publication of financial soundness indicators for all member countries. Regular stress tests would be a welcome step toward the introduction of an early warning system. Staff sees scope for improving the bank resolution framework, which would reduce the budgetary cost of government intervention. Staff underscored the importance of swift action in this area, including by giving broader powers to the supervisor and close collaboration with other supervisors in the case of cross-border groups.

#### **Authorities' views**

**27. The authorities concurred with the need to develop further the financial sector and shared the analysis on the main obstacles.** Improving the financing of the economies and financial inclusion are seen as priorities. Financial sector development will also help absorb the impact of shocks, including by making monetary policy more effective. A comprehensive action plan to develop the financial system was devised and endorsed by heads of state in 2012 and is now being implemented; it involves the national and regional authorities. The WAEMU authorities are also exploring with the CEMAC's options to increase financial integration between the two unions.

**28. Work is ongoing, or will be launched shortly, to address the stability issues raised by staff.** The resources of the Banking Commission have been significantly increased, and staff is being trained on a number of issues (risk-based supervision, bank resolution), including through Fund TA. With regards to prudential rules, the BCEAO reported that the transformation ratio linking long-term assets to long-term resources, which had long been seen as constraining excessively the provision of medium- and long-term credit, was loosened in December 2012. At the same time the ratio on portfolio structure (requiring a certain proportion of rated assets on bank balance sheets) was discontinued. The BCEAO reiterated its intention to move to Basel II in the next few years and expressed interest in Fund TA in this area. The authorities are also developing their macro-prudential analysis, with ongoing work on early warning indicators and a map of risks in the whole financial system. They welcomed the stress-testing exercise conducted jointly with staff and intend to develop their expertise in this area. Work is also well advanced on a deposit insurance scheme

and a financial stability fund, whose main goal would be to avoid possible debt payment incidents by sovereigns facing liquidity problems.

## INCREASING GROWTH AND COMPETITIVENESS THROUGH REGIONAL INTEGRATION

**29. Regional integration remains limited.** There are significant impediments to good labor and capital mobility. Nontariff barriers and inadequate transportation and energy infrastructure remain obstacles to reaping the full benefits of the common market. A recent study commissioned and endorsed by franc zone finance ministers suggested that the growth gains from further integration could be substantial.<sup>3</sup>

**30. Nonprice competitiveness problems continue to affect growth in WAEMU countries, which has been sub-par.** The 2010-13 Doing Business Reports show a deterioration in the average WAEMU rankings, most of which are in the lowest quartile of the distribution (Text Table 2). In addition to developing the financial sector, improving institutions, governance, infrastructure, and trade integration could contribute to increasing competitiveness and raising the region's growth potential. Stronger and sustainable growth, including in agriculture, and greater attention to inclusiveness in the design of growth strategies and policies will allow faster reduction of poverty incidence, which remains high in the region.

**Text Table 2. WAEMU: Doing Business Indicators**

|                 | 2010*      | 2011*      | 2012*      | 2013       | 2010/11 | 2011/12 | 2012/13 |
|-----------------|------------|------------|------------|------------|---------|---------|---------|
| Benin           | 172        | 173        | 176        | 175        | -1      | -3      | 1       |
| Burkina Faso    | 154        | 151        | 149        | 153        | 3       | 2       | -4      |
| Cote d'Ivoire   | 168        | 170        | 177        | 177        | -2      | -7      | 0       |
| Guinea-Bissau   | 175        | 181        | 178        | 179        | -6      | 3       | -1      |
| Mali            | 155        | 148        | 145        | 151        | 7       | 3       | -6      |
| Niger           | 171        | 172        | 175        | 176        | -1      | -3      | -1      |
| Senegal         | 151        | 157        | 162        | 166        | -6      | -5      | -4      |
| Togo            | 162        | 158        | 161        | 156        | 4       | -3      | 5       |
| <b>Average</b>  | <b>164</b> | <b>164</b> | <b>165</b> | <b>167</b> | 0       | -1      | -2      |
| <i>Total of</i> | 183        | 183        | 183        | 185        |         |         |         |

\* Adjusted for data corrections and comparability.

Source: World Bank, Doing Business Indicators, 2010-13.

<sup>3</sup> *Evaluation des gains attendus de l'intégration économique régionale dans les pays africains de la Zone franc*, FERDI, September 2012 ([http://www.ferdi.fr/uploads/sfCmsContent/html/135/Rapport\\_ZF\\_4oct\\_IMP.pdf](http://www.ferdi.fr/uploads/sfCmsContent/html/135/Rapport_ZF_4oct_IMP.pdf))

**Staff's advice**

**31. The integration agenda needs to be reinvigorated.** The regional authorities could build on the momentum generated by the recent franc zone study to develop a plan for coordinated action on removing all barriers to intra-WAEMU trade, implementing fully the common external tariff (CET), coordinating further tax and customs practices, facilitating labor mobility, and developing regional structural policies.

**32. Staff encouraged the authorities to preserve the integrity of the CET and common market.** In the absence of an agreement in the negotiations between ECOWAS and the European Union on an Economic Partnership Agreement (EPA), the interim EPA of Côte d'Ivoire could enter into force in early 2014. This could seriously affect free trade within the WAEMU and the CET. Staff reiterated its concerns regarding the introduction of a new tariff band of 35 percent in the context of the extension of the CET to ECOWAS, potentially covering a large number of products, which would lead to an increase in the overall tariff protection.

**Authorities' views**

**33. The WAEMU Commission was confident that the second phase of the Regional Economic Program would accelerate integration.** It stressed that many lessons were learned from the first phase with regards to the selection and implementation of projects. It indicated that fundraising efforts were stepped up in recent months to ensure full financing of the program. The Commission also reported on its plans to enhance the identification and dissemination in the region of the best-practice business approaches adopted by single countries. On EPA issues, it expressed concern about the risks to free trade within the WAEMU and the CET should an agreement not be found with the European Union.

**STAFF APPRAISAL**

**34. Growth is expected to remain robust in 2013.** It will be driven by continued post-crisis recovery in Côte d'Ivoire, mining and infrastructure investment in a number of countries, and strong output in agriculture. Growth would remain strong in the medium term under the assumption of full implementation of growth-enhancing policies. Inflation would remain moderate.

**35. Risks are on the downside.** While the situation in Mali is evolving fast toward a restoration of territorial integrity, broader political stability and security issues could arise for the region, with a negative impact on public finances, risk perception by investors, and ultimately growth. Another downside risk is whether the policies needed to reach the projected growth rates, which are high by historical standards, will be fully implemented. Failure in this area would reduce significantly growth prospects with implications for poverty reduction and fiscal sustainability.

**36. The macroeconomic policy mix is appropriate.** The planned fiscal consolidation in the countries with higher deficits is warranted in light of the projected high growth and the need to

reconstitute policy buffers. The modest easing of monetary policy in 2012 has been appropriate, taking into account the outlook for inflation. Official reserves remain adequate, even though their recent decline requires close monitoring. Should a temporary downside risk materialize, automatic stabilizers could be left to operate where financing is available, and monetary policy could be further loosened. Debt management needs to be strengthened at the country level and better coordinated.

**37. Preserving debt sustainability and the stability of the Union in the medium term will require better coordination of fiscal policies.** The regional authorities' intention to conduct a comprehensive review of their regional surveillance framework is therefore welcome. Convergence criteria on public debt and the fiscal deficit need to be reconsidered, and implementation of the framework strengthened to increase adherence and traction.

**38. Further development of the financial system is desirable; a strengthening of the regulatory and supervisory framework is necessary to address existing and new risks.** Financial development will help raise growth, mitigate the impact of volatility, increase inclusion and improve the effectiveness of macroeconomic policies. Completing ongoing reforms that will allow the development of the interbank market and secondary government debt market is critical. Although banks on average seem relatively well capitalized and liquid, there is substantial heterogeneity among them, with high lending concentration and uneven asset quality being the main risks. Banks are also increasingly exposed to sovereigns in the region and more generally to the public sector. Finally, the emergence of regional groups raises new risks to address. Observance of prudential rules needs to improve, and some of the rules need to be brought closer to international standards. Staff welcomes the authorities' ongoing efforts to strengthen bank supervision and improve bank regulation. Ongoing work to strengthen the financial crisis prevention and resolution framework is also welcome.

**39. Nonprice competitiveness problems affecting growth require concerted regional and national efforts.** Beyond developing the financial sector, improving institutions, governance, infrastructure, and trade integration are needed. The area-wide real exchange rate appears to be in line with fundamentals.

**40. Transparency and availability of information need to improve.** Efforts at all levels to improve data quality, coverage, and timeliness should continue. The data should be widely shared at the national and regional levels between the authorities and with the public.

**41.** It is proposed that the discussions with the WAEMU authorities remain on the standard 12-month consultation cycle.



**Table 1. WAEMU: Selected Economic and Financial Indicators, 2009—2017**

|   | 2009   | 2010   | 2011   | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   |
|---|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|   |        |        |        | Est.   | Proj.  | Proj.  | Proj.  | Proj.  | Proj.  |
| (Annual percentage change)  |        |        |        |        |        |        |        |        |        |
| National income and prices  |        |        |        |        |        |        |        |        |        |
| GDP at constant prices  | 2.9    | 4.8    | 1.1    | 5.8    | 6.0    | 6.3    | 6.1    | 5.9    | 5.8    |
| GDP per capita at constant prices   | 0.1    | 1.8    | -1.1   | 2.9    | 3.2    | 3.4    | 3.2    | 3.1    | 3.0    |
| Broad money to GDP  | 9.7    | 8.6    | 5.5    | 4.1    | ...    | ...    | ...    | ...    | ...    |
| Consumer prices (average)   | 0.4    | 1.4    | 3.9    | 2.4    | 2.4    | 2.4    | 2.2    | 2.1    | 2.3    |
| Terms of trade  | 4.3    | -4.7   | -0.4   | 1.5    | -0.2   | 0.6    | 0.2    | -0.4   | -0.4   |
| Nominal effective exchange rates  | 0.9    | -4.3   | 1.7    | -2.2   | ...    | ...    | ...    | ...    | ...    |
| Real effective exchange rates   | 0.2    | -6.3   | 0.9    | -2.5   | ...    | ...    | ...    | ...    | ...    |
| (Percent of GDP)  |        |        |        |        |        |        |        |        |        |
| National accounts   |        |        |        |        |        |        |        |        |        |
| Gross domestic savings  | 15.3   | 14.1   | 15.5   | 13.0   | 14.4   | 15.5   | 16.0   | 16.5   | 15.9   |
| Gross domestic investment   | 18.7   | 18.8   | 18.6   | 20.2   | 21.4   | 22.0   | 22.1   | 21.9   | 22.0   |
| <i>Of which:</i> public investment  | 7.1    | 6.4    | 6.3    | 7.8    | 9.1    | 9.6    | 9.7    | 9.6    | 9.5    |
| Resource gap  | -3.4   | -4.7   | -3.1   | -7.2   | -7.0   | -6.5   | -6.2   | -5.5   | -6.1   |
| (Annual changes in percent of beginning-of-period broad money)  |        |        |        |        |        |        |        |        |        |
| Money and credit <sup>1</sup>   |        |        |        |        |        |        |        |        |        |
| Net foreign assets  | 5.8    | 3.1    | 1.0    | -5.5   | ...    | ...    | ...    | ...    | ...    |
| Net domestic assets   | 8.9    | 12.6   | 9.7    | 13.9   | ...    | ...    | ...    | ...    | ...    |
| Broad money   | 14.7   | 15.7   | 10.7   | 8.4    | ...    | ...    | ...    | ...    | ...    |
| (Percent of GDP, unless otherwise indicated)  |        |        |        |        |        |        |        |        |        |
| Government financial operations <sup>2</sup>  |        |        |        |        |        |        |        |        |        |
| Government total revenue, excl. grants  | 17.4   | 17.9   | 16.7   | 19.0   | 19.1   | 19.3   | 19.5   | 19.7   | 19.8   |
| Government expenditure  | 23.9   | 23.3   | 23.2   | 25.5   | 26.5   | 25.7   | 25.7   | 25.6   | 25.5   |
| Overall fiscal balance, excl. grants  | -6.5   | -5.4   | -6.5   | -6.5   | -7.3   | -6.4   | -6.2   | -5.9   | -5.7   |
| Official grants   | 3.0    | 2.3    | 2.5    | 2.7    | 3.1    | 3.4    | 3.3    | 3.2    | 3.0    |
| Overall fiscal balance, incl. grants  | -3.5   | -3.1   | -4.0   | -3.8   | -4.2   | -3.0   | -2.9   | -2.7   | -2.7   |
| Basic fiscal balance, incl. grants & HIPC   | -1.3   | -0.6   | -2.1   | -2.0   | -0.6   | -0.6   | -0.4   | -0.3   | -0.3   |
| External sector   |        |        |        |        |        |        |        |        |        |
| Exports of goods and services <sup>3</sup>  | 27.0   | 29.4   | 29.9   | 27.8   | 28.9   | 29.1   | 29.0   | 28.8   | 28.8   |
| Imports of goods and services <sup>3</sup>  | 32.7   | 36.5   | 34.5   | 36.4   | 37.2   | 36.9   | 36.3   | 35.5   | 35.2   |
| Current account, excl. grants <sup>4</sup>  | -5.8   | -6.7   | -5.0   | -8.8   | -8.8   | -8.3   | -7.9   | -7.3   | -7.2   |
| Current account, incl. grants <sup>4</sup>  | -3.6   | -4.9   | -3.1   | -7.3   | -7.2   | -6.9   | -6.5   | -5.9   | -5.8   |
| External public debt  | 35.9   | 32.3   | 31.5   | 29.1   | 28.8   | 28.7   | 28.6   | 28.4   | 28.0   |
| Total public debt   | 45.4   | 43.4   | 43.5   | 40.9   | 39.3   | 38.8   | 38.5   | 37.9   | 37.1   |
| Broad money   | 32.3   | 35.0   | 37.0   | 38.5   | ...    | ...    | ...    | ...    | ...    |
| <i>Memorandum items:</i>  |        |        |        |        |        |        |        |        |        |
| Nominal GDP (in billions of CFA francs)   | 32,560 | 34,671 | 36,468 | 39,589 | 42,770 | 46,483 | 50,529 | 54,919 | 59,753 |
| Nominal GDP per capita (in US dollars)  | 722    | 714    | 775    | 750    | 783    | 822    | 861    | 901    | 944    |
| CFA franc per US dollars, average   | 472    | 495    | 472    | 511    | ...    | ...    | ...    | ...    | ...    |
| Euro per US dollars, average  | 0.72   | 0.76   | 0.72   | 0.78   | ...    | ...    | ...    | ...    | ...    |
| Foreign exchange cover ratio <sup>5</sup>   | 98.9   | 99.9   | 97.2   | 97.7   | ...    | ...    | ...    | ...    | ...    |
| Reserves in months of imports<br>(excl. intra-WAEMU imports)  | 5.9    | 6.5    | 5.9    | 5.2    | 4.9    | 4.8    | ...    | ...    | ...    |
| <b>Sources:</b> IMF, African Department database; World Economic Outlook; IMF staff estimates.  |        |        |        |        |        |        |        |        |        |
| <sup>1</sup> The estimates for 2012 refer to annual change at end-Sep, with the beginning-of-period referring to end-Sep 2011.                |        |        |        |        |        |        |        |        |        |
| <sup>2</sup> Fiscal data for 2013 reflect a strong increase in the fiscal deficit of Niger following a new project in the hydrocarbon sector. |        |        |        |        |        |        |        |        |        |
| <sup>3</sup> Excluding intra-regional trade.  |        |        |        |        |        |        |        |        |        |
| <sup>4</sup> Data up to 2011 are corrected for intra-regional trade discrepancies by BCEAO.   |        |        |        |        |        |        |        |        |        |
| <sup>5</sup> Gross official reserves divided by short term domestic liabilities (IMF definition). For 2012, the estimate refers to end-Sep.   |        |        |        |        |        |        |        |        |        |

**Table 2. Sub-Saharan Africa: Cross-Group Comparison, 2009—2017**

|  | 2009   | 2010 | 2011 | 2012 | 2013  | 2014  | 2015  | 2016  | 2017  |
|--|--|------|------|------|-------|-------|-------|-------|-------|
|  |  |      |      | Est. | Proj. | Proj. | Proj. | Proj. | Proj. |
|  | (Annual percentage change)                   |      |      |      |       |       |       |       |       |
| Real GDP   |  |      |      |      |       |       |       |       |       |
| WAEMU  | 2.9  | 4.8  | 1.1  | 5.8  | 6.0   | 6.3   | 6.1   | 5.9   | 5.8   |
| CEMAC <sup>1</sup>   | 0.5  | 5.3  | 4.0  | 4.7  | 4.9   | 5.8   | 7.1   | 5.1   | 4.7   |
| Sub-Saharan Africa <sup>2</sup>  | 2.7  | 5.4  | 5.2  | 4.7  | 5.5   | 6.2   | 6.1   | 5.9   | 5.5   |
| Inflation (annual averages)  |  |      |      |      |       |       |       |       |       |
| WAEMU  | 0.9  | 1.2  | 3.6  | 2.7  | 2.4   | 2.4   | 2.2   | 2.1   | 2.3   |
| CEMAC <sup>1</sup>   | 4.4  | 1.9  | 2.5  | 4.4  | 3.4   | 3.1   | 3.0   | 3.0   | 2.9   |
| Sub-Saharan Africa <sup>2</sup>  | 9.3  | 7.5  | 9.3  | 9.2  | 6.8   | 6.1   | 5.6   | 5.5   | 5.5   |
| Terms of trade   |  |      |      |      |       |       |       |       |       |
| WAEMU  | 4.3  | -4.7 | -0.4 | 1.5  | -0.2  | 0.6   | 0.2   | -0.4  | -0.4  |
| CEMAC <sup>1</sup>   | -16.4  | 12.4 | 11.3 | -0.7 | 4.2   | 0.9   | 1.5   | -2.2  | -1.7  |
| Sub-Saharan Africa <sup>2</sup>  | -4.6   | 8.5  | 7.0  | -1.2 | -2.9  | -1.2  | -0.2  | -0.9  | -0.8  |
|  | (Percent of GDP, unless otherwise indicated) |      |      |      |       |       |       |       |       |
| Gross national investment  |  |      |      |      |       |       |       |       |       |
| WAEMU  | 18.7   | 18.8 | 18.6 | 20.2 | 21.4  | 22.0  | 22.1  | 21.9  | 22.0  |
| CEMAC <sup>1</sup>   | 30.9   | 29.8 | 28.2 | 29.4 | 28.8  | 29.2  | 31.5  | 31.0  | 30.1  |
| Sub-Saharan Africa <sup>2</sup>  | 23.6   | 22.6 | 21.9 | 22.6 | 23.3  | 23.8  | 24.0  | 23.8  | 23.7  |
| Overall fiscal balance, incl. grants                                   |  |      |      |      |       |       |       |       |       |
| WAEMU  | -3.5   | -3.1 | -4.0 | -3.8 | -4.2  | -3.0  | -2.9  | -2.7  | -2.7  |
| CEMAC <sup>1</sup>   | -0.6   | 1.2  | 3.0  | -0.5 | -1.5  | -1.9  | -2.2  | -2.2  | -2.5  |
| Sub-Saharan Africa <sup>2</sup>  | -5.6   | -3.9 | -1.1 | -1.9 | -2.7  | -2.5  | -2.4  | -2.3  | -2.5  |
| External current account, incl. grants                                 |  |      |      |      |       |       |       |       |       |
| WAEMU  | -3.6   | -4.9 | -3.1 | -7.3 | -7.2  | -6.9  | -6.5  | -5.9  | -5.8  |
| CEMAC <sup>1</sup>   | -4.5   | -3.2 | -0.1 | -1.9 | -1.3  | -2.0  | -4.3  | -4.6  | -4.7  |
| Sub-Saharan Africa <sup>2</sup>  | -3.0   | -1.2 | -1.2 | -2.7 | -3.1  | -3.4  | -3.8  | -3.9  | -3.8  |
| External public debt   |  |      |      |      |       |       |       |       |       |
| WAEMU  | 35.9   | 32.3 | 31.5 | 29.1 | 28.8  | 28.7  | 28.6  | 28.4  | 28.0  |
| CEMAC <sup>1</sup>   | 14.0   | 10.0 | 11.1 | 12.8 | 14.1  | 15.6  | 16.8  | 17.9  | 18.7  |
| Sub-Saharan Africa <sup>2</sup>  | 11.7   | 9.3  | 9.5  | 9.6  | 10.3  | 10.9  | 11.2  | 11.4  | 11.5  |
| <b>Sources: IMF, African Department database; and staff estimates.</b> |  |      |      |      |       |       |       |       |       |
| <sup>1</sup> Central African Economic and Monetary Community (CEMAC).  |  |      |      |      |       |       |       |       |       |
| <sup>2</sup> Including Nigeria and South Africa.                       |  |      |      |      |       |       |       |       |       |

Table 3. WAEMU: Selected National Accounts and Inflation Statistics, 2009–2017

|                           | 2009                       | 2010 | 2011 | 2012 | 2013  | 2014  | 2015  | 2016  | 2017  |
|---------------------------|----------------------------|------|------|------|-------|-------|-------|-------|-------|
|                           |                            |      |      | Est. | Proj. | Proj. | Proj. | Proj. | Proj. |
|                           | (Annual percentage change) |      |      |      |       |       |       |       |       |
| Real GDP                  |                            |      |      |      |       |       |       |       |       |
| Benin                     | 2.7                        | 2.6  | 3.5  | 3.5  | 3.8   | 4.1   | 4.3   | 4.5   | 4.5   |
| Burkina Faso              | 3.0                        | 7.9  | 4.2  | 8.0  | 7.0   | 7.0   | 7.0   | 6.9   | 6.8   |
| Côte d'Ivoire             | 3.7                        | 2.4  | -4.7 | 8.6  | 8.0   | 7.3   | 7.0   | 6.7   | 6.5   |
| Guinea-Bissau             | 3.0                        | 3.5  | 5.3  | -2.8 | 5.7   | 11.0  | 5.2   | 4.6   | 4.5   |
| Mali                      | 4.5                        | 5.8  | 2.7  | -1.5 | 4.8   | 5.8   | 5.3   | 5.0   | 5.0   |
| Niger                     | -1.0                       | 10.7 | 2.2  | 11.2 | 6.2   | 7.3   | 6.9   | 6.9   | 5.7   |
| Senegal                   | 2.1                        | 4.1  | 2.6  | 3.7  | 4.3   | 4.8   | 5.0   | 5.1   | 5.2   |
| Togo                      | 3.5                        | 4.0  | 4.9  | 5.0  | 5.3   | 5.5   | 5.6   | 4.9   | 5.8   |
| WAEMU                     | 2.9                        | 4.8  | 1.1  | 5.8  | 6.0   | 6.3   | 6.1   | 5.9   | 5.8   |
| Real GDP per capita       |                            |      |      |      |       |       |       |       |       |
| Benin                     | -0.3                       | -0.3 | 0.7  | 0.7  | 1.1   | 1.4   | 1.7   | 1.9   | 2.0   |
| Burkina Faso              | -0.1                       | 4.7  | 1.1  | 5.6  | 4.6   | 4.5   | 4.6   | 4.5   | 4.4   |
| Côte d'Ivoire             | 0.7                        | -0.6 | -7.5 | 5.5  | 4.9   | 4.1   | 3.8   | 3.6   | 3.4   |
| Guinea-Bissau             | 0.9                        | 1.3  | 3.2  | -4.8 | 3.5   | 8.8   | 3.0   | 2.5   | 2.4   |
| Mali                      | 1.3                        | 2.7  | -0.4 | -4.5 | 1.7   | 2.6   | 2.1   | 1.8   | 1.8   |
| Niger                     | -2.8                       | 7.0  | 6.5  | 7.9  | 3.0   | 4.1   | 3.7   | 3.7   | 2.6   |
| Senegal                   | -0.6                       | 1.4  | -0.1 | 0.9  | 1.5   | 2.1   | 2.2   | 2.3   | 2.5   |
| Togo                      | 1.3                        | 1.7  | 2.6  | 2.7  | 3.0   | 3.2   | 3.3   | 2.6   | 3.5   |
| WAEMU                     | 0.1                        | 1.8  | -1.1 | 2.9  | 3.2   | 3.4   | 3.2   | 3.1   | 3.0   |
| Inflation                 |                            |      |      |      |       |       |       |       |       |
| Benin                     | 0.9                        | 2.6  | 2.7  | 6.6  | 3.3   | 3.1   | 3.0   | 2.8   | 2.8   |
| Burkina Faso              | 2.6                        | -0.6 | 2.7  | 3.6  | 2.0   | 2.0   | 2.0   | 2.0   | 2.0   |
| Côte d'Ivoire             | 1.0                        | 1.4  | 4.9  | 1.3  | 2.5   | 2.5   | 2.5   | 2.5   | 2.5   |
| Guinea-Bissau             | -1.6                       | 1.1  | 5.0  | 5.0  | 2.5   | 3.0   | 2.0   | 2.0   | 2.0   |
| Mali                      | 2.2                        | 1.3  | 3.1  | 5.4  | 3.1   | 3.0   | 2.5   | 2.6   | 2.5   |
| Niger                     | 1.1                        | 0.9  | 2.9  | 0.5  | 1.5   | 1.6   | 1.3   | 1.5   | 1.7   |
| Senegal                   | -1.7                       | 1.2  | 3.4  | 1.1  | 1.6   | 1.7   | 1.7   | 1.7   | 1.7   |
| Togo                      | 1.9                        | 3.2  | 3.6  | 2.5  | 4.2   | 3.6   | 2.9   | 0.5   | 4.5   |
| WAEMU                     | 0.4                        | 1.4  | 3.9  | 2.4  | 2.4   | 2.4   | 2.2   | 2.1   | 2.3   |
|                           | (Percent of GDP)           |      |      |      |       |       |       |       |       |
| Gross domestic savings    |                            |      |      |      |       |       |       |       |       |
| Benin                     | 11.9                       | 10.3 | 8.7  | 9.6  | 9.6   | 10.5  | 10.9  | 11.4  | 11.9  |
| Burkina Faso              | 13.3                       | 16.0 | 14.5 | 13.9 | 13.6  | 14.1  | 15.0  | 16.0  | 16.1  |
| Côte d'Ivoire             | 16.4                       | 11.4 | 17.6 | 9.2  | 11.9  | 12.7  | 13.3  | 13.1  | 12.8  |
| Guinea-Bissau             | 3.7                        | 1.6  | 3.7  | 2.9  | 5.9   | 12.0  | 12.6  | 12.9  | 16.1  |
| Mali                      | 13.0                       | 5.8  | 10.0 | 10.6 | 11.5  | 14.6  | 15.8  | 16.4  | 15.6  |
| Niger                     | 7.8                        | 17.6 | 14.1 | 14.5 | 17.5  | 18.2  | 15.9  | 19.2  | 13.6  |
| Senegal                   | 22.6                       | 25.3 | 22.6 | 22.7 | 23.5  | 23.9  | 24.4  | 24.8  | 25.2  |
| Togo                      | 11.3                       | 12.6 | 11.6 | 11.6 | 12.6  | 15.2  | 16.9  | 15.8  | 15.8  |
| WAEMU                     | 15.3                       | 14.1 | 15.5 | 13.0 | 14.4  | 15.5  | 16.0  | 16.5  | 15.9  |
| Gross domestic investment |                            |      |      |      |       |       |       |       |       |
| Benin                     | 20.9                       | 17.6 | 18.7 | 19.1 | 19.2  | 19.2  | 19.2  | 19.4  | 19.7  |
| Burkina Faso              | 18.0                       | 18.3 | 15.6 | 18.2 | 17.6  | 17.7  | 18.0  | 17.7  | 17.7  |
| Côte d'Ivoire             | 8.9                        | 9.0  | 8.2  | 12.5 | 15.6  | 16.9  | 17.1  | 17.3  | 17.4  |
| Guinea-Bissau             | 10.1                       | 9.8  | 10.1 | 5.7  | 8.8   | 14.6  | 14.2  | 14.2  | 17.7  |
| Mali                      | 20.3                       | 18.4 | 20.2 | 16.3 | 19.5  | 23.5  | 24.7  | 24.8  | 24.8  |
| Niger                     | 32.6                       | 37.5 | 38.8 | 40.2 | 38.5  | 33.2  | 31.1  | 28.9  | 28.8  |
| Senegal                   | 29.3                       | 29.7 | 28.7 | 30.3 | 30.1  | 30.2  | 30.5  | 30.5  | 30.5  |
| Togo                      | 18.0                       | 18.9 | 18.8 | 20.1 | 21.0  | 22.3  | 22.5  | 21.7  | 21.4  |
| WAEMU                     | 18.7                       | 18.8 | 18.6 | 20.2 | 21.4  | 22.0  | 22.1  | 21.9  | 22.0  |

Sources: IMF, African Department database; and staff estimates.

Table 4. WAEMU: Fiscal Balances, 2009—2017

|   | 2009             | 2010 | 2011 | 2012 | 2013  | 2014  | 2015  | 2016  | 2017  |
|---|------------------|------|------|------|-------|-------|-------|-------|-------|
|   |                  |      |      | Est. | Proj. | Proj. | Proj. | Proj. | Proj. |
|   | (Percent of GDP) |      |      |      |       |       |       |       |       |
| Primary fiscal balance                                  |                  |      |      |      |       |       |       |       |       |
| Benin   | -3.8             | -1.0 | -1.4 | -0.1 | -0.7  | 0.3   | 0.5   | 0.5   | 0.5   |
| Burkina Faso  | -4.3             | -4.0 | -1.9 | -2.7 | -2.1  | -2.4  | -2.3  | -2.0  | -1.9  |
| Côte d'Ivoire   | 0.0              | -0.6 | -2.3 | -2.4 | -1.4  | -1.2  | -1.4  | -1.2  | -1.1  |
| Guinea-Bissau   | 2.8              | -1.9 | -2.7 | -1.8 | -1.5  | -1.0  | -0.9  | -0.9  | -1.0  |
| Mali  | -3.9             | -2.3 | -3.5 | -1.5 | -1.7  | -2.0  | -2.0  | -2.0  | -2.1  |
| Niger <sup>1</sup>                                      | -5.2             | -2.2 | -2.7 | -3.1 | -16.1 | -3.4  | -2.8  | -2.7  | -2.6  |
| Senegal   | -4.2             | -4.2 | -5.2 | -4.2 | -3.0  | -2.8  | -2.4  | -2.1  | -1.9  |
| Togo  | -1.9             | -0.7 | -2.2 | -5.6 | -2.9  | -3.0  | -2.4  | -1.6  | -1.3  |
| WAEMU   | -2.6             | -2.1 | -2.9 | -2.6 | -3.0  | -1.9  | -1.8  | -1.6  | -1.4  |
| Overall fiscal balance (including grants)               |                  |      |      |      |       |       |       |       |       |
| Benin   | -4.3             | -1.6 | -1.8 | -0.7 | -1.2  | -0.3  | -0.1  | -0.1  | 0.0   |
| Burkina Faso  | -4.8             | -4.5 | -2.5 | -3.2 | -2.6  | -3.0  | -2.9  | -2.5  | -2.3  |
| Côte d'Ivoire   | -1.6             | -2.3 | -4.3 | -4.3 | -2.9  | -2.8  | -3.2  | -3.1  | -3.1  |
| Guinea-Bissau   | 2.7              | -2.5 | -2.8 | -1.9 | -2.0  | -1.4  | -1.3  | -1.3  | -1.4  |
| Mali  | -4.2             | -2.7 | -4.1 | -2.1 | -2.3  | -2.6  | -2.6  | -2.6  | -2.6  |
| Niger   | -5.4             | -2.4 | -3.0 | -3.5 | -17.1 | -3.9  | -3.4  | -3.2  | -3.2  |
| Senegal   | -4.8             | -5.2 | -6.7 | -5.9 | -4.9  | -4.4  | -3.9  | -3.7  | -3.5  |
| Togo  | -2.8             | -1.6 | -2.9 | -6.6 | -4.4  | -4.1  | -3.6  | -2.8  | -2.5  |
| WAEMU   | -3.5             | -3.1 | -4.0 | -3.8 | -4.2  | -3.0  | -2.9  | -2.7  | -2.7  |
| Government revenue (commitment basis, excluding grants) |                  |      |      |      |       |       |       |       |       |
| Benin   | 18.5             | 18.6 | 17.6 | 18.9 | 19.1  | 19.7  | 19.9  | 19.9  | 20.0  |
| Burkina Faso  | 13.7             | 15.6 | 16.5 | 16.6 | 16.8  | 16.9  | 17.1  | 17.8  | 18.0  |
| Côte d'Ivoire   | 18.9             | 19.2 | 14.9 | 20.0 | 19.9  | 20.0  | 20.2  | 20.4  | 20.6  |
| Guinea-Bissau   | 9.0              | 10.8 | 10.9 | 10.1 | 13.8  | 13.9  | 14.0  | 14.0  | 14.1  |
| Mali  | 17.1             | 17.3 | 16.9 | 18.5 | 18.9  | 19.2  | 19.3  | 19.5  | 19.7  |
| Niger   | 14.5             | 13.6 | 14.3 | 16.4 | 17.1  | 17.5  | 18.0  | 18.5  | 19.0  |
| Senegal   | 18.6             | 19.4 | 20.2 | 20.9 | 20.8  | 20.8  | 20.8  | 20.6  | 20.6  |
| Togo  | 16.9             | 18.9 | 18.2 | 19.3 | 20.2  | 20.0  | 20.2  | 20.2  | 20.2  |
| WAEMU   | 17.4             | 17.9 | 16.7 | 19.0 | 19.1  | 19.3  | 19.5  | 19.7  | 19.8  |
| Government expenditure                                  |                  |      |      |      |       |       |       |       |       |
| Benin   | 26.0             | 21.6 | 21.9 | 22.5 | 22.5  | 22.2  | 22.0  | 22.0  | 22.0  |
| Burkina Faso  | 24.3             | 24.6 | 24.3 | 27.2 | 26.0  | 26.3  | 26.4  | 26.5  | 26.3  |
| Côte d'Ivoire   | 21.1             | 22.0 | 19.4 | 24.8 | 24.6  | 24.8  | 25.2  | 25.2  | 25.3  |
| Guinea-Bissau   | 23.2             | 22.5 | 21.2 | 16.0 | 22.8  | 22.4  | 22.3  | 22.3  | 22.3  |
| Mali  | 25.9             | 22.8 | 24.7 | 20.3 | 21.4  | 23.7  | 23.8  | 23.9  | 23.9  |
| Niger   | 24.3             | 20.7 | 21.1 | 26.2 | 42.2  | 29.2  | 28.9  | 28.8  | 28.7  |
| Senegal   | 26.7             | 27.1 | 29.0 | 29.7 | 28.4  | 27.9  | 27.4  | 26.9  | 26.7  |
| Togo  | 21.2             | 22.5 | 24.2 | 29.5 | 28.2  | 28.3  | 28.0  | 27.1  | 26.4  |
| WAEMU   | 23.9             | 23.3 | 23.2 | 25.5 | 26.5  | 25.7  | 25.7  | 25.6  | 25.5  |
| Government current expenditure                          |                  |      |      |      |       |       |       |       |       |
| Benin   | 15.9             | 15.5 | 15.0 | 15.7 | 15.7  | 15.5  | 15.5  | 15.4  | 15.4  |
| Burkina Faso  | 12.7             | 12.1 | 13.1 | 14.5 | 12.5  | 12.8  | 12.8  | 12.9  | 12.9  |
| Côte d'Ivoire   | 17.9             | 18.6 | 16.9 | 19.5 | 17.1  | 17.1  | 17.1  | 17.2  | 17.3  |
| Guinea-Bissau   | 12.8             | 11.9 | 12.4 | 13.6 | 14.8  | 14.4  | 14.3  | 14.3  | 14.3  |
| Mali  | 13.0             | 12.9 | 14.1 | 14.4 | 13.7  | 13.0  | 12.9  | 12.9  | 12.9  |
| Niger   | 12.0             | 13.0 | 12.7 | 13.1 | 13.0  | 13.2  | 13.0  | 13.3  | 13.5  |
| Senegal   | 16.5             | 15.6 | 18.1 | 17.7 | 16.6  | 16.1  | 15.5  | 15.2  | 15.1  |
| Togo  | 15.7             | 14.7 | 15.9 | 19.7 | 17.3  | 16.5  | 16.5  | 16.6  | 16.5  |
| WAEMU   | 15.6             | 15.5 | 15.6 | 16.9 | 15.4  | 15.3  | 15.1  | 15.1  | 15.2  |
| Government capital expenditure <sup>2</sup>             |                  |      |      |      |       |       |       |       |       |
| Benin   | 9.7              | 5.5  | 6.6  | 6.8  | 6.8   | 6.6   | 6.5   | 6.5   | 6.7   |
| Burkina Faso  | 11.6             | 11.1 | 10.2 | 12.5 | 13.4  | 13.4  | 13.5  | 13.5  | 13.3  |
| Côte d'Ivoire   | 3.1              | 3.1  | 2.5  | 5.4  | 7.5   | 7.7   | 8.1   | 8.0   | 8.1   |
| Guinea-Bissau   | 9.2              | 8.8  | 8.1  | 2.1  | 7.7   | 7.7   | 7.7   | 7.8   | 7.8   |
| Mali  | 10.8             | 7.9  | 8.7  | 4.1  | 6.0   | 8.9   | 9.1   | 9.2   | 9.2   |
| Niger   | 12.3             | 7.7  | 6.9  | 13.0 | 16.2  | 16.0  | 15.9  | 15.5  | 15.4  |
| Senegal   | 10.1             | 11.6 | 10.5 | 12.1 | 11.8  | 11.8  | 11.9  | 11.7  | 11.6  |
| Togo  | 5.5              | 7.9  | 8.3  | 9.8  | 10.9  | 11.8  | 11.5  | 10.5  | 9.9   |
| WAEMU   | 7.9              | 7.2  | 6.9  | 8.4  | 9.7   | 10.1  | 10.3  | 10.2  | 10.1  |

Sources: IMF, African Development database; and staff estimates.

<sup>1</sup> 2013 data for Niger reflect the impact of a new project in the hydrocarbon sector.<sup>2</sup> Excludes net lending.

Table 5. WAEMU: External Balances, 2009—2017

|   | 2009             | 2010  | 2011  | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  |
|---|------------------|-------|-------|-------|-------|-------|-------|-------|-------|
|   |                  |       |       | Est.  | Proj. | Proj. | Proj. | Proj. | Proj. |
|   | (Percent of GDP) |       |       |       |       |       |       |       |       |
| Exports of goods and services           |                  |       |       |       |       |       |       |       |       |
| Benin                                   | 16.5             | 20.6  | 15.0  | 15.1  | 15.3  | 15.8  | 15.8  | 15.8  | 15.7  |
| Burkina Faso                            | 12.6             | 21.4  | 25.4  | 27.0  | 26.0  | 26.7  | 28.1  | 29.1  | 29.4  |
| Côte d'Ivoire                           | 50.9             | 54.1  | 54.9  | 50.6  | 49.7  | 49.9  | 50.2  | 50.0  | 50.1  |
| Guinea-Bissau                           | 15.4             | 17.7  | 23.5  | 15.7  | 20.2  | 21.3  | 21.1  | 21.0  | 21.3  |
| Mali                                    | 23.7             | 26.0  | 26.1  | 31.2  | 30.8  | 29.8  | 28.4  | 27.0  | 25.4  |
| Niger                                   | 20.6             | 22.2  | 22.2  | 24.8  | 25.7  | 28.6  | 27.6  | 27.3  | 29.4  |
| Senegal                                 | 24.4             | 25.0  | 24.7  | 24.2  | 23.9  | 23.2  | 23.0  | 23.2  | 23.1  |
| Togo                                    | 36.7             | 40.2  | 40.0  | 40.0  | 40.6  | 41.2  | 42.4  | 43.0  | 43.1  |
| WAEMU <sup>1</sup>                      | 27.0             | 29.4  | 29.9  | 27.8  | 28.9  | 29.1  | 29.0  | 28.8  | 28.8  |
| Imports of goods and services           |                  |       |       |       |       |       |       |       |       |
| Benin                                   | 29.8             | 31.1  | 27.6  | 27.7  | 27.9  | 27.6  | 27.0  | 26.8  | 26.7  |
| Burkina Faso                            | 23.3             | 29.0  | 32.1  | 36.3  | 33.5  | 33.8  | 34.4  | 34.1  | 34.2  |
| Côte d'Ivoire                           | 39.0             | 45.9  | 40.4  | 47.9  | 48.8  | 49.0  | 49.1  | 49.3  | 49.5  |
| Guinea-Bissau                           | 29.1             | 28.6  | 31.2  | 22.3  | 27.2  | 27.2  | 25.8  | 24.9  | 24.6  |
| Mali                                    | 31.4             | 39.9  | 36.1  | 36.1  | 36.8  | 37.4  | 36.0  | 34.8  | 34.1  |
| Niger                                   | 47.5             | 49.2  | 50.7  | 51.7  | 45.0  | 43.5  | 41.7  | 38.7  | 37.1  |
| Senegal                                 | 41.3             | 40.5  | 40.9  | 41.7  | 39.9  | 38.6  | 37.8  | 37.0  | 36.4  |
| Togo                                    | 52.3             | 57.3  | 57.1  | 58.1  | 58.4  | 58.3  | 57.9  | 58.4  | 57.7  |
| WAEMU <sup>1</sup>                      | 32.7             | 36.5  | 34.5  | 36.4  | 37.2  | 36.9  | 36.3  | 35.5  | 35.2  |
| External current account (excl. grants) |                  |       |       |       |       |       |       |       |       |
| Benin                                   | -12.8            | -10.3 | -11.8 | -12.1 | -11.9 | -11.0 | -10.4 | -10.5 | -10.9 |
| Burkina Faso                            | -9.1             | -6.2  | -5.3  | -8.0  | -6.3  | -5.9  | -5.3  | -4.2  | -4.0  |
| Côte d'Ivoire                           | 4.9              | 1.7   | 8.1   | -3.6  | -5.3  | -5.1  | -4.8  | -5.3  | -5.7  |
| Guinea-Bissau                           | -14.4            | -11.8 | -9.2  | -7.3  | -8.8  | -8.3  | -7.6  | -7.0  | -7.0  |
| Mali                                    | -9.2             | -14.8 | -11.5 | -7.3  | -8.8  | -10.4 | -10.1 | -9.7  | -10.5 |
| Niger                                   | -25.4            | -25.4 | -28.0 | -28.7 | -23.0 | -18.7 | -18.6 | -15.2 | -11.5 |
| Senegal                                 | -7.1             | -4.9  | -6.4  | -8.0  | -6.9  | -6.6  | -6.4  | -5.9  | -5.7  |
| Togo                                    | -8.2             | -8.7  | -10.4 | -12.0 | -12.0 | -11.3 | -9.8  | -9.2  | -8.5  |
| WAEMU                                   | -5.8             | -6.7  | -5.0  | -8.8  | -8.8  | -8.3  | -7.9  | -7.3  | -7.2  |
| External current account (incl. grants) |                  |       |       |       |       |       |       |       |       |
| Benin                                   | -8.9             | -7.3  | -10.0 | -9.7  | -9.7  | -8.9  | -8.4  | -8.5  | -8.7  |
| Burkina Faso                            | -4.7             | -2.3  | -1.0  | -4.3  | -4.0  | -3.6  | -3.0  | -1.8  | -1.6  |
| Côte d'Ivoire                           | 7.5              | 2.4   | 9.4   | -3.3  | -3.7  | -4.2  | -3.9  | -4.4  | -4.7  |
| Guinea-Bissau                           | -6.4             | -8.3  | -6.4  | -4.0  | -4.1  | -3.6  | -2.6  | -2.2  | -2.6  |
| Mali                                    | -7.3             | -12.7 | -10.2 | -5.8  | -8.0  | -9.0  | -8.9  | -8.5  | -9.3  |
| Niger                                   | -24.7            | -19.9 | -24.7 | -25.8 | -20.5 | -16.6 | -16.7 | -13.5 | -10.0 |
| Senegal                                 | -6.7             | -4.4  | -6.1  | -7.5  | -6.6  | -6.3  | -6.1  | -5.6  | -5.4  |
| Togo                                    | -6.6             | -6.7  | -7.2  | -8.4  | -8.4  | -7.1  | -5.6  | -5.5  | -5.1  |
| WAEMU                                   | -3.6             | -4.9  | -3.1  | -7.3  | -7.2  | -6.9  | -6.5  | -5.9  | -5.8  |

Sources: IMF, African Department database; and staff estimates.

<sup>1</sup>Excludes intraregional trade

**Table 6. WAEMU: Government Debt, 2009—2017**

|                      | 2009             | 2010 | 2011 | 2012 | 2013  | 2014  | 2015  | 2016  | 2017  |
|----------------------|------------------|------|------|------|-------|-------|-------|-------|-------|
|                      |                  |      |      | Est. | Proj. | Proj. | Proj. | Proj. | Proj. |
|                      | (Percent of GDP) |      |      |      |       |       |       |       |       |
| <b>External Debt</b> |                  |      |      |      |       |       |       |       |       |
| Benin                | 16.2             | 18.1 | 16.5 | 17.8 | 18.5  | 18.8  | 19.2  | 19.6  | 19.9  |
| Burkina Faso         | 23.1             | 24.0 | 22.8 | 25.2 | 25.4  | 25.4  | 25.4  | 25.1  | 24.7  |
| Côte d'Ivoire        | 53.9             | 50.6 | 55.1 | 35.6 | 33.3  | 31.6  | 30.3  | 29.1  | 28.1  |
| Guinea-Bissau        | 127.8            | 19.0 | 17.9 | 21.0 | 20.9  | 18.2  | 17.5  | 16.7  | 16.3  |
| Mali                 | 20.7             | 28.4 | 25.4 | 26.3 | 23.1  | 23.9  | 24.8  | 25.8  | 24.0  |
| Niger                | 19.9             | 16.9 | 15.7 | 34.4 | 36.6  | 37.4  | 38.3  | 39.0  | 40.0  |
| Senegal              | 26.9             | 27.5 | 28.8 | 32.7 | 34.6  | 35.4  | 35.8  | 36.1  | 36.2  |
| Togo                 | 55.1             | 17.2 | 15.5 | 18.2 | 20.5  | 21.8  | 22.5  | 22.8  | 23.0  |
| WAEMU                | 35.9             | 32.3 | 31.5 | 29.1 | 28.8  | 28.7  | 28.6  | 28.4  | 28.0  |
| <b>Domestic Debt</b> |                  |      |      |      |       |       |       |       |       |
| Benin                | 11.8             | 12.1 | 13.8 | 15.5 | 11.1  | 9.8   | 8.6   | 7.2   | 6.3   |
| Burkina Faso         | 4.1              | 3.2  | 5.2  | 4.1  | 3.5   | 3.7   | 3.8   | 3.5   | 3.2   |
| Côte d'Ivoire        | 12.6             | 15.8 | 16.0 | 15.2 | 13.6  | 13.4  | 13.2  | 13.0  | 12.9  |
| Guinea-Bissau        | 36.0             | 29.9 | 26.3 | 25.9 | 23.4  | 19.8  | 18.0  | 16.3  | 14.8  |
| Mali                 | 2.1              | 4.4  | 4.7  | 5.1  | 4.7   | 4.3   | 4.0   | 3.8   | 3.5   |
| Niger                | 8.0              | 6.8  | 6.2  | 5.5  | 4.7   | 3.9   | 3.3   | 2.8   | 2.3   |
| Senegal              | 7.2              | 8.2  | 11.3 | 12.3 | 12.2  | 12.8  | 13.0  | 13.0  | 12.9  |
| Togo                 | 20.8             | 31.4 | 30.8 | 28.3 | 25.3  | 23.5  | 21.9  | 20.1  | 17.9  |
| WAEMU                | 9.5              | 11.1 | 12.0 | 11.8 | 10.5  | 10.2  | 9.9   | 9.5   | 9.1   |
| <b>Total Debt</b>    |                  |      |      |      |       |       |       |       |       |
| Benin                | 28.0             | 30.2 | 30.3 | 33.3 | 29.6  | 28.6  | 27.8  | 26.8  | 26.2  |
| Burkina Faso         | 27.2             | 27.2 | 28.0 | 29.3 | 28.9  | 29.1  | 29.2  | 28.6  | 27.9  |
| Côte d'Ivoire        | 66.5             | 66.4 | 71.2 | 50.9 | 46.9  | 45.0  | 43.5  | 42.1  | 41.0  |
| Guinea-Bissau        | 163.8            | 49.0 | 44.2 | 46.9 | 44.2  | 38.0  | 35.4  | 33.0  | 31.0  |
| Mali                 | 22.9             | 32.8 | 30.1 | 31.4 | 27.8  | 28.2  | 28.8  | 29.6  | 27.5  |
| Niger                | 27.9             | 23.7 | 21.9 | 39.9 | 41.3  | 41.3  | 41.6  | 41.8  | 42.3  |
| Senegal              | 34.2             | 35.7 | 40.0 | 45.0 | 46.8  | 48.2  | 48.8  | 49.1  | 49.1  |
| Togo                 | 75.9             | 48.5 | 46.3 | 46.5 | 45.8  | 45.3  | 44.4  | 42.9  | 40.8  |
| WAEMU                | 45.4             | 43.4 | 43.5 | 40.9 | 39.3  | 38.8  | 38.5  | 37.9  | 37.1  |

Source: IMF, African Department database.

Table 7. WAEMU: Monetary Survey , March 2010—Sep 2012

|  | 2010<br>Mar.   | 2010<br>Jun. | 2010<br>Sep. | 2010<br>Dec. | 2011<br>Mar. | 2011<br>Jun. | 2011<br>Sep | 2011<br>Dec | 2012<br>Mar. | 2012<br>Jun. | 2012<br>Sep |
|--|--|--------------|--------------|--------------|--------------|--------------|-------------|-------------|--------------|--------------|-------------|
|  | (Billions of CFA francs)   |              |              |              |              |              |             |             |              |              |             |
| Net foreign assets                     | 5,047  | 5,188        | 4,980        | 5,385        | 5,144        | 5,423        | 5,549       | 5,501       | 5,408        | 5,002        | 4,860       |
| Net domestic assets                    | 5,260  | 5,670        | 6,050        | 6,587        | 6,916        | 6,847        | 6,886       | 7,751       | 7,771        | 8,489        | 8,618       |
| Domestic credit                        | 7,218  | 7,450        | 7,987        | 8,643        | 8,993        | 9,004        | 9,262       | 10,065      | 10,214       | 10,754       | 11,001      |
| Net credit to government               | 1,439  | 1,402        | 1,625        | 1,842        | 2,215        | 1,903        | 2,111       | 2,251       | 2,449        | 2,596        | 2,662       |
| Net credit to the economy              | 5,779  | 6,049        | 6,362        | 6,801        | 6,778        | 7,101        | 7,150       | 7,814       | 7,765        | 8,158        | 8,339       |
| Claims on private sector               | 5,778  | 6,046        | 6,357        | 6,796        | 6,775        | 7,097        | 7,149       | 7,813       | 7,764        | 8,156        | 8,334       |
| Claims on other financial institutions | 2  | 3            | 5            | 4            | 2            | 4            | 1           | 1           | 1            | 2            | 4           |
| Other items, net                       | -1,959   | -1,781       | -1,937       | -2,056       | -2,077       | -2,157       | -2,375      | -2,313      | -2,443       | -2,265       | -2,382      |
| Broad Money                            | 10,306   | 10,858       | 11,030       | 11,972       | 12,060       | 12,270       | 12,435      | 13,252      | 13,179       | 13,491       | 13,478      |
| Money                                  | 6,677  | 6,947        | 6,933        | 7,709        | 7,779        | 7,914        | 7,992       | 8,714       | 8,529        | 8,728        | 8,571       |
| of which: Currency in circulation      | 2,967  | 2,992        | 2,971        | 3,559        | 3,447        | 3,397        | 3,232       | 3,676       | 3,546        | 3,593        | 3,468       |
| Quasi-money                            | 3,629  | 3,911        | 4,097        | 4,263        | 4,280        | 4,355        | 4,443       | 4,539       | 4,650        | 4,763        | 4,907       |
|  | (Factors affecting liquidity, in percent of previous period's broad money) |              |              |              |              |              |             |             |              |              |             |
| Net foreign assets                     | 7.2  | 9.2          | 6.6          | 3.1          | 0.9          | 2.2          | 5.2         | 1.0         | 2.2          | -3.4         | -5.5        |
| Net domestic assets                    | 7.6  | 8.6          | 11.6         | 12.6         | 16.1         | 10.8         | 7.6         | 9.7         | 7.1          | 13.4         | 13.9        |
| Domestic credit                        | 10.8   | 10.7         | 14.0         | 14.0         | 17.2         | 14.3         | 11.6        | 11.9        | 10.1         | 14.3         | 14.0        |
| Net credit to government               | 8.8  | 6.6          | 8.4          | 7.4          | 7.5          | 4.6          | 4.4         | 3.4         | 1.9          | 5.6          | 4.4         |
| Net credit to the economy              | 1.9  | 4.1          | 5.6          | 6.6          | 9.7          | 9.7          | 7.1         | 8.5         | 8.2          | 8.6          | 9.6         |
| Claims on private sector               | 1.9  | 4.1          | 5.6          | 6.6          | 9.7          | 9.7          | 7.2         | 8.5         | 8.2          | 8.6          | 9.5         |
| Claims on other financial institutions | 0.0  | 0.0          | 0.0          | 0.0          | 0.0          | 0.0          | 0.0         | 0.0         | 0.0          | 0.0          | 0.0         |
| Other items, net                       | -3.1   | -2.1         | -2.4         | -1.5         | -1.1         | -3.5         | -4.0        | -2.2        | -3.0         | -0.9         | -0.1        |
| Broad Money                            | 14.8   | 17.7         | 18.2         | 15.7         | 17.0         | 13.0         | 12.7        | 10.7        | 9.3          | 10.0         | 8.4         |
|  | (Year on year percent change)  |              |              |              |              |              |             |             |              |              |             |
| Net foreign assets                     | 14.6   | 19.5         | 14.0         | 6.4          | 1.9          | 4.5          | 11.4        | 2.2         | 5.1          | -7.7         | -12.4       |
| Net domestic assets                    | 15.0   | 16.2         | 21.9         | 24.6         | 31.5         | 20.8         | 13.8        | 17.7        | 12.4         | 24.0         | 25.2        |
| Domestic credit                        | 15.5   | 15.2         | 19.5         | 20.2         | 24.6         | 20.9         | 16.0        | 16.5        | 13.6         | 19.4         | 18.8        |
| Net credit to government               | 122.2  | 75.8         | 93.2         | 71.0         | 53.9         | 35.8         | 29.9        | 22.2        | 10.6         | 36.4         | 26.1        |
| Net credit to the economy              | 3.1  | 6.7          | 8.9          | 11.2         | 17.3         | 17.4         | 12.4        | 14.9        | 14.6         | 14.9         | 16.6        |
| Claims on private sector               | 3.1  | 6.7          | 8.9          | 11.2         | 17.3         | 17.4         | 12.5        | 15.0        | 14.6         | 14.9         | 16.6        |
| Claims on other financial institutions | 57.6   | 55.0         | 294.5        | 163.8        | 45.5         | 33.6         | -78.4       | -74.7       | -53.3        | -44.8        | 300.5       |
| Other items, net                       | 16.8   | 12.1         | 12.8         | 7.9          | 6.0          | 21.1         | 22.6        | 12.5        | 17.6         | 5.0          | 0.3         |
| Broad Money                            | 14.8   | 17.7         | 18.2         | 15.7         | 17.0         | 13.0         | 12.7        | 10.7        | 9.3          | 10.0         | 8.4         |

Source: IMF, *International Financial Statistics* .

**Table 8. West African Economic and Monetary Union: Financial Soundness Indicators 2005-2012**

|   | 2005                                     | 2006  | 2007  | 2008  | 2009  | 2010  | 2011  | 2012  |
|---|--|-------|-------|-------|-------|-------|-------|-------|
|   | Dec.                                     | Dec.  | Dec.  | Dec.  | Dec.  | Dec.  | Dec.  | Jun.  |
|   | (in percent, unless otherwise indicated) |       |       |       |       |       |       |       |
| <b>Solvency ratios</b>                              |  |       |       |       |       |       |       |       |
| Regulatory capital to risk weighted assets          | 9.17                                     | 8.36  | 6.75  | 9.79  | 10.16 | 11.09 | 10.72 | 10.99 |
| Tier I capital to risk-weighted assets              | 8.78                                     | 7.98  | 6.01  | 9.37  | 9.80  | 10.55 | 10.08 | 10.59 |
| Provisions to risk-weighted assets                  | 14.98                                    | 14.17 | 12.75 | 12.24 | 10.96 | 12.05 | 10.40 | 12.49 |
| Capital to total assets                             | 5.82                                     | 5.45  | 4.29  | 6.07  | 6.20  | 6.41  | 6.48  | 5.71  |
| <b>Composition and quality of assets</b>            |  |       |       |       |       |       |       |       |
| Total loans to total assets                         | 63.44                                    | 61.91 | 59.06 | 59.41 | 57.56 | 55.27 | 55.17 | 55.29 |
| Gross NPLs to total loans                           | 19.90                                    | 20.50 | 18.90 | 19.20 | 17.20 | 17.58 | 15.92 | 16.17 |
| Provisioning rate                                   | 66.88                                    | 66.17 | 65.74 | 68.05 | 61.45 | 63.68 | 64.23 | 64.96 |
| Net NPLs to total loans                             | 7.60                                     | 8.00  | 7.40  | 7.10  | 7.40  | 7.19  | 6.35  | 6.33  |
| Net NPLs to capital                                 | 82.74                                    | 91.17 | 90.85 | 69.00 | 68.54 | 61.99 | 54.07 | 61.33 |
| <b>Earnings and profitability</b>                   |  |       |       |       |       |       |       |       |
| Average cost of borrowed funds                      | 2.10                                     | 2.20  | 2.40  | 2.60  | 2.50  | 2.90  | 2.40  | ...   |
| Average interest rate on loans                      | 9.70                                     | 8.80  | 9.90  | 10.60 | 10.10 | 10.90 | 9.60  | ...   |
| Average interest margin <sup>1</sup>                | 7.60                                     | 6.60  | 7.50  | 8.00  | 7.60  | 8.00  | 7.20  | ...   |
| After-tax return on average assets (ROA)            |  |       |       |       |       | 1.11  | 1.19  | ...   |
| After-tax return on average equity (ROE)            | 5.20                                     | 4.80  | 4.80  | 1.90  | 14.80 | 12.63 | 13.67 | ...   |
| Noninterest expenses/net banking income             | 57.90                                    | 60.75 | 62.64 | 60.91 | 63.79 | 64.75 | 61.63 | ...   |
| Salaries and wages/net banking income               | 26.50                                    | 27.75 | 27.57 | 26.50 | 27.09 | 27.11 | 26.37 | ...   |
| <b>Liquidity</b>                                    |  |       |       |       |       |       |       |       |
| Liquid assets to total assets                       | 41.79                                    | 40.89 | 38.13 | 36.64 | 33.93 | 33.27 | 33.59 | 33.25 |
| Liquid assets to total deposits                     | 55.15                                    | 54.41 | 50.95 | 50.43 | 46.04 | 45.12 | 46.07 | 46.61 |
| Total loans to total deposits                       | 83.76                                    | 82.38 | 78.89 | 81.76 | 78.45 | 83.97 | 84.29 | 86.59 |
| Total deposits to total liabilities                 | 75.74                                    | 75.15 | 74.87 | 72.66 | 73.37 | 74.12 | 72.91 | 71.35 |
| Sight deposits to total liabilities <sup>2</sup>    | 38.17                                    | 37.89 | 38.41 | 36.90 | 36.07 | 36.66 | 37.79 | 36.72 |
| Term deposits to total liabilities                  | 37.57                                    | 37.26 | 36.45 | 35.76 | 37.30 | 37.46 | 35.11 | 34.63 |
| <b>Source: BCEAO. Simple average.</b>               |  |       |       |       |       |       |       |       |
| <b>Note: Simple averages of country indicators.</b> |  |       |       |       |       |       |       |       |
| <sup>1</sup> Excluding tax on bank operations       |  |       |       |       |       |       |       |       |
| <sup>2</sup> Including saving accounts              |  |       |       |       |       |       |       |       |



Table 9. WAEMU: Main Features of WAEMU Economies in 2011 <sup>1</sup>

|  | Benin | Burkina<br>Faso | Côte<br>d'Ivoire | Guinea-<br>Bissau | Mali   | Niger  | Senegal | Togo | WAEMU<br>Total |
|--|-------|-----------------|------------------|-------------------|--------|--------|---------|------|----------------|
| Population (millions)  | 9.1   | 17.0            | 20.2             | 1.5               | 15.8   | 16.1   | 12.8    | 6.2  | 98.6           |
| Land area (thousands of sq.km.)  | 110.6 | 273.6           | 318.0            | 28.1              | 1220.2 | 1266.7 | 192.5   | 54.4 | 3464.2         |
| GNP (billions of U.S. dollars)   | 7.1   | 9.7             | 23.0             | 0.9               | 9.6    | 5.8    | 13.7    | 3.4  | 73.4           |
| GNP per capita (current U.S. dollars)  | 780   | 570             | 1090             | 600               | 610    | 360    | 1070    | 560  | 705            |
| Agriculture, value added (percent of GDP) <sup>2</sup>                       | 32.2  | 33.3            | 24.3             | n.a.              | 36.5   | 39.6   | 17.8    | 43.2 | 32.4           |
| Industry, value added (percent of GDP) <sup>2</sup>                          | 13.4  | 22.4            | 30.3             | n.a.              | 24.2   | 17.1   | 23.7    | 15.9 | 21.0           |
| Services, etc. value added (percent of GDP) <sup>3</sup>                     | 54.4  | 44.4            | 45.4             | n.a.              | 39.1   | 43.2   | 58.4    | 40.9 | 46.5           |
| Exports of goods (billions of U.S. dollars)                                  | 0.7   | 2.3             | 12.7             | 0.2               | 2.4    | 1.3    | 2.4     | 1.1  | 23.0           |
| Imports of goods (billions of U.S. dollars)                                  | 1.6   | 2.2             | 7.0              | 0.2               | 2.8    | 2.2    | 4.7     | 1.6  | 22.4           |
| Intraregional trade <sup>4</sup>   |       |                 |                  |                   |        |        |         |      |                |
| Exports (in percent of total)  | 11.1  | 8.1             | 9.5              | 3.6               | 4.5    | 0.9    | 25.1    | 25.1 | 17.9           |
| Import (in percent of total)   | 2.5   | 25.3            | 1.3              | 15.7              | 19.5   | 12.8   | 3.2     | 3.5  | 6.5            |
| Share of individual countries (in percent) <sup>5</sup>                      |       |                 |                  |                   |        |        |         |      |                |
| In GNP   | 9.7   | 13.2            | 31.4             | 1.3               | 13.1   | 7.9    | 18.7    | 4.7  | 100.0          |
| In exports   | 2.9   | 9.8             | 55.2             | 0.8               | 10.3   | 5.5    | 10.6    | 4.9  | 100.0          |
| In imports   | 6.9   | 10.0            | 31.4             | 1.1               | 12.4   | 9.9    | 20.9    | 7.3  | 100.0          |
| In net domestic assets <sup>6</sup>  | 5.7   | 7.4             | 25.7             | 0.7               | 8.0    | 3.6    | 16.7    | 5.3  | 73.0           |
| In net foreign assets <sup>6</sup>   | 15.5  | 14.3            | 29.4             | 2.0               | 12.4   | 7.6    | 18.2    | 5.1  | 104.5          |
| Poverty headcount ratio at \$1.25 a day (PPP) (% of population) <sup>7</sup> | 47.3  | 44.6            | 23.8             | 48.9              | 50.4   | 43.6   | 33.5    | 38.7 | 41.4           |
| Poverty headcount ratio at \$2 a day (PPP) (% of population) <sup>7</sup>    | 75.3  | 72.6            | 46.3             | 78.0              | 78.7   | 75.2   | 60.4    | 69.3 | 69.5           |
| Health expenditure, total (% of GDP) <sup>8</sup>                            | 4.1   | 6.7             | 5.3              | 8.5               | 5.0    | 5.2    | 5.7     | 7.7  | 6.0            |
| Public spending on education, total (% of GDP) <sup>9</sup>                  | 5.3   | 4.0             | 4.6              | n.a.              | 4.8    | 4.5    | 5.6     | 4.6  | 4.8            |

Sources: World Bank, *World Development Report*; IMF, *Direction of Trade Statistics*; World Development Indicators; and staff estimates.

<sup>1</sup> Unless otherwise indicated.

<sup>2</sup> Data shown for Benin is 2005, Burkina Faso is 2006, Mali is 2007, and Niger is 2003.

<sup>3</sup> Data shown for Benin is 2005, Burkina Faso is 2006, Mali is 2006, Niger is 2003.

<sup>4</sup> Exports to and imports from WAEMU countries in percent of total exports and imports.

<sup>5</sup> Totals may not add up to 100 because of statistical discrepancy.

<sup>6</sup> September 2012 numbers.

<sup>7</sup> Data shown for Benin is 2003, Burkina Faso is 2009, Côte d'Ivoire is 2008, Guinea-Bissau is 2002, Mali is 2010, Niger is 2008, Senegal is 2005, and Togo is 2006. WAEMU is simple average.

<sup>8</sup> Data shown for 2010 for all countries. Sum of public and private health expenditure. WAEMU is simple average.

<sup>9</sup> Data shown for Benin is 2010, Burkina Faso 2010, Côte d'Ivoire 2008, Guinea-Bissau not available, Mali 2011, Niger 2011, Senegal 2010, and Togo 2011. WAEMU is simple average.

## APPENDIX I. DEBT SUSTAINABILITY IN THE WAEMU<sup>1</sup>

*This short note examines the evolution of debt sustainability in WAEMU countries in recent years. Thanks to debt relief, all WAEMU countries now have public debt to GDP ratios way below 70 percent, the ceiling set by the regional surveillance framework, and have low or moderate ratings for the risk of debt distress according to debt sustainability analyses (reflecting prudent fiscal policies, often under Fund-supported programs). Countries have tended to re-accumulate debt in the wake of debt relief, broadly in line with expectations. Overall, there is no indication of a significant deterioration of the overall debt sustainability outlook in the WAEMU. There are new risks, however, related to the characteristics of debt issued (increasingly) on the regional market, which has relatively short maturities and high interest rates.*

- 1. All WAEMU countries now have public debt ratios way below the convergence criterion.** With Côte d'Ivoire reaching the HIPC Initiative completion point in June 2012, all WAEMU countries now have public debt to GDP ratios around or below 50 percent, i.e., way below the ceiling of 70 percent set by the regional surveillance framework. Total public debt in the WAEMU as a percent of WAEMU GDP has slightly decreased from 2009 to 2011, and is expected to decrease again by end of 2012 to about 40 percent.
- 2. Public debt ratios have tended to increase in the wake of debt relief.** This can be seen by focusing on the five countries for which the debt relief process was completed in 2006 with the delivery of MDRI relief, namely Benin, Burkina Faso, Mali, Niger, and Senegal. Figures 1–3 show that the public debt ratio increased in all these countries. There is, however, a broad range of situations, with some countries recording only very limited increases (e.g., Burkina Faso) and others larger ones (particularly Senegal).
- 3. Public debt accumulation was generally in line with expectations.** This can be seen by comparing projected debt ratios in debt sustainability analyses (DSAs) conducted by Bank and Fund staff after MDRI relief with actual developments. Most older DSAs were projecting some debt accumulation post-MDRI relief, reflecting that debt ratios were low after debt relief and that the fiscal space thus created was expected to be at least partly used. Developments in Burkina-Faso, Mali and Niger have been very close to expectations, while debt accumulation was faster than expected in Benin and Senegal, likely reflecting the impact of various unanticipated shocks.
- 4. Taking into account countries that have received debt relief recently, the overall debt sustainability outlook has clearly improved in the WAEMU.** A simple way to assess the evolution of debt sustainability is to look at the recent history of DSA risk ratings. Ratings have not deteriorated since MDRI relief was provided in 2006 to the five countries mentioned above, which currently all face a low or moderate risk of debt distress.<sup>2</sup> The three countries that

<sup>1</sup> Douglas Shapiro is the author of this note.

<sup>2</sup> Benin actually recorded an improvement. Burkina Faso and Mali incurred rating changes during that period, but are back to the rating they had in 2006 or 2007.

benefitted from debt relief more recently (Côte d'Ivoire, Guinea-Bissau, and Togo) have improved their ratings and now face a moderate risk of debt distress (Table 1).

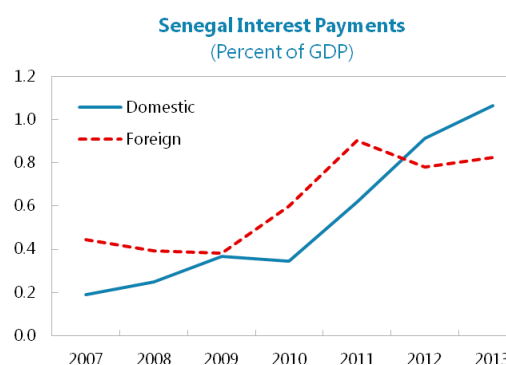
**Table 1. WAEMU DSA Ratings**

|               | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 |
|---------------|------|------|------|------|------|------|------|------|------|
| Benin         |      |      | ●    | ●    | ●    | ●    | ●    | ●    |      |
| Burkina Faso  | ●    |      | ●    | ●    | ●    | ●    | ●    | ●    |      |
| Côte d'Ivoire |      |      | ●    |      | ●    |      | ●    | ●    |      |
| Guinea-Bissau |      | ●    | ●    |      | ●    | ●    | ●    |      |      |
| Mali          |      | ●    |      | ●    | ●    |      | ●    | ●    | ●    |
| Niger         |      | ●    | ●    | ●    |      | ●    | ●    |      |      |
| Senegal       |      |      | ●    | ●    | ●    | ●    | ●    | ●    |      |
| Togo          |      |      | ●    | ●    | ●    | ●    | ●    | ●    |      |

Source: WAEMU Joint World Bank/IMF Debt Sustainability Analyses.

Debt Distress Ratings Legend ● Low ● Moderate ● High ● In Debt Distress

**5. In all countries, the share of domestic debt in public debt has increased.** This reflects, to a large extent, debt relief which has only affected external debt (Table 2). The share of domestic debt to GDP did not increase substantially, with the exception of Senegal (Figures 1–3). However, domestic debt composition has changed in recent years, following the elimination of BCEAO financing and with the development of the regional debt market. This shift may have changed significantly the risk characteristics on domestic debt, because financing raised on the regional market has relatively short maturities and relatively high interest rates. This point is well illustrated in the case of Senegal, which has also relied recently on financing from international markets.



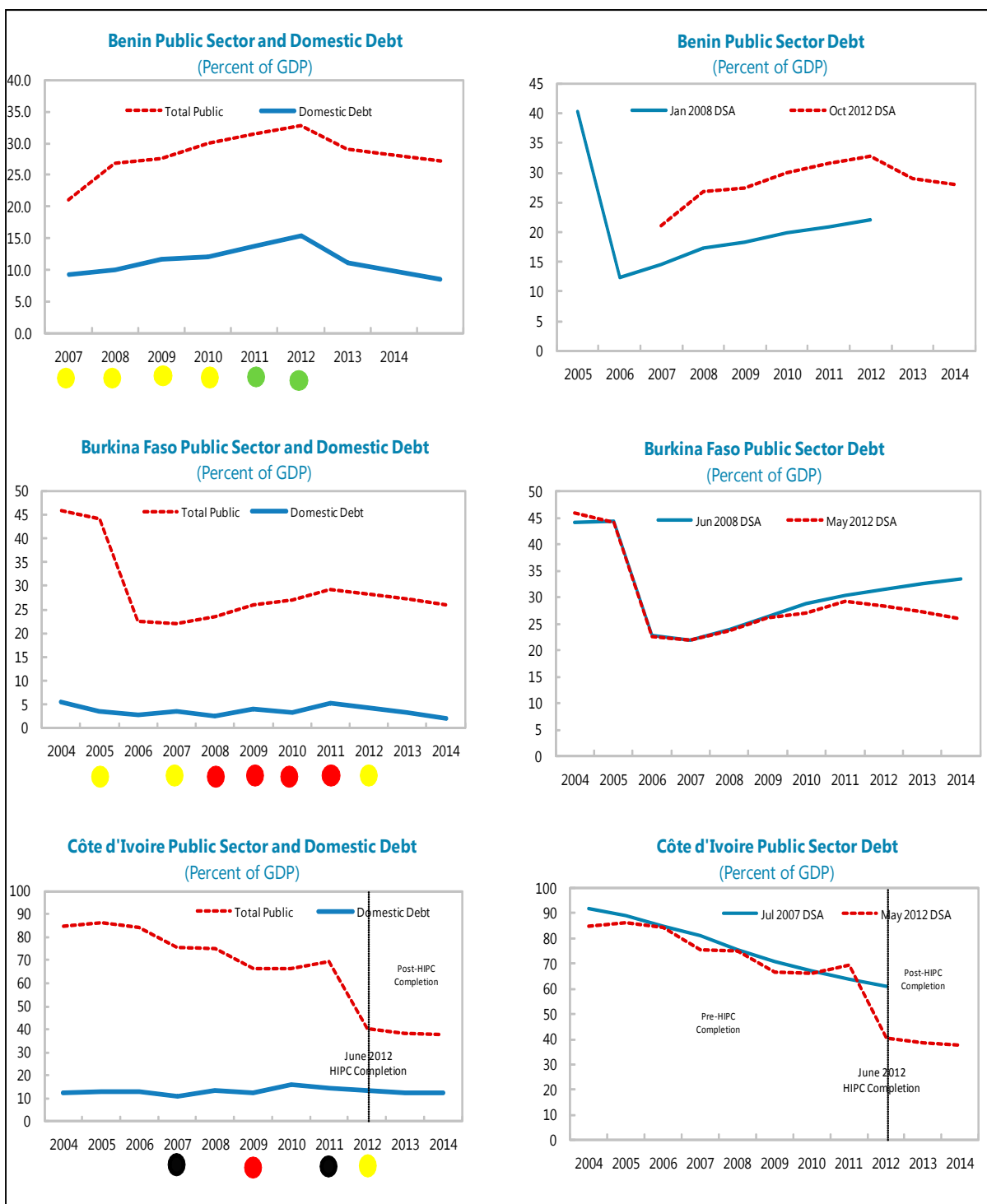
**Table 2. WAEMU: Domestic Debt as Share of Total Debt, 2007—2012**

|                   | 2007                    | 2008 | 2009 | 2010 | 2011 | 2012<br>Est. |
|-------------------|-------------------------|------|------|------|------|--------------|
|                   | (Percent of Total Debt) |      |      |      |      |              |
| Benin             | 42.3                    | 39.2 | 42.2 | 40.1 | 45.6 | 46.4         |
| Burkina Faso      | 14.8                    | 11.8 | 15.1 | 11.7 | 18.6 | 13.9         |
| Côte d'Ivoire     | 14.3                    | 17.8 | 19.0 | 23.8 | 22.5 | 30.0         |
| Guinea-Bissau     | 20.5                    | 22.1 | 22.0 | 61.1 | 59.5 | 55.2         |
| Mali              | 11.1                    | 9.1  | 9.3  | 13.3 | 15.7 | 16.1         |
| Niger             | 36.0                    | 33.2 | 28.8 | 28.8 | 28.5 | 13.8         |
| Senegal           | 23.8                    | 18.2 | 21.1 | 23.1 | 28.1 | 27.3         |
| Togo <sup>1</sup> | 23.5                    | 33.4 | 27.4 | 64.6 | 66.5 | 60.8         |
| WAEMU             | 17.8                    | 21.1 | 20.8 | 25.6 | 27.6 | 28.8         |

Source: IMF, African Department database.

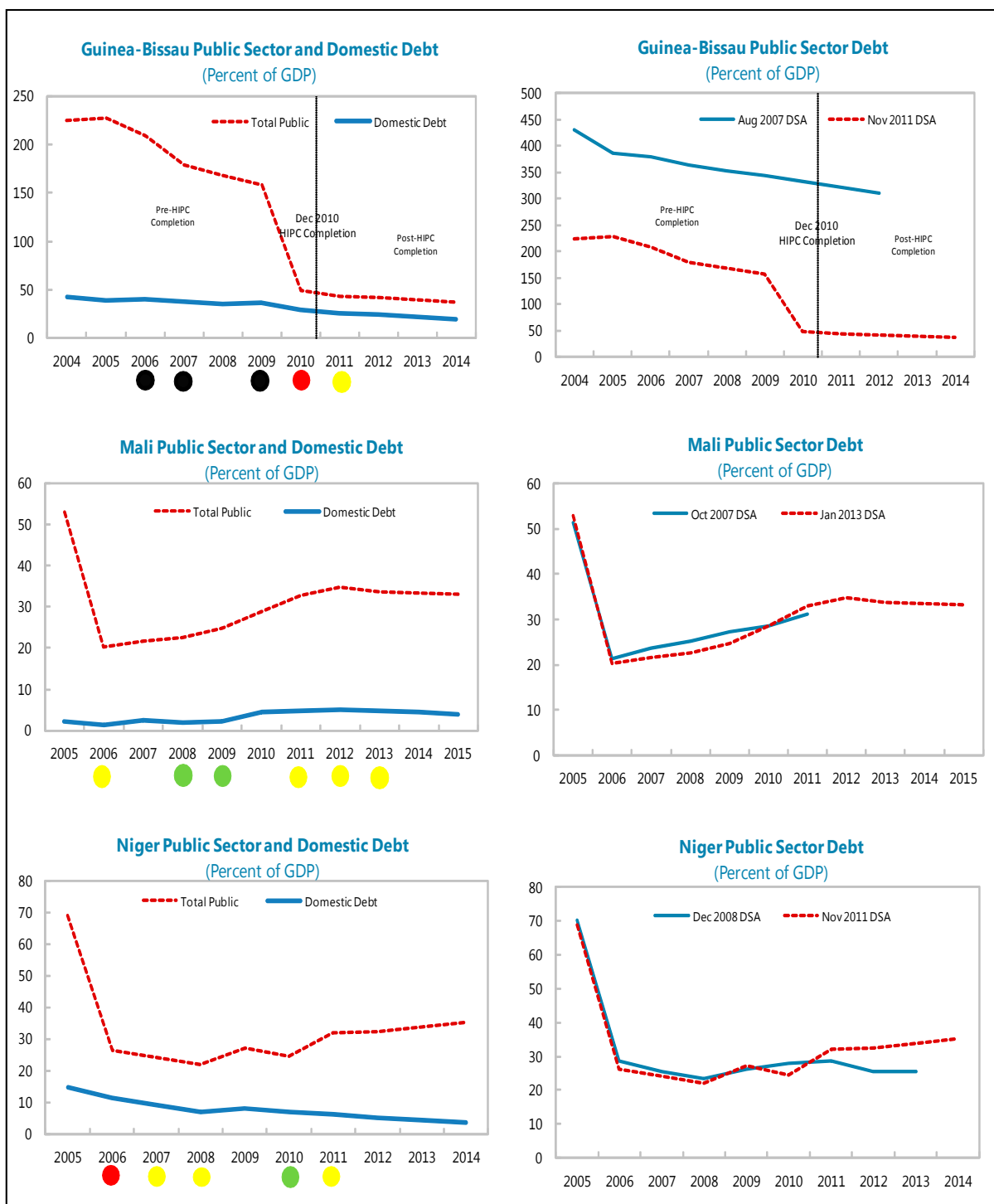
<sup>1</sup>Togo's domestic debt has been revised up since the country's last DSA.

**Figure 1. Benin, Burkina Faso, Côte d'Ivoire: Total Public and Domestic Debt**



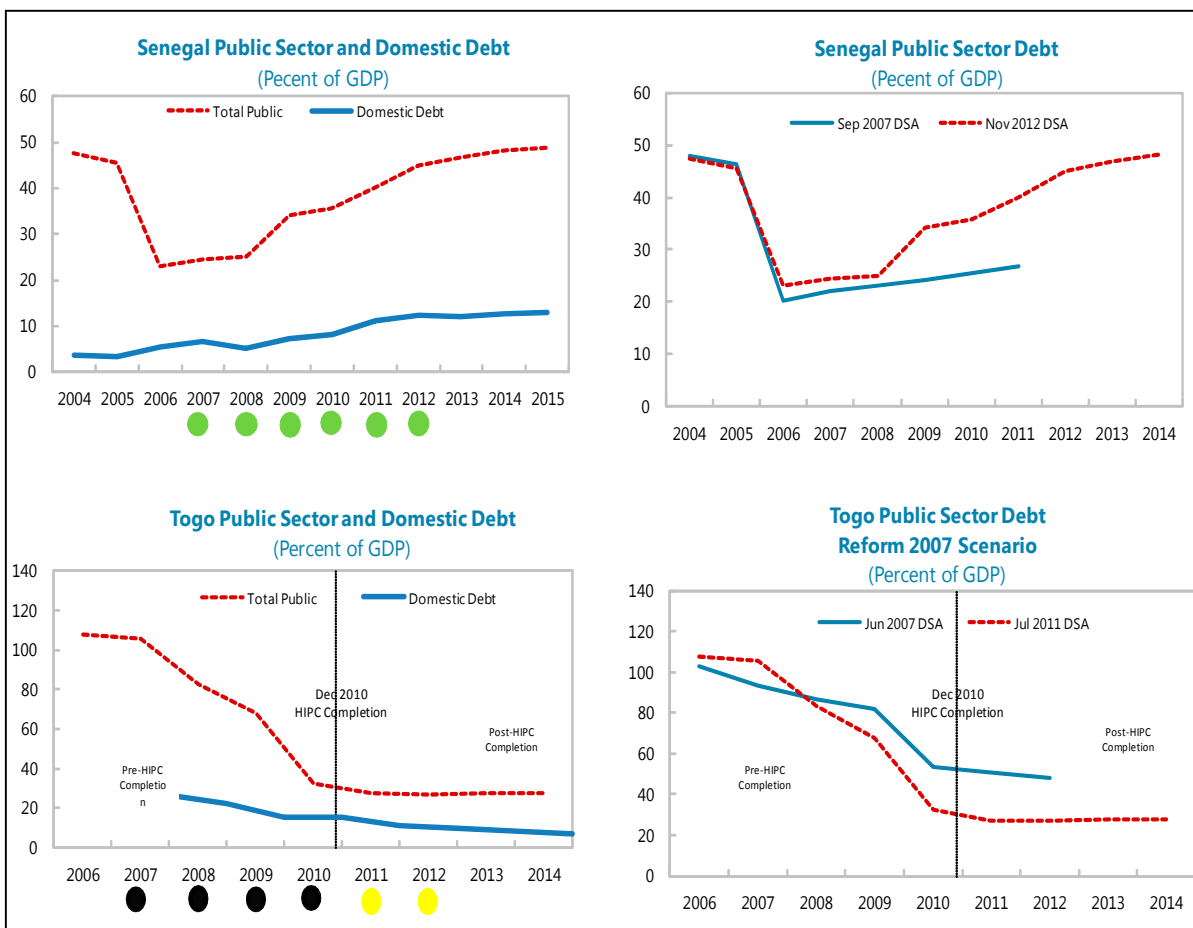
Source: WAEMU Joint World Bank/IMF Debt Sustainability Analyses. Circles represent DSA ratings for respective years following Table 1 legend: green for low, yellow for moderate, red for high, black for in debt distress.

Figure 2. Guinea-Bissau, Mali, Niger: Total Public and Domestic Debt



Source: WAEMU Joint World Bank/IMF Debt Sustainability Analyses. Circles represent DSA ratings for respective years following Table 1 legend: green for low, yellow for moderate, red for high, black for in debt distress.

**Figure 3. Senegal, Togo: Total Public and Domestic Debt**



Source: WAEMU Joint World Bank/IMF Debt Sustainability Analyses. Circles represent DSA ratings for respective years following Table 1 legend: green for low, yellow for moderate, red for high, black for in debt distress.

## APPENDIX II. EXTERNAL STABILITY ASSESSMENT

*The WAEMU current account deficit has hovered around 5 percent of GDP during the last decade and has been financed mainly by aid and foreign direct investment. Official reserves coverage remains adequate and the real effective exchange rate is broadly in line with the region's fundamentals. Non-price competitiveness, however, needs to improve.<sup>1</sup>*

### A. Balance of Payments

**1. The region's current account deficit has hovered around 5 percent of GDP during the last decade** (Figure 1A). In 2012, the current account deficit increased substantially reflecting exceptional factors such as reconstruction efforts in Côte d'Ivoire and investment in mining in Burkina Faso and Niger. The current account deficit is projected to remain high in 2013 for similar reasons, but would decline subsequently as Côte d'Ivoire's reconstruction needs subside. All WAEMU countries have experienced current account deficits of various magnitudes over the past decade, with the exception of Côte d'Ivoire which used to record surpluses until recently (Figure 1B).

**The current account deficit is financed mostly through aid.** Official transfers (grants) increased substantially in the second half of the 2000s, averaging 4 ½ percent of GDP in the past 5 years (Figure 1C). Official loans, with the exception of a 2009 spike, have remained stable at about 1 percent of GDP. Foreign direct investment is another stable source of financing (about 1 ½–2 percent of GDP).

### B. Official Reserves Adequacy

**2. Official reserves coverage remains adequate.** Foreign exchange reserves declined in 2012, reflecting the large increase in the region's current account deficit. However, they still amounted to CFAF 6,777 billion at end-2012 (about US\$ 13 billion) covering more than 5 months of next year's imports excluding intra-regional trade (Figure 1D), about 50 percent of broad money, and about 100 percent of short-term external liabilities. Reserves therefore look ample according to traditional metrics. An alternative methodology to assess adequacy suggests however that reserves are not excessive.<sup>2</sup> This approach takes into account the cost of holding reserves and their benefits in terms of mitigating the impact of macroeconomic volatility. According to this approach, the optimal reserve coverage in the WAEMU varies between 5 and 10 months of imports, depending on the interest rate differential with the rest of the world.<sup>3</sup> This approach, however, does not take into account the access to reserves guaranteed by the French Treasury under the franc zone arrangements.

<sup>1</sup> The authors of this note are Aleksandra Zdzienicka and Christina Kolerus.

<sup>2</sup> Dabla-Norris, E., J.I. Kim, and K. Shorono, 2011, "Optimal Precautionary Reserves for Low-Income Countries: A Cost-Benefits Analysis", *IMF WP* 11/249.

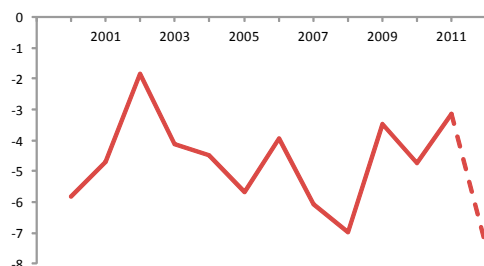
<sup>3</sup> See last year's report for more detail (*IMF Country Report* no 12/59, March 2012).



**Figure 1. WAEMU: External Sector Developments**

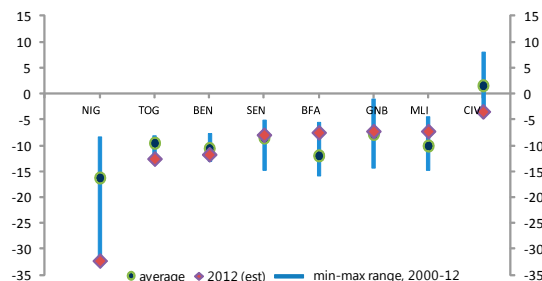
The current account deficit has hovered around 5 percent of GDP...

**A. Current account balance of the region**  
(in percent of GDP; 2000-2012)



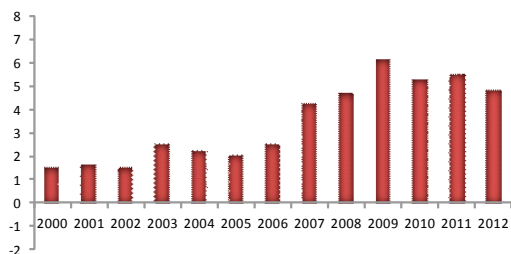
... with a range of situations across countries.

**B. Current account balance of WAEMU countries - excl. grants**  
(in percent of GDP; 2000-12)



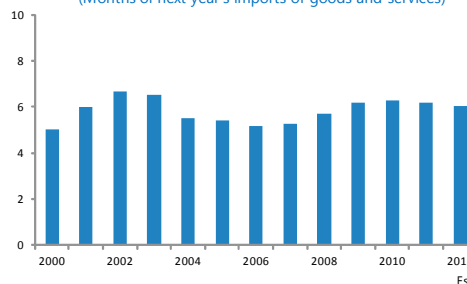
Official flows have constituted the main source of external financing.

**C. Current transfers to the region**  
(net; in percent of GDP; 2000-12)



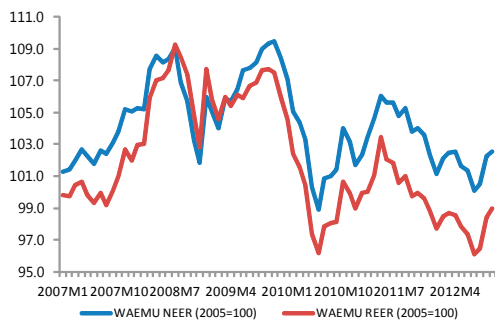
Reserve coverage remains adequate.

**D. Foreign Reserves**  
(Months of next year's imports of goods and services)



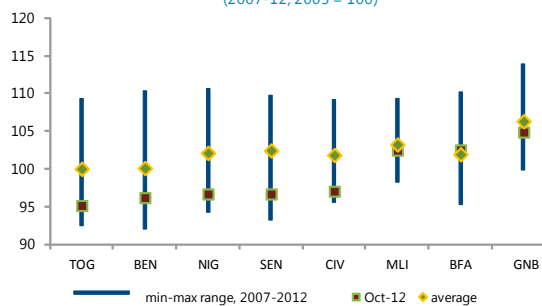
Real and nominal effective exchange rates have continued to depreciate,

**E. WAEMU real and nominal effective exchange**



with some variations across countries.

**F. Real effective exchange rate of WAEMU countries**  
(2007-12; 2005 = 100)



Source: BCEAO, DTTS, IMF staff calculations

## C. Price Competitiveness

**3. The real exchange rate remains broadly in line with fundamentals.** The real and nominal effective exchange rates for the WAEMU have depreciated slightly by about 1 percent in the last 12 months. Among WAEMU member states, the largest depreciation occurred in Senegal and Niger. Model-based assessments (Box 1) do not suggest a significant misalignment of the real effective exchange rate.

### Box 1. Various Approaches to Assess the Real Effective Exchange Rate

The macroeconomic balance approach estimates the exchange rate adjustment necessary to close the gap between the equilibrium current account balance, based on economic fundamentals, and the underlying current account projected over the medium term. The exchange rate adjustment is computed using WAEMU country-specific trade elasticities estimated by Tokarick (2010).<sup>1</sup>

The equilibrium real exchange rate is estimated as a function of medium-term fundamentals (e.g., terms of trade, openness, productivity differentials).

The external sustainability method compares the underlying current account balance with the balance that stabilizes net foreign assets (NFA) at its 2011 level (48 percent of GDP).

The results from applying these three approaches are reported in the table below. They show relatively small deviations from equilibrium, both positive and negative, which suggest no significant misalignment.

|                                | CAB/GDP |            | REER <sup>1</sup> |
|--------------------------------|---------|------------|-------------------|
|                                | Norm    | Underlying |                   |
| Macroeconomic Balance          | -3.9    | -6.3       | 3.8               |
| Equilibrium real exchange rate | ...     | ...        | -5.2              |
| External Sustainability        | -3.7    | -6.3       | 4.1               |

<sup>1</sup> "-" indicates undervaluation  
Source: IMF staff estimates.

<sup>1</sup> Tokarick, S., 2010, "A Method for Calculating Export Supply and Import Demand Elasticities", *IMF WP* 10/180.

## D. Structural Competitiveness

4. **Survey-based indicators point to low non-price competitiveness.** Various indicators rank WAEMU countries among the worst performers.

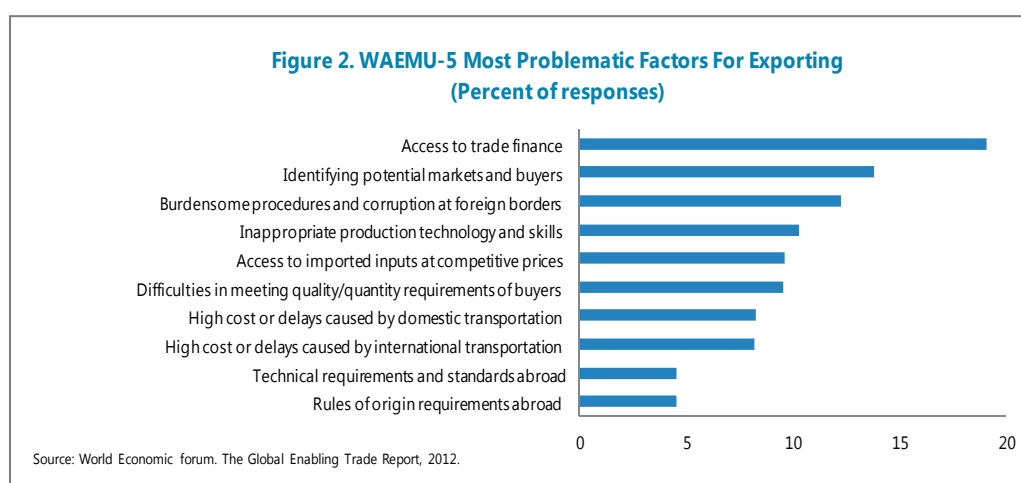
- The World Bank's 2013 Doing Business Report ranks on average WAEMU countries 167 among 185 countries. Many WAEMU countries (and the aggregate) moved down in the ranking compared to previous years, suggesting worsening deterioration in the business climate (at least

|                | 2010       | 2011       | 2012       | 2013       |
|----------------|------------|------------|------------|------------|
| Benin          | 172        | 173        | 175        | 175        |
| Burkina Faso   | 147        | 151        | 150        | 153        |
| Cote d'Ivoire  | 168        | 170        | 167        | 177        |
| Guinea-Bissau  | 181        | 181        | 176        | 179        |
| Mali           | 156        | 148        | 146        | 151        |
| Niger          | 174        | 172        | 173        | 176        |
| Senegal        | 157        | 157        | 154        | 166        |
| Togo           | 165        | 158        | 162        | 156        |
| <b>Average</b> | <b>165</b> | <b>164</b> | <b>163</b> | <b>167</b> |

Source: World Bank, Doing Business Indicators.

in relative terms). The region faces particular challenges in protecting investors' rights, enforcing contracts, starting a business, and accessing financing. Supply of infrastructure remains inadequate and procedures for paying taxes and registering propriety continue to be cumbersome.

- The recent World Economic Forum's Global Enabling Trade Report ranks five WAEMU countries 125.6 on average out of 144 countries. Factors identified as having the highest negative impact on the ease of exporting include access to trade financing and production inputs, availability and use of information, burdensome procedures, and production technologies and skills.



## APPENDIX III. THE IMPACT OF THE MALIAN CRISIS ON WAEMU<sup>1</sup>

*The economic spillovers from the Malian crisis have been limited so far, reflecting that Mali trades significantly with only three countries in the region and other economic and financial linkages are not very strong. The main risks, should the political and security situation worsen in 2013, would be a further outflow of refugees and the spread of terrorist violence which could destabilize neighboring countries.*

### A. Background

**1. In the first quarter of 2012, Mali suffered the double shock of a conflict in the North of the country and a military coup in Bamako.** After the Malian army suffered a string of setbacks at the hands of Touareg separatists in Northern Mali, in March 2012 mid-ranking officers in Bamako staged a coup, overthrowing the government and forcing the resignation of President Touré. The power vacuum was exploited by a coalition of Touareg separatists and terrorist groups, which took control of the North of the country.

**2. Mediation efforts resulted in a gradual return to the constitutional order.** In April, the President of the National Assembly took over as interim President and appointed an interim Prime Minister. In August, the cabinet was reshuffled and expanded to broaden representation.

**3. In January 2013, the French military intervened to stop the advance of the terrorist groups and restore territorial integrity.** After terrorist groups advanced to key cities in central Mali without significant resistance, the Malian government solicited military assistance from France, which, in cooperation with the Malian army, halted the terrorist groups' advance and counterattacked.

### B. Linkages Between Mali and other WAEMU Countries

**4. While exports to other WAEMU economies are rather limited, Mali's imports from the region are non-negligible.** Gold constitutes about 75 percent of Mali's exports, and WAEMU-bound exports only add up to about 11 percent of the total (Table 1). Imports from other WAEMU countries have increased by about 50 percent over the past three years and made up 38 percent of Mali's total imports in 2011. Senegal has become an increasingly large source of imported goods (cement and petroleum products), accounting for CFAF 338 billion, or 21 percent of total imports in 2011. Imports

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<sup>1</sup> Ermal Hitaj is the author of this note. The note reflects information available at the time the mission took place (January 2013).

from Benin and Côte d'Ivoire are also significant, while imports from other WAEMU countries are negligible. The fact that the main three countries of origin in the WAEMU are those through which most imports from Mali get into the WAEMU (by sea) raises the possibility that some of this trade may be transit not properly recorded.

**Table 1. Mali: Trade Flows**

|                   | 2009                        |         | 2010    |         | 2011    |         | Average 2009-11 |         |
|-------------------|-----------------------------|---------|---------|---------|---------|---------|-----------------|---------|
|                   | Exports                     | Imports | Exports | Imports | Exports | Imports | Exports         | Imports |
|                   | (in CFAF billions)          |         |         |         |         |         |                 |         |
| Bénin             | 3.2                         | 63.8    | 2.7     | 113.0   | 8.1     | 119.8   | 4.7             | 98.9    |
| Burkina           | 15.0                        | 2.2     | 21.4    | 3.3     | 47.6    | 2.5     | 28.0            | 2.7     |
| Côte d'Ivoire     | 16.3                        | 143.0   | 19.8    | 113.0   | 42.4    | 127.4   | 26.2            | 127.8   |
| Guinée Bissau     | 0.0                         | 0.0     | 0.0     | 0.0     | 0.0     | 0.0     | 0.0             | 0.0     |
| Niger             | 1.3                         | 0.0     | 1.7     | 0.2     | 2.3     | 0.0     | 1.8             | 0.1     |
| Sénégal           | 48.0                        | 162.3   | 43.5    | 239.6   | 54.4    | 338.2   | 48.6            | 246.7   |
| Togo              | 0.8                         | 30.5    | 1.0     | 27.0    | 3.2     | 16.9    | 1.7             | 24.8    |
| WAEMU             | 84.7                        | 402.0   | 90.1    | 496.2   | 158.0   | 604.8   | 110.9           | 501.0   |
| Rest of the World | 756.6                       | 772.1   | 899.1   | 1196.7  | 974.2   | 976.9   | 876.6           | 981.9   |
|                   | (in percent of total trade) |         |         |         |         |         |                 |         |
| Bénin             | 0.4                         | 5.4     | 0.3     | 6.7     | 0.7     | 7.6     | 0.5             | 6.6     |
| Burkina           | 1.8                         | 0.2     | 2.2     | 0.2     | 4.2     | 0.2     | 2.7             | 0.2     |
| Côte d'Ivoire     | 1.9                         | 12.2    | 2.0     | 6.7     | 3.7     | 8.1     | 2.6             | 9.0     |
| Guinée Bissau     | 0.0                         | 0.0     | 0.0     | 0.0     | 0.0     | 0.0     | 0.0             | 0.0     |
| Niger             | 0.2                         | 0.0     | 0.2     | 0.0     | 0.2     | 0.0     | 0.2             | 0.0     |
| Sénégal           | 5.7                         | 13.8    | 4.4     | 14.2    | 4.8     | 21.4    | 5.0             | 16.5    |
| Togo              | 0.1                         | 2.6     | 0.1     | 1.6     | 0.3     | 1.1     | 0.2             | 1.8     |
| WAEMU             | 10.1                        | 34.2    | 9.1     | 29.3    | 14.0    | 38.2    | 11.0            | 33.9    |
| Rest of the World | 89.9                        | 65.8    | 90.9    | 70.7    | 86.0    | 61.8    | 89.0            | 66.1    |

Source: BCEAO

**5. The number of Malian emigrants in WAEMU countries is considerable and inward remittances significant.** There were more than 1 million Malians living abroad in 2010 (about 7 percent of the population),<sup>2</sup> with Côte d'Ivoire, Nigeria and Niger as the top-three destinations. Annual remittances have added up to about 4 percent of GDP on average over the past decade. The number of immigrants in Mali is much lower (about 163,000 in 2010, mostly from neighboring countries), and remittances outflows have hovered around 1 percent of GDP.

**6. Financial linkages between Mali and the rest of the WAEMU are limited.** The main one is likely to be Malian government securities purchases by WAEMU-area banks outside Mali (see next section and Table 2). Although there is no good information on other cross-border financial flows within the WAEMU, these linkages are likely to be very small.

<sup>2</sup> Migration and Remittance Factbook 2011, World Bank

## C. Economic Developments in 2012 and Implications for other WAEMU Countries

**7. The economy shrunk owing to the coup d'état, the conflict in the North and the reduction in donor support.** The coup and the ensuing violence had a negative effect on industrial activity, and the drastic reduction of donor support led to a contraction of the construction and public works sector. Travel to Mali was brought to a halt by the deterioration of the security situation, causing a reduction of the activity in the services sector. Despite strong growth in agriculture, gold, and cotton production, real GDP is estimated to have contracted by 1.5 percent.

**8. The Malian crisis had a limited economic impact on other WAEMU countries.** The drop in Malian imports of construction materials has contributed to a fall in Senegal's cement production and exports. Beyond that, there is little evidence that exports from other WAEMU countries have been substantially affected.

**9. Mali's maturing public debt was rolled over and has had little impact on the WAEMU banking system.** The government reached an agreement with banks, facilitated by the BCEAO, on rolling over its maturing treasury bills and bonds. The amount of debt rolled over was CFAF 138 billion, of which CFAF 43 billion was due to WAEMU-area banks outside Mali. While this is not negligible, it is only a fraction of bank holdings of WAEMU government debt.

**10. The humanitarian and security repercussions have been significant.** The violence in the North exacerbated the food crisis caused by the poor harvest of 2011, and resulted in the displacement of about 400 000 people, only about half of which remain within Mali. The other half sought refuge in neighboring countries, with Mauritania, Burkina Faso and Niger hosting about 96,000, 38,000,<sup>3</sup> and 53,000 refugees, respectively.

## D. Economic Outlook for 2013

**11. The baseline scenario for Mali in 2013 would entail no further negative effect on other WAEMU countries.** In 2013, the Malian economy is projected to recover. Real GDP growth would return to trend (4.8 percent), average inflation would decrease to 3 percent, and the current account deficit (including grants) would increase (to 8 percent of GDP) as economic activity picks up and the authorities reconstitute their emergency food stocks. This deficit would only be partially financed by foreign direct investment and the resumption of project aid, implying that Mali would draw down foreign exchange reserves to finance the rest (about \$160 million). In this scenario, other WAEMU countries' exports to Mali would be expected to pick up. However, the refugee situation in neighboring countries is likely to remain subject to uncertainty until the situation in the North has normalized.

<sup>3</sup> UNHCR estimates the number of Malian refugees in Burkina Faso at 38,000 as of December 2012. This figure is a significant downward revision from UNHCR's earlier estimate of 107,000, which was based on self-declaration by heads of refugee households. The new estimate was based on a biometric registration of all refugees, and a precise headcount of incoming refugees.

**12. The outlook for 2013 is subject to more downside risks than usual owing to uncertainties related to the political and security situation.** While the terrorists have been driven out of urban areas in the North and a roadmap envisaging new elections in July has been adopted, most of the terrorists are believed to have retreated into the rugged desert terrain, and the terrorist threat remains elevated. Setbacks in the government's attempts to stabilize the north of the country could worsen the security situation, weaken investor and consumer confidence, and slow down growth.

**13. For neighboring countries, the main risk would be the spread of terrorist violence.** The direct economic and financial impact would indeed be limited. Assuming import elasticity vis-à-vis output of 1.45,<sup>4</sup> a 2 percent<sup>5</sup> reduction in Malian real GDP would cause a reduction of WAEMU-area imports of about 3 percent, or CFAF 18 billion using 2011 data; the loss for Senegal would be about 0.1 percent of its GDP, assuming all countries are affected similarly. Another risk would be the inability of the Malian government to repay its debt to banks in other countries maturing in 2013 but the amount is limited (CFAF 57 billion, or less than 0.2 percent of the WAEMU GDP excluding Mali) and a rollover could presumably be envisaged as in 2012. The main risk for neighboring countries would likely be a period of prolonged instability the North, which could lead to an expansion of terrorist activities in these countries and require them to further increase defense and security spending.

**Table 2. Mali: Domestic Debt Service due in 2013**  
(in CFAF billions)

|           | Malian Banks | WAEMU Banks |
|-----------|--------------|-------------|
| T-bonds   |              |             |
| Principal | 13.2         | 4.6         |
| Interest  | 3.0          | 0.9         |
| T-bills   |              |             |
| Principal | 66.7         | 52.9        |
| Interest  | 3.1          | 2.6         |
| Total     |              |             |
| Principal | 79.8         | 57.5        |
| Interest  | 6.1          | 3.5         |

Source: Malian Authorities

<sup>4</sup> Senhadji (1998) estimates average short-run and long-run income elasticity of imports at 0.45 and 1.45, respectively. This note conservatively assumes a rapid reaction of Malian import demand to income changes.

<sup>5</sup> A 2 percent decline in GDP is predicated on a similar drop in services and industrial production as in 2012, and a lower growth in the primary sector.

## APPENDIX IV. SHOCKS AND SHOCKS ABSORPTION IN THE WAEMU.<sup>1</sup>

*This note first assesses to which extent business cycles are synchronized in the WAEMU, and how synchronization has evolved over time. Looking then at shocks more explicitly, it explores whether there has been “shock convergence” (i.e., whether shocks have become less asymmetric over time). In a second part, the note explores the effectiveness of monetary policy in influencing certain key variables, and whether other mechanisms contribute to smoothing the impact of shocks on consumption. The results suggest a still high prevalence of asymmetric shocks and limited smoothing of shocks. The limited scope for, and impact of, monetary policy suggests that fiscal policy has an important role to play in addressing both symmetric and asymmetric shocks. Further integration and strengthening of market-based smoothing mechanisms (e.g., developing and improving access to the financial system) would also likely reduce the occurrence and economic impact of asymmetric shocks.*

**1. The monetary policy framework in the WAEMU has ensured price and exchange rate stability, but reduces member countries’ ability to respond to asymmetric (idiosyncratic) shocks.**

This framework has produced substantial benefits in terms of price and exchange rate stability and convertibility of the CFA franc. At the same time, it can make maintaining macroeconomic stability more challenging if the business cycles of the member countries are not well synchronized and stabilization mechanisms aimed at absorbing common and idiosyncratic shocks are absent or ineffective (Karras, 2006).

**2. Susceptibility to idiosyncratic shocks reflects structural characteristics and a lack of integration.** The degree of business cycle synchronization depends on factors such as the similarity of economic structure, trade and financial openness, the presence and type of idiosyncratic shocks, and the efficiency of adjustment mechanisms to deal with such shocks (De Grauwe, 2005). Some authors (Frankel and Rose, 1998) have argued that business cycle synchronisation may be endogenous and increase over time with the level of economic integration within a monetary union. WAEMU countries are characterized by heterogeneous economic structures. In addition, limited economic diversification and a range of geographical conditions make them prone to output volatility. Although they have been members of a monetary union for decades, trade, labor and capital market integration has not progressed significantly. Output volatility remains large (Figure 1).

**3. This note : (i) assesses the degree of business cycle synchronization and shock convergence; and (ii) provides simple estimates of the ability of monetary policy to absorb common shocks and of various mechanisms in absorbing common and idiosyncratic shocks.**

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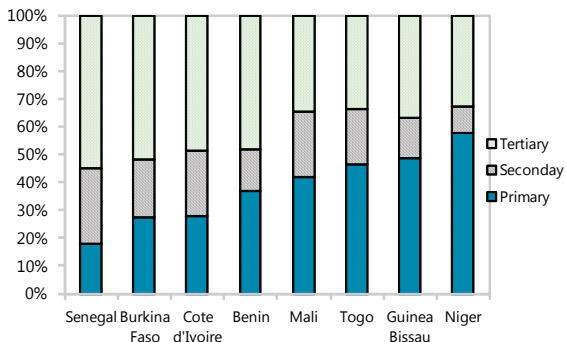
<sup>1</sup> The authors of this note are Aleksandra Zdzienicka and Christina Kolerus.



**Figure 1: Vulnerabilities of WAEMU Economies**

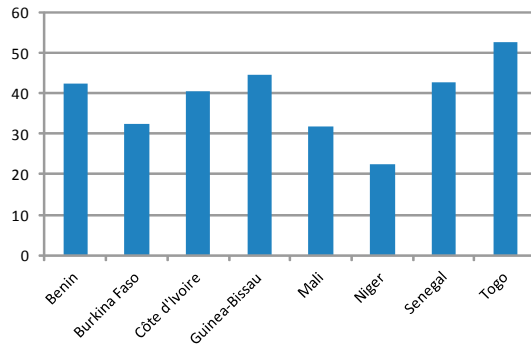
Some member states rely heavily on agriculture and economies are poorly diversified...

**Sectoral Composition of GDP, 2012**



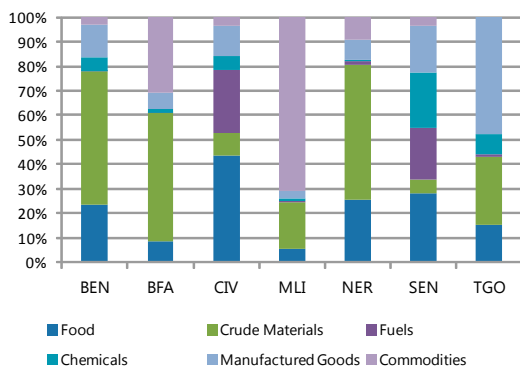
...while the financial sector remains relatively shallow.

**Broad Money, end 2011 (as percent of GDP)**



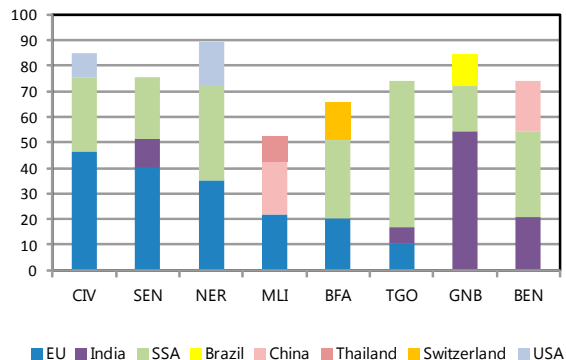
The export pattern reflects both, the lack of diversification and strong heterogeneity among WAEMU countries.

**WAEMU Export Categories, Average 2000-2010 (Percent of Total Exports)**



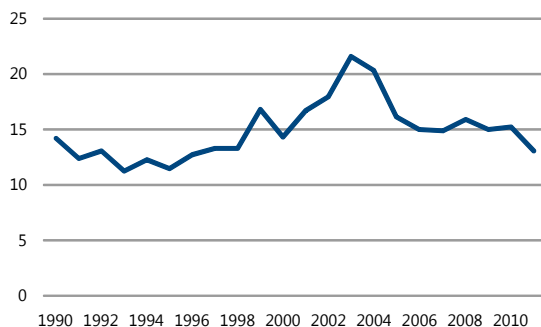
The region's economies are exposed to shocks in Europe, emerging Asia and neighboring Africa.

**Top 3 Export Markets, Average 2000-2011 (Percent of Total Exports)**



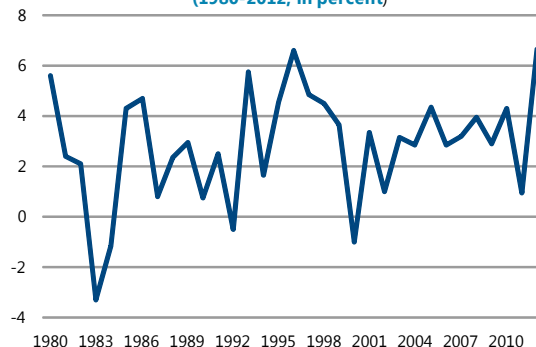
Intra-regional trade has remained relatively small.

**Intra-regional trade (1990-2011, in percentage of total trade)**



Real GDP growth has been highly volatile.

**WAEMU Real GDP growth (1980-2012, in percent)**



Source: BCEAO, DTTS, WITS, IMF staff calculations

## NATURE AND CONVERGENCE OF SHOCKS

### A. Business Cycle Synchronization over Time

**4. Business cycles synchronization in the WAEMU has been modest** (Table 1).<sup>2</sup> Over the period 1980–2012, business cycle synchronization in the WAEMU has averaged at about 0.2, ranging from about -0.2 for Togo (the less synchronized economy) to about 0.5 for Mali and 0.6 for Burkina Faso (the most synchronized economies). The degree of business cycle synchronization has varied over the last three decades, with a low point during the 1990s and an increase during the 2000s.

Synchronization has decreased again during the most recent years, possibly reflecting political instability in a number of countries (Côte d’Ivoire, Guinea-Bissau, Mali). Business cycle correlation has tended to be higher in landlocked countries (Burkina Faso, Mali, and Niger), which are more dependent on intra-WAEMU trade, and lower in countries with higher extra-zone trade links (Benin, Senegal, and Togo).

**5. Business cycles of many WAEMU countries have become more synchronized with that of the euro zone** (Table 2). This

synchronization has become relatively strong in several countries in the recent period (with the notable exceptions of Côte d’Ivoire, probably due to its political crisis at the time, and Togo). This increased correlation may reflect the impact of the global crisis. Business cycle correlation with China (taken as a proxy for emerging markets) remains limited on average, except for Guinea-Bissau and Senegal.

**Table 1. WAEMU: Business cycle correlation with WAEMU aggregate<sup>1</sup> (1980-2012)**

|               | 1980's | 1990's | 2000's | since 2007 |
|---------------|--------|--------|--------|------------|
| Benin         | 0.37   | 0.12   | 0.47   | -0.11      |
| Burkina Faso  | 0.76   | 0.57   | 0.71   | 0.44       |
| Guinea-Bissau | 0.35   | -0.13  | 0.26   | 0.03       |
| Cote d'Ivoire | 0.63   | 0.03   | 0.30   | 0.15       |
| Mali          | 0.36   | 0.63   | 0.90   | 0.43       |
| Niger         | 0.34   | 0.11   | 0.56   | 0.41       |
| Senegal       | 0.12   | 0.14   | 0.39   | 0.05       |
| Togo          | 0.22   | -0.80  | -0.03  | 0.17       |
| Average       | 0.39   | 0.08   | 0.45   | 0.20       |

<sup>1</sup> Each country is taken out in the computation of the WAEMU aggregate for its respective correlation. Source: IMF staff estimations.

**Table 2. WAEMU: Business cycle correlation with the Euro zone and China (1990-2012)**

|               | the Euro zone |        |            | China  |        |            |
|---------------|---------------|--------|------------|--------|--------|------------|
|               | 1990's        | 2000's | since 2007 | 1990's | 2000's | since 2007 |
| Benin         | -0.53         | 0.39   | 0.40       | -0.71  | 0.16   | 0.16       |
| Burkina Faso  | -0.53         | 0.00   | 0.47       | -0.01  | -0.07  | -0.08      |
| Guinea-Bissau | -0.01         | 0.34   | 0.58       | 0.01   | 0.01   | 0.33       |
| Cote d'Ivoire | -0.95         | -0.44  | -0.30      | 0.15   | -0.27  | -0.09      |
| Mali          | -0.44         | -0.21  | 0.43       | -0.55  | -0.04  | -0.20      |
| Niger         | -0.32         | 0.15   | 0.55       | -0.07  | -0.02  | -0.08      |
| Senegal       | 0.14          | 0.18   | 0.94       | 0.12   | 0.17   | 0.86       |
| Togo          | 0.73          | -0.25  | -0.37      | -0.40  | 0.02   | -0.51      |
| WAEMU         | -0.84         | -0.14  | 0.02       | -0.08  | -0.09  | 0.00       |

Source: IMF staff estimations.

<sup>2</sup> Business cycle synchronization measures for WAEMU countries are obtained by: (i) de-trending the series of real GDP using a Hodrick-Prescott (HP) filter with a smoothness parameter equal to 1 (Rand and Tarp, 2012); (ii) computing the correlation between the country's cyclical component and WAEMU's cyclical component.

## B. Shocks Convergence

**6. Supply shocks have not converged across all WAEMU countries.** The methodology used to identify various kinds of shocks and their dynamics is detailed in Box 1. Supply shocks appear very heterogeneous among WAEMU members. In Burkina Faso, Mali, Niger, and Senegal supply shocks have become more asymmetric (Figure 2). They have become more symmetric in other countries.<sup>3</sup>

### Box 1. Structural Shocks Convergence

Structural shocks convergence is assessed following a two-step approach. In the first step, three types of structural shocks—supply, real demand, and nominal—are identified using a structural vector autoregressive (VAR) model<sup>1</sup> with the Blanchard and Quah (1994) long-term restrictions, as developed by Clarida and Gali (1994).

$$\begin{pmatrix} \Delta y_t \\ \Delta reer_t \\ \Delta p_t \end{pmatrix} = \begin{pmatrix} A_{11} & A_{12} & A_{13} \\ A_{12} & A_{22} & A_{23} \\ A_{13} & A_{23} & A_{33} \end{pmatrix} \begin{pmatrix} e_{supply,t} \\ e_{real\ dem,t} \\ e_{nominal,t} \end{pmatrix} \quad (1)$$

In particular, it is assumed that: (i) only supply shocks, such as productivity or demographic shocks, affect output ( $\Delta y_t$ ) in the long term; (ii) both supply and real demand shocks (government spending or change in fiscal policy) affect the real exchange rate ( $\Delta reer_t$ ) in the long term; and (iii) all shocks influence prices ( $\Delta p_t$ ). These restrictions require that  $A_{12} = A_{13} = A_{23} = 0$ . The structural shocks are serially uncorrelated and have a covariance matrix normalized to the identity matrix. A reduced-form of the VAR model is then estimated and the time series of structural shocks are recovered.

In the second step, a dynamic space-state model using the Kalman filter technique<sup>2</sup> is estimated to assess how shocks convergence has evolved.

$$(e_t^W - e_t^i) = \alpha_t + \beta_t (e_t^W - e_t^k) + \omega_t \quad (2)$$

The dependent variable in (2) represents asymmetric shocks, measured as the difference between shocks affecting WAEMU ( $e_t^W$ ) and each country ( $e_t^i$ ). A time-varying coefficient  $\beta_t$  getting closer to zero is interpreted as increasing convergence, while  $\beta_t$  close to one suggests that shocks affecting the rest of the world ( $e_t^k$ ) affect countries in an asymmetric fashion.  $\alpha_t$  denotes the time-varying coefficients, capturing idiosyncratic shocks not related to the external environment. The two time-varying coefficients are shown in Figure 2.

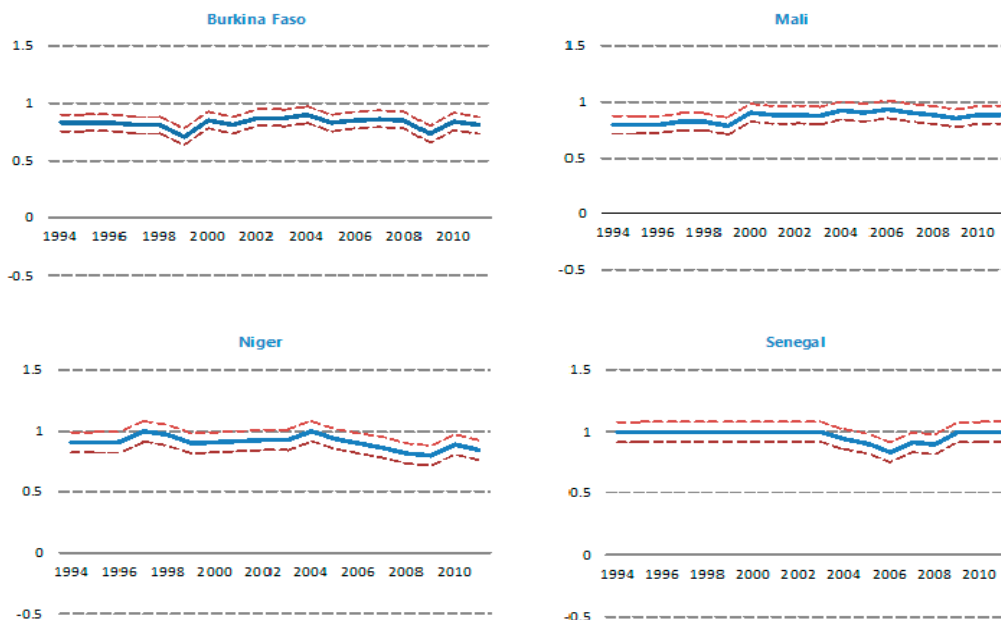
<sup>1</sup>The data are annual and taken from the IMF database; they cover the period 1970–2012.

<sup>2</sup> See Boone (1997), Babetzki et al., (2002), Zdzienicka (2010) for details.

<sup>3</sup> Similar analysis shows a higher symmetry of demand shocks in the WAEMU.

**Figure 2: Dynamics in Supply Shocks Convergence in the WAEMU (1994-2012)**

**Panel A: Burkina-Faso, Mali, Niger, and Senegal**



**Panel B: Benin, Côte d'Ivoire, Guinea-Bissau, and Togo**



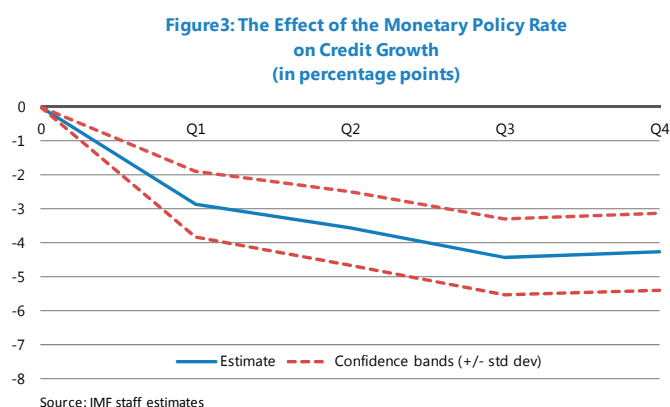
Source: IMF staff calculations

## MONETARY POLICY AND RESPONSE TO SYMMETRIC SHOCKS

**7. Monetary policy can be used in the WAEMU to address symmetric shocks.** Although the CFA franc is pegged to the euro, there is some scope for an active monetary policy in the WAEMU because of limited capital mobility (Kireyev 2012). The most important transmission channel of monetary policy in the region is the bank lending channel. While transmission is imperfect due to a shallow interbank market, there is correlation of about 0.5 between policy rates and interbank market rates after one to four quarters. The absence of a secondary government debt market and relatively illiquid equity and real estate markets make it difficult for the asset and interest rate channels to be effective.

**8. Monetary policy seems to have a significant, but relatively small, impact on economic activity via the credit market.**<sup>4</sup> An increase of 100 basis points in the main monetary policy rate is found to decrease private credit growth by about 3 percentage points after one quarter and 4

percentage points after one year (non-cumulative) (Figure 3). Reserve requirements are found not to affect credit growth in the short term. When testing the effect of changes in both interest rates and reserve requirements by means of an index, the impact of monetary policy is higher.



## OTHER SMOOTHING MECHANISMS

**9. Smoothing of the impact of macroeconomic shocks may occur through a range of channels.** The main ones are: (i) private insurance via international capital markets (e.g., through the holding of diversified portfolio of international assets or explicit insurance); (ii) saving and borrowing via international credit markets; (iii) private transfers (e.g., remittances) and official ones (e.g., foreign aid); and (iv) fiscal risk sharing across countries (e.g., via intra-union transfers). A methodology to measure the effect of some of these mechanisms is presented in Box 2.

<sup>4</sup> The impact of monetary policy measures is identified by estimating panel regression equations of the changes in the monetary policy rate on private sector credit up to four quarters ahead.

## Box 2. Measuring the Effectiveness of Smoothing Mechanisms

The effectiveness of shock smoothing mechanisms in the WAEMU is estimated using the approach proposed by Asdrubali et al. (1996). The approach consists in disaggregating GDP into different national account aggregates: Gross National Product (GNP), Net National Income (NI), Disposable National Income (DNI), and the sum of Government Consumption and Private Consumption (G+C). Using these aggregates, GDP can be decomposed as follows:

$$GDP_i = \frac{GDP_i}{GNP_i} \frac{GNP_i}{NI_i} \frac{NI_i}{DNI_i} \frac{DNI_i}{(C+G)_i} (C+G)_i \quad (1)$$

where  $i$  denotes each WAEMU state. Each ratio measures a specific smoothing mechanism. For instance, if  $\frac{GDP_i}{GNP_i}$  varies like  $GDP_i$ , then smoothing is taking place through international income transfers (which reduces GNP variations). The  $\frac{GNP_i}{NI_i}$  ratio will measure smoothing through capital depreciation or unilateral transfers (foreign aid). Further smoothing may take place through net international transfers and taxes ( $\frac{NI_i}{DNI_i}$ ) and total saving ( $\frac{DNI_i}{(C+G)_i}$ ).

Full smoothing of shocks (deviations from the trend) occurs if total consumption remains unchanged when GDP varies.

To measure the contribution of each factor (channel) in smoothing shocks to GDP, we take log and first difference of both size of equation (1) and we multiply each term by  $\Delta \log GDP_{i,t}$ . The cross-sectional variance in GDP is then divided by  $\Delta \log GDP_{i,t}$  to obtain the following equation:

$$1 = \beta^m + \beta^d + \beta^g + \beta^v + \beta^s + \beta^u \quad (2).$$

The  $\beta$ s are then estimated running the following system of independent panel regressions:

$$\Delta \log GDP_{i,t} - \Delta \log GNP_{i,t} = \alpha_t^m + \beta^m \Delta \log GDP_{i,t} + \varepsilon_{i,t}^m \quad (3)$$

$$\Delta \log GNP_{i,t} - \Delta \log NI_{i,t} = \alpha_t^d + \beta^d \Delta \log GDP_{i,t} + \varepsilon_{i,t}^d \quad (4)$$

$$\Delta \log NI_{i,t} - \Delta \log DNI_{i,t} = \alpha_t^g + \beta^g \Delta \log GDP_{i,t} + \varepsilon_{i,t}^g \quad (5)$$

$$\Delta \log DNI_{i,t} - \Delta \log (DNI + G)_{i,t} = \alpha_t^p + \beta^p \Delta \log GDP_{i,t} + \varepsilon_{i,t}^p \quad (6.1)$$

$$\Delta \log (DNI + G)_{i,t} - \Delta \log (C + G)_{i,t} = \alpha_t^s + \beta^s \Delta \log GDP_{i,t} + \varepsilon_{i,t}^s \quad (6.2)$$

$$\Delta \log (C + G)_{i,t} = \alpha_t^u + \beta^u \Delta \log GDP_{i,t} + \varepsilon_{i,t}^u \quad (7)$$

Each  $\beta$  measures the incremental percentage of smoothing achieved by each channel described above<sup>1/</sup> and  $\beta^u$  measures the part of the shock to GDP which is not smoothed. The  $\beta$  coefficients are not constrained; a negative value indicates amplification, rather than smoothing, of a shock. The  $\alpha_t$  coefficients capture time fixed effects,

1/ Table 3 presents how the  $\beta$  coefficients changed over time. Capital depreciation (equation 4) and net tax and transfers (equation 5) channels are reported jointly because of data availability issues.

**10. Shock smoothing, while on the rise, remains limited in WAEMU countries** (Table 3). A large share of shocks to GDP (about 83 percent in the recent period) is not smoothed in the WAEMU, which generates substantial consumption volatility (and likely welfare losses). In particular, net taxes and transfers and public and private saving do not have a statistically significant effect on consumption smoothing. The main (statistically significant) smoothing mechanism in the recent period has been factor income (most likely remittances, which have been shown to be counter-cyclical). Smoothing has modestly increased over the past decades. The limited amount of smoothing likely reflect a number of factors: (i) limited access to credit markets, which reduces the scope for counter-cyclical fiscal policies (with possible adverse implications for investment volatility too); (ii) the fact that most aid flows tend to be procyclical; and (iii) the absence of significant risk-sharing mechanisms at the level of the region.

**Table 3. WAEMU: Channels of output smoothing**

| Risk-smoothing channels <sup>1</sup> | B coefficient <sup>2</sup> |                    |                    |
|--------------------------------------|----------------------------|--------------------|--------------------|
|                                      | 1980-2010                  | 1980-1994          | 1995-2010          |
| Factors income flows                 | 0.068**<br>[-1.91]         | 0.170<br>[0.39]    | 0.205***<br>[2.84] |
| Capital depreciation                 | 0.098                      | 0.138              | -0.006             |
| & Net tax and transfers              | [-1.27]                    | [1.30]             | [-0.04]            |
| Saving                               |                            |                    |                    |
| Public                               | 0.004<br>[0.90]            | 0.261<br>[0.51]    | 0.151<br>[1.24]    |
| Private                              | 0.055<br>[0.46]            | 0.087<br>[0.61]    | -0.179<br>[-0.54]  |
| Unsmoothed                           | 0.878***<br>[8.56]         | 0.884***<br>[7.94] | 0.830***<br>[2.83] |

Source: IMF staff estimates

<sup>1</sup> indicates the risk-smoothing channels identified by equation (4)-(7) in Box 2; <sup>2</sup> reports the percentage of smoothing achieved by each channel; \*\*\*, \*\*, \* denotes significance at 1%, 5%, 10%, respectively.

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## APPENDIX V. FISCAL DISCIPLINE IN THE WAEMU: RULES AND MARKETS<sup>1</sup>

*This note explores the extent to which rules and market discipline are effective in ensuring fiscal sustainability in the West African Economic and Monetary Union (WAEMU). After evaluating the responsiveness of sovereign interest rates to governments' fiscal behavior, the paper finds that an improvement of the effectiveness of market discipline in WAEMU would necessitate further development of the regional financial market. In addition, fiscal aspects of the WAEMU's regional surveillance framework could be reconsidered to improve both design and enforceability.*

### A. Introduction

**1. Achieving fiscal discipline in a monetary union without a central fiscal authority, while crucial for its stability, is more challenging than elsewhere.** A monetary union is likely to increase economic and financial interconnectedness among its members. While regional integration is in itself a welcome development, it also brings new risks. One of them is that debt sustainability issues in one country could have a higher impact on the other members. Close financial linkages, such as large holdings of government debt by banks in other countries of the union, can indeed be a powerful channel of transmission of a fiscal crisis in one country to the rest of the union, with implications for the stability of the latter as has been seen in the euro area. While ensuring fiscal sustainability in all the countries may be vital for the survival of a monetary union, some its members may actually have incentives to over-borrow in the absence of a credible commitment that no country will be bailed out by the others should it face an unsustainable debt burden. Countries with weaker fiscal situations may indeed benefit from the credibility of those with stronger public finances, and face lower interest rates than they would otherwise.

**2. Fiscal discipline can in principle be supported by rules and financial markets.** Fiscal rules can be useful in anchoring expectations and providing macroeconomic stability (Morris et al., 2006), and have been viewed as a central pillar of the policy coordination framework that aims at ensuring the stability of a monetary union. Designing such rules is a delicate exercise: they need to help preserve fiscal discipline while leaving scope for counter-cyclical policies, since fiscal policy is the main tool to cope with asymmetric shocks in a monetary union. Market discipline can also help if a number of conditions are met, including free movement of capital, a credible no bail-out commitment, no monetization of the debt, and sensitivity of sovereign interest rates to fiscal behavior (Anker et al., 1997).

**3. This note explores the extent to which rules and market discipline are effective in ensuring fiscal sustainability in the WAEMU.** It first evaluates the responsiveness of interest rates on sovereign debt issued in the regional market to governments' fiscal behavior, thus gauging the

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<sup>1</sup> This note was prepared by Ermal Hitaj.



market's ability to signal the need for fiscal tightening. It also reviews the design and enforcement mechanism of fiscal rules in the WAEMU and their effectiveness. Finally, the note discusses possible ways to improve the effectiveness of the regional surveillance framework and market discipline.

## B. The Role of the Regional Market in Fostering Fiscal Discipline

**4. The regional government debt market has become an important source of financing for a number of WAEMU countries** (Table 1). The elimination of BCEAO statutory advances to governments from 2003 served as a catalyst for the government securities market, which was sustained by excess liquidity in the banking system (Sy, 2010). A few countries have accounted for the bulk of the issuances, which consist mostly of T-bills with a maturity of less than a year (Diouf et al., 2012). Furthermore, foreign participation in the WAEMU government securities market remains marginal, and trade in the secondary market limited.

### Box 1. Estimating the Disciplining Effect of the Regional Debt Market

The objective is to assess the relationship between interest rates requested by investors on the regional market and the fiscal behaviour of sovereigns. The dataset used covers all WAEMU countries over 1997-2011. All data used in the estimations are annual. The dependent variable is the average short-term annual interest rate a country is charged by the market.

The estimates in Table 2 are obtained through the Arellano-Bond estimation technique, which accommodates a dynamic equation specification while controlling for time-invariant country characteristics. The variables used are:

- (i) Fiscal variables: the overall fiscal balance as a share of GDP and the general government's debt-to-GDP ratio. One would expect higher deficit and debt ratios to lead to higher interest rates, as they both increase the probability of default and therefore the credit risk premium. The debt variable used here is domestic debt, which to a large extent is composed of debt issued in the WAEMU market. External debt remains mostly owed to donors, and in the past decade has been relieved in all WAEMU countries, while regional market debt continued to be serviced.
- (ii) The level of excess bank reserves in the region. With banks being the main investors, a higher level of excess reserves is likely to lead to lower interest rates.
- (iii) The WAEMU overall fiscal balance-to-GDP ratio. This variable gives a sense of how much demand there is in the market for bank excess reserves. One would expect a higher WAEMU fiscal deficit to lead to higher interest rates. This variable is calculated separately for each country, excluding the country's own fiscal balance to avoid multicollinearity.

**Table 1. WAEMU: Treasury Bills Issuance**

|               | 2001            | 2002 | 2003 | 2004  | 2005  | 2006  | 2007  | 2008  | 2009  | 2010   | 2011   |
|---------------|-----------------|------|------|-------|-------|-------|-------|-------|-------|--------|--------|
|               | (CFAF billions) |      |      |       |       |       |       |       |       |        |        |
| Benin         | 0.0             | 0.0  | 0.0  | 0.0   | 23.4  | 45.6  | 0.0   | 40.1  | 119.7 | 119.8  | 237.7  |
| Cote d'Ivoire | 0.0             | 0.0  | 16.3 | 15.7  | 47.5  | 0.0   | 164.8 | 103.0 | 538.3 | 1245.9 | 2278.8 |
| Mali          | 12.0            | 0.0  | 15.2 | 21.0  | 114.9 | 44.1  | 53.1  | 30.5  | 54.1  | 99.5   | 119.6  |
| Senegal       | 42.9            | 0.0  | 23.0 | 45.3  | 35.5  | 50.8  | 67.2  | 63.2  | 82.0  | 94.7   | 238.8  |
| Burkina Faso  | 0.0             | 51.9 | 30.9 | 41.5  | 43.3  | 50.9  | 46.9  | 61.0  | 34.3  | 43.6   | 160.8  |
| Niger         | 0.0             | 0.0  | 0.0  | 0.0   | 30.0  | 23.3  | 50.0  | 35.0  | 0.0   | 35.0   | 64.5   |
| Guinee        | 0.0             | 0.0  | 0.0  | 0.0   | 6.0   | 6.7   | 0.0   | 0.0   | 0.0   | 0.0    | 0.0    |
| Togo          | 0.0             | 0.0  | 0.0  | 0.0   | 0.0   | 0.0   | 0.0   | 10.0  | 15.0  | 30.0   | 60.0   |
| WAEMU         | 54.9            | 51.9 | 85.4 | 123.5 | 300.5 | 221.4 | 382.0 | 342.7 | 843.5 | 1668.5 | 3160.2 |

## 5. While the regional market responds to fiscal variables, borrowing costs seem to be driven mostly by the relative supply and demand for excess bank reserves.

An increase in domestic debt has a positive and significant impact on the interest rate, suggesting that the regional market does discriminate across sovereigns based on their fiscal behavior. However, the magnitudes of the effects of the WAEMU-level excess reserves and overall fiscal balance indicate that availability of and demand for bank reserves in the regional market are the main determinants of borrowing costs. This suggests a currently limited role of WAEMU financial markets in enforcing fiscal discipline. These results are in line with those from Sy (2010), who finds that supply and demand conditions are the most important determinants of the yield curve in the WAEMU. They likely reflect the limited development of the financial system, which means in particular that banks have limited investment opportunities for their excess reserves, and the quasi-absence of other investors.

**Table 2: Determinants of Interest Rates in the WAEMU**

|                                       |                      |                      |
|---------------------------------------|----------------------|----------------------|
| Overall Balance to GDP                | -0.153***<br>(0.001) | -0.0577<br>(0.274)   |
| Domestic Debt to GDP                  | 0.0944**<br>(0.013)  | 0.103***<br>(0.006)  |
| Inflation                             | 0.0608**<br>(0.016)  | -0.0201<br>(0.487)   |
| Excess Reserves                       | -0.787***<br>(0.000) | -1.290***<br>(0.000) |
| WAEMU Overall Balance to GDP          | -0.498***<br>(0.000) | -0.228*<br>(0.099)   |
| Political Risk Rating                 |                      | 0.0502***<br>(0.000) |
| L.Int Rate                            | 0.736***<br>(0.000)  | 0.528***<br>(0.000)  |
| Observations                          | 52                   | 47                   |
| p-values in parentheses               |                      |                      |
| * p < 0.10, ** p < 0.05, *** p < 0.01 |                      |                      |

## C. The Role of the Regional Surveillance Framework

**6. The regional macroeconomic surveillance framework in the WAEMU includes key fiscal rules.** Three of the four first-order convergence criteria are of a fiscal nature: the basic fiscal balance should record a surplus, the overall public debt-to-GDP ratio should be less than 70 percent, and governments should not accumulate arrears. Second-order criteria also include a number of fiscal targets, but they are less directly aimed at the stability of the monetary union.

**7. All WAEMU countries now have debt ratios way below the convergence criterion** (Table 3). The latter was designed at a time when all WAEMU countries were over-indebted, with debt ratios way above 70 percent of GDP. With Côte d'Ivoire having reached the completion point under the HIPC Initiative in 2012, all WAEMU countries have now benefitted from substantial debt

relief and have debt ratios way below 70 percent of GDP. This major structural break raises the issue of whether the existing ceiling remains appropriate.

**Table 3: WAEMU First-order Convergence Criteria, 2001–12**

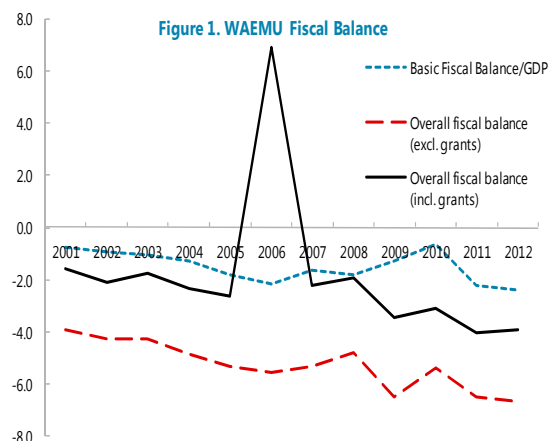
|   | 2001  | 2002  | 2003  | 2004  | 2005  | 2006  | 2007  | 2008  | 2009  | 2010 | 2011 | 2012 Est. |
|---|-------|-------|-------|-------|-------|-------|-------|-------|-------|------|------|-----------|
| <b>Basic fiscal balance/GDP (<math>\geq 0</math> percent)<sup>1</sup></b> |       |       |       |       |       |       |       |       |       |      |      |           |
| Benin   | -3.0  | -2.8  | -0.1  | -0.5  | -1.4  | 0.1   | 1.5   | -1.1  | -1.5  | 1.5  | -0.2 | 0.4       |
| Burkina Faso  | -2.5  | -3.7  | -2.9  | -3.2  | -3.5  | -4.5  | -5.8  | -4.9  | -1.9  | 0.4  | 1.2  | -0.8      |
| Côte d'Ivoire   | 1.1   | -0.4  | -1.7  | -1.3  | -1.6  | -1.6  | -0.6  | -1.6  | -1.0  | -1.6 | -4.0 | -3.8      |
| Guinea Bissau   | -6.9  | -5.8  | -7.0  | -12.0 | -7.2  | -6.2  | -7.7  | -6.7  | 3.2   | 1.0  | 2.9  | 1.5       |
| Mali  | -1.7  | -1.3  | -0.3  | -0.7  | -1.2  | -0.4  | -1.2  | -1.2  | 0.4   | 0.2  | -1.1 | -1.1      |
| Niger   | -3.7  | -1.9  | -2.1  | -2.2  | -1.5  | 1.1   | -0.2  | 1.9   | -2.8  | -1.0 | -0.1 | 0.9       |
| Senegal   | -1.2  | 1.2   | 0.2   | -0.5  | -1.2  | -4.7  | -2.6  | -2.4  | -2.1  | -1.8 | -4.2 | -3.0      |
| Togo  | 1.5   | 0.3   | 2.7   | 1.4   | -2.0  | -2.8  | -2.7  | -0.7  | -1.4  | 1.3  | -1.7 | -4.2      |
| WAEMU   | -0.8  | -0.9  | -1.1  | -1.3  | -1.8  | -2.1  | -1.6  | -1.8  | -1.3  | -0.6 | -2.1 | -2.0      |
| <i>Number of countries violating</i>                                      | 6     | 6     | 6     | 7     | 8     | 6     | 7     | 7     | 6     | 3    | 6    | 5         |
| <b>Total debt/GDP (<math>\leq 70</math> percent)</b>                      |       |       |       |       |       |       |       |       |       |      |      |           |
| Benin   | 54.0  | 47.7  | 36.5  | 33.8  | 37.2  | 11.6  | 21.9  | 25.6  | 28.0  | 30.2 | 30.3 | 33.3      |
| Burkina Faso  | 0.0   | 0.0   | 0.0   | 0.0   | 0.0   | 0.0   | 23.2  | 22.1  | 27.2  | 27.2 | 28.0 | 29.3      |
| Côte d'Ivoire   | 175.2 | 150.7 | 133.6 | 120.4 | 107.2 | 107.1 | 75.6  | 75.3  | 66.5  | 66.4 | 71.2 | 50.9      |
| Guinea Bissau   | 208.3 | 230.7 | 217.3 | 195.6 | 179.3 | 176.9 | 187.5 | 157.6 | 163.8 | 49.0 | 44.2 | 46.9      |
| Mali  | 88.7  | 56.1  | 51.6  | 48.4  | 48.3  | 19.9  | 21.0  | 20.8  | 22.9  | 32.8 | 30.1 | 31.4      |
| Niger   | 85.2  | 88.9  | 69.9  | 58.8  | 52.3  | 17.2  | 25.1  | 21.0  | 27.9  | 23.7 | 21.9 | 39.9      |
| Senegal   | 77.3  | 80.3  | 69.2  | 68.0  | 57.3  | 37.2  | 23.5  | 23.9  | 34.2  | 35.7 | 40.0 | 45.0      |
| Togo  | 108.0 | 93.4  | 92.4  | 82.5  | 72.6  | 82.5  | 112.9 | 84.0  | 75.9  | 48.5 | 46.3 | 46.5      |
| WAEMU   | 110.1 | 96.3  | 82.9  | 75.3  | 67.0  | 54.9  | 48.4  | 42.8  | 45.4  | 43.4 | 43.5 | 40.9      |
| <i>Number of countries violating</i>                                      | 6     | 5     | 3     | 3     | 3     | 3     | 3     | 3     | 2     | 0    | 1    | 0         |
| <b>Overall fiscal balance (including grants)</b>                          |       |       |       |       |       |       |       |       |       |      |      |           |
| Benin   | -4.8  | -5.1  | -1.7  | -1.2  | -2.3  | -0.3  | 0.2   | -1.7  | -4.3  | -1.6 | -1.8 | -0.7      |
| Burkina Faso  | -3.9  | -4.9  | -3.0  | -4.5  | -5.0  | 16.6  | -5.7  | -4.4  | -4.8  | -4.5 | -2.5 | -3.2      |
| Côte d'Ivoire   | 0.9   | -1.1  | -2.1  | -1.7  | -1.7  | -1.8  | -0.8  | -0.6  | -1.6  | -2.3 | -4.3 | -4.3      |
| Guinea-Bissau   | -5.4  | -3.6  | -1.0  | -4.6  | -4.9  | -2.3  | -2.7  | 1.7   | 2.7   | -2.5 | -2.8 | -1.9      |
| Mali  | -3.2  | -3.8  | -1.3  | -2.6  | -3.1  | 31.3  | -3.2  | -2.2  | -4.2  | -2.7 | -4.1 | -2.1      |
| Niger   | -3.5  | -3.0  | -2.8  | -3.6  | -2.0  | 40.3  | -1.0  | 1.5   | -5.4  | -2.4 | -3.0 | -3.5      |
| Senegal   | -2.4  | 0.0   | -1.3  | -3.1  | -3.0  | -5.7  | -3.7  | -4.6  | -4.8  | -5.2 | -6.7 | -5.9      |
| Togo  | -0.1  | -0.4  | 2.4   | 1.0   | -2.4  | -2.8  | -1.9  | -0.9  | -2.8  | -1.6 | -2.9 | -6.6      |
| WAEMU   | -1.6  | -2.1  | -1.7  | -2.4  | -2.7  | 6.9   | -2.2  | -1.9  | -3.5  | -3.1 | -4.0 | -3.8      |

<sup>1</sup> Total fiscal revenues, excluding grants, minus total expenditures excluding foreign-financed investment expenditure. From 2009, total fiscal revenues plus budget support grants plus counterpart of HIPC/M DRI-related spending for both current and capital spending less current expenditure and capital expenditure financed by own resources.

**8. The basic fiscal balance criterion has rarely been met, raising issues about its relevance and credibility.** Most countries have repeatedly missed the target over the past ten years (Table 3 and Figure 1). This begs the question of whether policies were inadequate (in light of the repeated breaches) or if the criterion itself needs to be reconsidered.

**9. Another issue which could warrant reconsideration is monitoring and enforcement.**

The Excessive Deficit Procedure (EDP), while outlining a sequence of remedial steps, does not stipulate a clear timeline or specify the mitigating circumstances that could temporarily exempt a country from the process. A deviating country is given 30 days to develop an adjustment strategy, which can benefit from financial assistance from the Union. In case a



country cannot come up with corrective measures or they are poorly executed, it is liable to sanctions, which can include publication of a statement on the country's economic situation, withdrawal of the Union's assistance, recommendation to the BCEAO to review its intervention policy towards the country, and finally suspending financial support from the Union. It is not clear how much time a country is given to take the correcting measures and whether, in case adjustment fails, the process reverts to the very beginning, or to the last fulfilled step. Furthermore, the acceptable adjustment and the monetary value of the sanctions are not specified; in fact financial sanctions have never been implemented. The ambiguity of the corrective mechanism above is compounded by the leeway provided by Article 71 of the WAEMU Treaty which states that, if a member country is experiencing economic distress or is susceptible to such distress because of exceptional circumstances, the (unanimous) WAEMU Council can exempt it from the obligation to meet part or all of the convergence criteria.

## D. Strengthening the surveillance framework and market discipline

**10. Deepening the regional market would increase market discipline.** The WAEMU financial market, while having developed substantially in the last decade, is still relatively shallow. This likely results in imperfect pricing of sovereign borrowing. Market monitoring may also be hampered by banks' limited capacity to assess fiscal sustainability. Further market development, and the associated increasing reliance of sovereigns on this kind of financing, can be expected to increase market discipline. Improving information quality and availability, which can then be used by market participants for pricing purposes, would also help. Banks, on their side, may need to improve their analytical capabilities. Finally, the supervision authorities could consider introducing a non-zero risk weight for government paper in the financial institutions' capital adequacy calculations.

**11. The ceiling for the public debt ratio could be lowered.** The current ceiling was set at a time when debt ratios were much higher. Recent research conducted by Bank and Fund staff in the context of the debt sustainability framework (DSF) suggests that a ceiling of 70 percent of GDP may be higher than desirable from the perspective of limiting the risk of debt distress. It could be considered to lower it to around 50 percent, which is the level suggested by Bank and Fund staff for countries with low or medium quality of policies and institutions in the sense of the DSF (i.e., countries with a Country Policy and Institutional Assessment (CPIA) index lower than 3.75). Whatever its level, the ceiling should be seen as a debt level to avoid reaching, not as an optimal level.

**12. The design of the fiscal balance criterion could also be reconsidered if its main objective is to preserve fiscal sustainability.** The exclusion of foreign-financed capital expenditure from the current definition raises two issues: first, it excludes a substantial source of debt accumulation, which in the past was a major contributor to over-indebtedness; second, it discriminates among sources of financing, to the detriment of regional financing at a time when it might actually be desirable to develop the regional market. An overall deficit target would allow better control over debt accumulation and would not create distortions. If the authorities were to move in this direction, the next issue to address would be how to set the ceiling for the overall deficit to both ensure debt sustainability and allow for counter-cyclical policy responses. A solution considered in the euro area

has been to set a target for the structural (cyclically-adjusted) balance. However, such an approach may be more challenging to implement in the WAEMU, due to the absence of clear business cycles and data quality and availability issues. A possible alternative approach would be to use as a reference for the ceiling the deficit level which would stabilize the debt ratio in the steady state. For instance, assuming that nominal GDP grows by 7 percent at the steady state (5 percent for real growth, and 2 percent for inflation, which is the BCEAO's objective), a deficit of 3.5 percent stabilizes the debt ratio at 50 percent. The ceiling could be set slightly below this level, while allowing it to exceed it temporarily (and by a limited amount) under exceptional circumstances.

**13. Finally, the monitoring and enforcement mechanism may need to be strengthened.**

The WAEMU Commission encounters difficulties collecting the information it needs to do effective regional surveillance; for instance, the data on fiscal arrears do not seem easily available. The timeliness of information may also be an issue. Improving the availability, quality, and timeliness of information is critical if the regional institutions are to exercise meaningful surveillance. Another issue is enforcement. While the design of the EDP could perhaps be improved, the more fundamental issue is the readiness of member states to subject themselves to strong oversight and possible sanctions from their peers. This is obviously a highly political issue, and perhaps not an urgent one, but it will need to be addressed in the medium term. A first step should be increased transparency and dissemination of regional and national fiscal outcomes.

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INTERNATIONAL MONETARY FUND

# WEST AFRICAN ECONOMIC AND MONETARY UNION (WAEMU)

## STAFF REPORT ON COMMON POLICIES FOR MEMBER COUNTRIES: SUPPLEMENT-FINANCIAL DEPTH AND MACRO- STABILITY

March 8, 2013

*This enhanced review of WAEMU's financial sector is one of several pilot reviews called for by the Executive Board in May 2012. The purpose of the reviews is to go beyond the traditional surveillance focus on banking system soundness and solvency by analyzing in more depth the interplay between financial development, macroeconomic and financial stability, and effectiveness of macroeconomic policies in low-income countries. As the WAEMU is a monetary union composed of eight countries, a number of key macroeconomic and financial policies—including monetary policy and supervision—are designed and implemented at the union level, while responsibility for others rests with national authorities. This study focuses therefore on WAEMU-specific issues. This follows and complements the two previous pilots on Benin and Senegal.*

*The financial system in the WAEMU is dominated by the banking sector, but is evolving rapidly with the emergence of new transnational banking groups and micro-finance institutions. The regional securities and equity market is a marginal source of funding, except for governments. The interbank market remains shallow. The banking system in the region is highly heterogeneous. While most banks are adequately capitalized and profitable, pockets of vulnerability, including public banks, were identified. Compliance with prudential norms remains low for a number of ratios, suggesting a degree of regulatory forbearance, and some of these norms are not in line with international standards. Stress tests and financial soundness indicators show that concentration of lending and asset quality are significant risks. The rising sovereign-bank linkage requires close monitoring.*

*While financial development broadly reflects the region's structural characteristics, there is scope for further deepening and broadening. This would facilitate the financing of growth, improve financial inclusion and the ability of firms and households to cope with a volatile environment, and increase the effectiveness of macroeconomic policies. Financial development will bring new challenges.*

*A significant strengthening of the regulatory and supervisory framework is necessary to address existing and new risks. The emergence of regional banking groups requires the development of supervision on a consolidated basis and strengthening of cooperation with banking supervisors in countries where these groups operate. The increasing exposure of banks to sovereigns is also a risk which needs to be recognized, including through a non-zero weight on government paper in capital adequacy calculations. Micro-prudential regulation should be revised to bring certain prudential standards closer to international best practice, for example on risk concentration, classification of claims and provisioning, while taking into account the regional context. The move to Basel II will be a good opportunity to address many of these issues.*

*The financial crisis prevention and management framework could also be strengthened. Crisis prevention requires greater transparency, including through the regular and timely compilation and publication of financial soundness indicators for all member countries. Regular stress tests would be a welcome step toward the introduction of an early warning system. There is scope for improving the bank resolution framework, which would reduce the budgetary cost of government intervention. Swift action in this area, including by giving broader powers to the supervisor and close collaboration with other supervisors in the case of cross-border groups, is necessary.*



Approved By  
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# FINANCIAL SYSTEMS IN THE WAEMU: STRUCTURE, PERFORMANCE, AND RISKS

## A. Overview of the Structure of the Financial System<sup>1</sup>

**1. The financial system in the WAEMU remains largely bank-based.** The banking sector comprises 106 banks and 13 financial institutions which together hold more than 90 percent of the financial system's assets (about 54 percent of GDP end-2011). Five banks account for 50 percent of banking assets (see Figure 1). The ownership structure of the sector is changing fast, with the rapid rise of foreign-owned (pan-African) banks. This contributes to higher competition but also rising heterogeneity in the banking system, with large and profitable cross-country groups competing with often weaker country-based (and sometime government-owned) banks. Nonbank financial institutions are developing quickly, notably insurance companies, but remain overall small. More detailed analysis on the banking system is presented in section I.B.

**Text Table 1: Structure of the Financial System**

|  | Number of                      |                            | Total Assets        |                            | Deposits outstanding | Loans outstanding   |
|--|--------------------------------|----------------------------|---------------------|----------------------------|----------------------|---------------------|
|  | Institutions<br>as of end-2011 | Branches<br>as of end-2011 | Amount<br>(bn FCFA) | (% of Total)<br>(% of GDP) | Amount<br>(bn FCFA)  | Amount<br>(bn FCFA) |
| <b>Private depository institutions</b>       |                                |                            |                     |                            |                      |                     |
| Banks  | 107                            | 1,853                      | 19,725              | 53.8                       | 11,173               | 8,465               |
| Microfinance Institutions <sup>(1)</sup>     | 880                            | 3,179                      |                     |                            | 517                  | 501                 |
| <b>Non-depository financial institutions</b> |                                |                            |                     |                            |                      |                     |
| Insurance companies                          | 14                             | NA                         |                     |                            | NA                   | NA                  |
| Securities companies/Money market dealers    | NA                             | NA                         |                     |                            | NA                   | NA                  |
| Other  | 14                             | NA                         |                     |                            | NA                   | NA                  |
| <b>Public financial institutions</b>         | NA                             | NA                         |                     |                            | NA                   | NA                  |
| Total financial system (excl. BCEAO)         |                                |                            |                     |                            |                      |                     |

(1) data for end-2010

**2. Microfinance institutions (MFIs) represent a small but rising share of the financial system and contribute strongly to improving access to finance<sup>2</sup> by lower-income households and SMEs.** The WAEMU has 759 registered MFIs. 61 entities are classified as large institutions with assets or deposits above CFAF 2 billion and are supervised by the Banking Commission. These account for 90 percent of the MFI sector's assets. Although significantly smaller than the banking system—MFIs' total loans amount to about 8 percent of total bank credit—more people, particularly in rural areas, have accounts at MFIs than at banks, which helps raise overall access to the financial system from 5 to about 15 percent of the population. In countries such as Benin, Senegal, and Togo, MFIs have helped lift the overall access ratio to more than 20 percent of the population (see Benin and Senegal pilots<sup>3</sup>). Most

<sup>1</sup> This section describes mostly aggregate results at the WAEMU level. They may mask significant heterogeneity across countries.

<sup>2</sup> Access to finance refers to the possibility that individuals or enterprises can access [financial services](#), including [credit](#), [deposit](#), [payment](#), [insurance](#), and other [risk management](#) services (Demirgüç-Kunt et al. 2008).

<sup>3</sup> Benin: 2012 Article IV Consultation and Fourth Review Under the Extended Credit Facility Arrangement—Staff Report and Staff Supplements, IMF Country Report No. 13/9.

(continued)

MFIs are operated as mutuals or by civil society organizations (CSOs) and have a social mandate, such as lending to farmers in remote regions. Overall, the sector is profitable but many of the smaller networks are loss-making and rely heavily on donor financing. More detailed analysis on MFIs is presented in Section I.C.

**3. The regional financial markets remain a marginal source of funding except for the governments.** The regional stock market, based in Abidjan, has 37 quoted companies as of end-2012. Only 11 initial public offerings took place between 1998 and 2011. Its capitalization is small (about 12 percent of the WAEMU GDP in 2012). Companies listed are mostly in the financial and industrial sectors; Sonatel (a Senegalese telecom company) and Ecobank (a regional bank, headquartered in Togo) are the largest two companies, accounting for close to 50 percent of market capitalization. The debt market consists mostly of government paper and is small (about 10 percent of the WAEMU GDP in 2012). There is no significant secondary debt market, including for government paper. More detailed analysis on the regional financial markets is presented in Section I.D.

## B. The Banking Sector

**4. The banking sector has expanded in recent years.** Bank credit to the economy has increased substantially in most countries since the mid-2000s (Figure 1). This trend continued in 2012, taking the ratio to GDP to about 20 percent, from 14 percent in 2010 (with an average credit growth rate of 6 percent annually). The number of bank branches and bank accounts also increased significantly in recent years. Credit is largely short-term, and goes mostly to manufacturing and the service sector (particularly trade, hotels and restaurants). Clients vary substantially across banks, with some dealing mostly with bigger firms (including subsidiaries of multinationals in the case of foreign-owned banks) and others are more focused on domestic retail clients. In some countries, increased competition from MFIs and new business strategies from entrants have led to diversification of the banks' traditional customer base and higher competition. Most banks are significantly exposed to government securities and more generally to the public sectors.

**5. An important recent development has been the emergence in the WAEMU of cross-border (pan-African) banking groups.** This has often occurred through the purchase of domestic banks, in particular by Moroccan and Nigerian groups seeking to expand out of their home markets. Twenty large groups, accounting for most of the banking system, are involved in cross-border activities within the WAEMU (Figure 1). These groups, which are mostly incorporated as subsidiaries, are funded through local deposits. This funding model, coupled with their domestic orientation, explains why the direct impact of the global crisis was rather mild on these banks. European banks have remained engaged in the region, while pan-African banking groups have taken the opportunity to expand.

**6. At this juncture, however, banking in the WAEMU is still conducted within national borders.** Cross-border flows to households or corporations within the region are largely in the form of syndicated loans involving a sister bank located in the country of the client; in the recent period Côte

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Senegal: Staff Report for the 2012 Article IV Consultation, Fourth Review Under the Policy Support Instrument, and Request for Modification of an Assessment Criterion—Staff Report and Supplements, IMF Country Report No. 12/337.

d'Ivoire and Senegal were net recipients of these flows, while most other countries were net exporters. The flows are still relatively small, at about 1.6 percent of total lending in 2012. Limited integration is also attested by large differences in lending and deposit rates for households and enterprises across countries. Limited banking integration reflects a number of factors, such as the still limited economic integration, but also the importance of local knowledge for lending activities. The main cross-border financial flows in the WAEMU involve bank purchases of government paper.

**7. On average, the banking system is liquid and well capitalized, although the situation varies substantially across banks and countries** (Box 1, Figure 2, and Text Table 1). As mentioned above, banks are very heterogeneous with regard to business models, size, geographical coverage, profitability, and vulnerabilities. Aggregate information hides this diversity and therefore needs to be complemented by a more granular approach. The analysis of financial soundness indicators (FSIs—which are highly aggregated, available with long lags, and backward looking) and the results of the stress-tests (which rely on bank-by-bank data) confirm the need for a dual approach. Both lending concentration, which is high in all countries of the region, and quality of assets, as reflected in high gross NPLs, represent the main risks. Lack of data regrettably did not allow assessing risks related to the exposure of banks to WAEMU sovereigns, but this exposure is clearly increasing, raising new (possibly systemic) risks.<sup>4</sup> The broader exposure of banks to the public sectors (e.g., through public enterprises) is even more substantial. The emergence of cross-border banking groups also brings new risks; for instance, cross-border banks may propagate foreign shocks into the domestic economy. Another potential risk arises when large banking groups have similar portfolios making them susceptible to similar shocks; in this case, while the diversification of the banking portfolio reduces the probability of an idiosyncratic failure, it increases the probability of a systemic crisis. Some of these banking groups are large enough to be considered domestic systemically important financial institutions (D-SIFIs).

**8. Compliance with prudential norms remains low for a number of ratios.** As shown in Figure 1, compliance varies across countries and across ratios. Also, there are banks in all countries breaching the capital adequacy ratio (lack of granular data did not permit to scale the compliance of prudential ratio by banks' assets). Compliance improved in late 2012, but this reflected changes made to two ratios (the transformation ratio, which was lowered from 75 to 50 percent; and the ratio on portfolio structure, which was abolished). Progress over the last few years has been limited, which suggests a degree of regulatory forbearance. In addition, some of these norms are not in line with international standards. Low compliance is particularly problematic for ratios which are less demanding than international standards, such as the one on risk division (see below). As discussed in the last section, there are other important issues to address with regard to the supervision of regional groups and the crisis prevention and resolution frameworks.

<sup>4</sup> The Senegal study showed that smaller banks in Senegal were highly exposed to sovereign risk.

### Box 1. Banking System Soundness: Findings from the Stress Tests

**In collaboration with the authorities, stress-tests were performed on the banking systems of 7 of the 8 WAEMU countries.** Data for Guinea Bissau were not available. The stress tests were based on end-2011 data; for two countries, granular data were only available for end-2010. The stress tests covered all banks—public, private, and foreign owned—and tested for market risk, credit risk and interest rate risk. Stress tests were not performed for exchange rate risks, given the credible peg to the euro, and for sovereign risks because of insufficient data. The lack of recent and comprehensive data is an important limitation to the use of stress tests for crisis prevention purposes. The tests performed did not incorporate macroeconomic feedbacks and other second round effects, and assumed no policy response. The stress tests calibrated a series of large but plausible shocks, which comprised sectoral risks, including default by the largest individual borrower, interest rate spikes of 500 bps, as well as liquidity shocks—deposit runs with losses of 5 percent of deposits per day for 10 days.

**The results illustrated some of the known strengths and vulnerabilities of the system.**

- **Limited interest rate risk.** As the asset side of banks' portfolio is typically short-term in nature—reducing maturity mismatches—and bonds are typically held until maturity, banks in most countries are resistant to large changes in interest rates.
- **Limited liquidity risk.** With large liquidity buffers in most banks, only smaller ones face liquidity risks.
- **Severe sectoral/company concentration.** The lack of economic diversification and the large informal sector lead banks to concentrate lending on only a few sectors and corporations. In the WAEMU, the 50 largest companies account for 1/3 of total bank credit. This is a major vulnerability for banks, and the risk can be systemic if banks are substantially exposed to the same large borrower (like ICS in Senegal a few years ago).
- **Weak asset quality.** While varying across banks, the generally weak quality of assets is reflected in large NPL ratios (even after accounting for provisioning). Local accounting rules take longer to write-off NPLs compared to most jurisdictions, with some of these NPLs likely to be old and potentially reflecting difficulties in exercising guarantees through the judicial system. Data on NPL flows were not available to assess recent trends.

**Other vulnerabilities, known but not explored in the stress tests, include:**

- **Political instability.** This risk is high in the region, as shown by the crises in Côte d'Ivoire, Mali and Guinea-Bissau in the past 2-3 years.
- **Weather-related risks.** Given the still important role of the agricultural sector in the economy, climate hazards (floods, droughts, etc.) subject the system to large, exogenous shocks.
- **Sovereign-bank relationship:** WAEMU banks hold over 70 percent of public debt issued by WAEMU sovereigns, and cross-border holdings are sometimes large. In the case of Côte d'Ivoire in late 2010 (when the crisis started), more than half of the debt was held by residents of other WAEMU countries, generally banks. A default on this debt could have created a systemic bank crisis in the region.

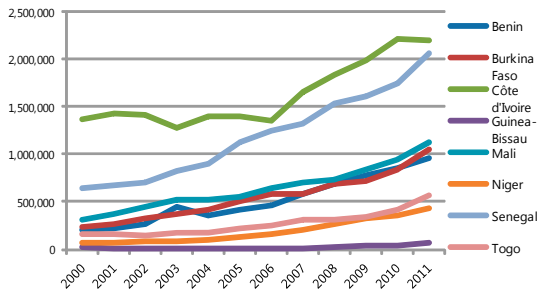
**Table. WAEMU: Financial Soundness Indicators 2005–2012**

|   | 2005                                     | 2006  | 2007  | 2008  | 2009  | 2010  | 2011  | 2012  |
|---|--|-------|-------|-------|-------|-------|-------|-------|
|   | Dec.                                     | Dec.  | Dec.  | Dec.  | Dec.  | Dec.  | Dec.  | Jun.  |
|   | (in percent, unless otherwise indicated) |       |       |       |       |       |       |       |
| <b>Solvency ratios</b>                              |  |       |       |       |       |       |       |       |
| Regulatory capital to risk weighted assets          | 9.17                                     | 8.36  | 6.75  | 9.79  | 10.16 | 11.09 | 10.72 | 10.99 |
| Tier I capital to risk-weighted assets              | 8.78                                     | 7.98  | 6.01  | 9.37  | 9.80  | 10.55 | 10.08 | 10.59 |
| Provisions to risk-weighted assets                  | 14.98                                    | 14.17 | 12.75 | 12.24 | 10.96 | 12.05 | 10.40 | 12.49 |
| Capital to total assets                             | 5.82                                     | 5.45  | 4.29  | 6.07  | 6.20  | 6.41  | 6.48  | 5.71  |
| <b>Composition and quality of assets</b>            |  |       |       |       |       |       |       |       |
| Total loans to total assets                         | 63.44                                    | 61.91 | 59.06 | 59.41 | 57.56 | 55.27 | 55.17 | 55.29 |
| Gross NPLs to total loans                           | 19.90                                    | 20.50 | 18.90 | 19.20 | 17.20 | 17.58 | 15.92 | 16.17 |
| Provisioning rate                                   | 66.88                                    | 66.17 | 65.74 | 68.05 | 61.45 | 63.68 | 64.23 | 64.96 |
| Net NPLs to total loans                             | 7.60                                     | 8.00  | 7.40  | 7.10  | 7.40  | 7.19  | 6.35  | 6.33  |
| Net NPLs to capital                                 | 82.74                                    | 91.17 | 90.85 | 69.00 | 68.54 | 61.99 | 54.07 | 61.33 |
| <b>Earnings and profitability</b>                   |  |       |       |       |       |       |       |       |
| Average cost of borrowed funds                      | 2.10                                     | 2.20  | 2.40  | 2.60  | 2.50  | 2.90  | 2.40  | ...   |
| Average interest rate on loans                      | 9.70                                     | 8.80  | 9.90  | 10.60 | 10.10 | 10.90 | 9.60  | ...   |
| Average interest margin <sup>1</sup>                | 7.60                                     | 6.60  | 7.50  | 8.00  | 7.60  | 8.00  | 7.20  | ...   |
| After-tax return on average assets (ROA)            |  |       |       |       |       | 1.11  | 1.19  | ...   |
| After-tax return on average equity (ROE)            | 5.20                                     | 4.80  | 4.80  | 1.90  | 14.80 | 12.63 | 13.67 | ...   |
| Noninterest expenses/net banking income             | 57.90                                    | 60.75 | 62.64 | 60.91 | 63.79 | 64.75 | 61.63 | ...   |
| Salaries and wages/net banking income               | 26.50                                    | 27.75 | 27.57 | 26.50 | 27.09 | 27.11 | 26.37 | ...   |
| <b>Liquidity</b>                                    |  |       |       |       |       |       |       |       |
| Liquid assets to total assets                       | 41.79                                    | 40.89 | 38.13 | 36.64 | 33.93 | 33.27 | 33.59 | 33.25 |
| Liquid assets to total deposits                     | 55.15                                    | 54.41 | 50.95 | 50.43 | 46.04 | 45.12 | 46.07 | 46.61 |
| Total loans to total deposits                       | 83.76                                    | 82.38 | 78.89 | 81.76 | 78.45 | 83.97 | 84.29 | 86.59 |
| Total deposits to total liabilities                 | 75.74                                    | 75.15 | 74.87 | 72.66 | 73.37 | 74.12 | 72.91 | 71.35 |
| Sight deposits to total liabilities <sup>2</sup>    | 38.17                                    | 37.89 | 38.41 | 36.90 | 36.07 | 36.66 | 37.79 | 36.72 |
| Term deposits to total liabilities                  | 37.57                                    | 37.26 | 36.45 | 35.76 | 37.30 | 37.46 | 35.11 | 34.63 |
| <b>Source:</b> BCEAO. Simple average.               |  |       |       |       |       |       |       |       |
| <b>Note:</b> Simple averages of country indicators. |  |       |       |       |       |       |       |       |
| <sup>1</sup> Excluding tax on bank operations       |  |       |       |       |       |       |       |       |
| <sup>2</sup> Including saving accounts              |  |       |       |       |       |       |       |       |

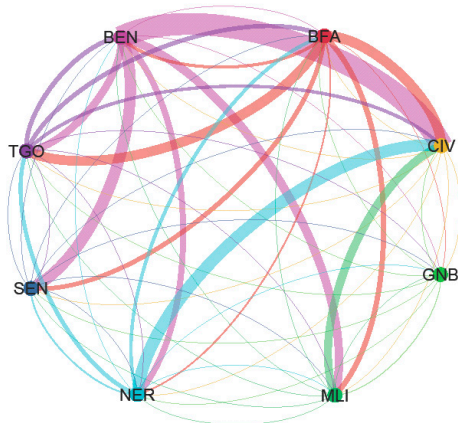
**Figure 1: WAEMU: Evolution of the Banking Sector**

Outstanding credit by the banking system has grown steadily in all WAEMU countries...

**Outstanding Credit, 2000-2011**  
(CFAF million)



Inter-regional cross-border banking liabilities, however, remained small, with lending flows mainly to Senegal and Côte d'Ivoire ...



Note: The links indicate net lending flows originating from the country with the same-color nod.

Banking groups have evolved in the region and are expanding rapidly.

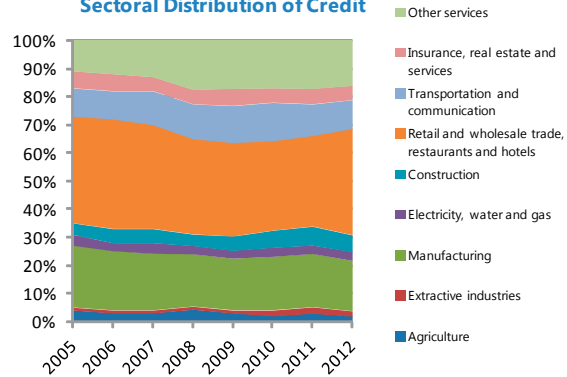
**Main Banking Groups in the WAEMU**

| Group                  | Presence in countries | Market share (%) | Number of agencies | Number of accounts |
|------------------------|-----------------------|------------------|--------------------|--------------------|
| Ecobank (ETI)          | 8                     | 15.3             | 225                | 1,131,339          |
| Société Général        | 4                     | 11.2             | 129                | 524,584            |
| Bank of Africa Group   | 6                     | 10.1             | 145                | 573,827            |
| Attijariwafa Bank      | 4                     | 8.7              | 210                | 571,078            |
| BNP Paribas            | 7                     | 7                | 176                | 362,658            |
| ABI (Ex-AFG)           | 4                     | 6.2              | 81                 | 442,144            |
| United Bank for Africa | 4                     | 3.3              | 59                 | 212,941            |
| BSIC                   | 7                     | 2.4              | 73                 | 68,649             |
| <b>Total</b>           |                       | <b>63.9</b>      | <b>1,098</b>       | <b>3,887,220</b>   |

Source: BCEAO, Banking Commission of the WAEMU and IMF staff calculations

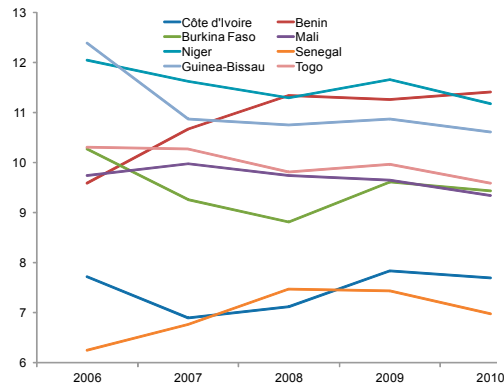
...with the largest share allocated to retail and whole sale trade.

**Sectoral Distribution of Credit**



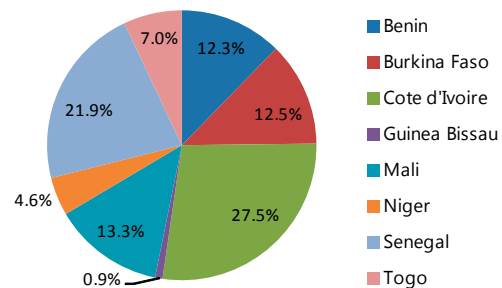
... and limited convergence of cross-country lending rates implying limited integration.

**Lending Rates by Country, 2006-2010**



Côte d'Ivoire remains the largest market in terms of bank assets, closely followed by Senegal.

**Distribution of Bank Assets by Country, 2011**

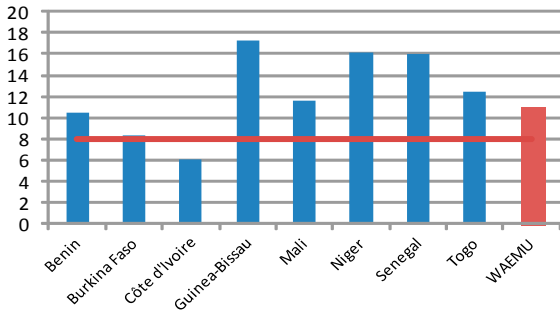




**Figure 2. WAEMU: Financial Soundness**

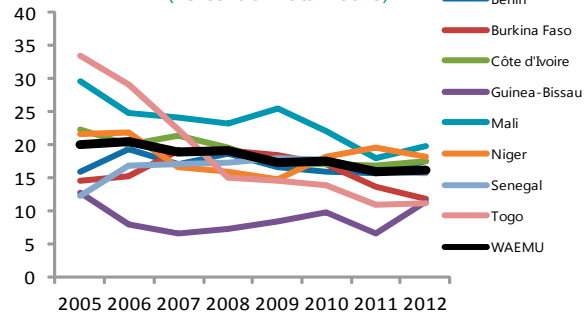
Although the banking sector appears well capitalized overall, banks in Côte d'Ivoire are significantly undercapitalized on average.

**Capital Adequacy Ratio, June 2012**



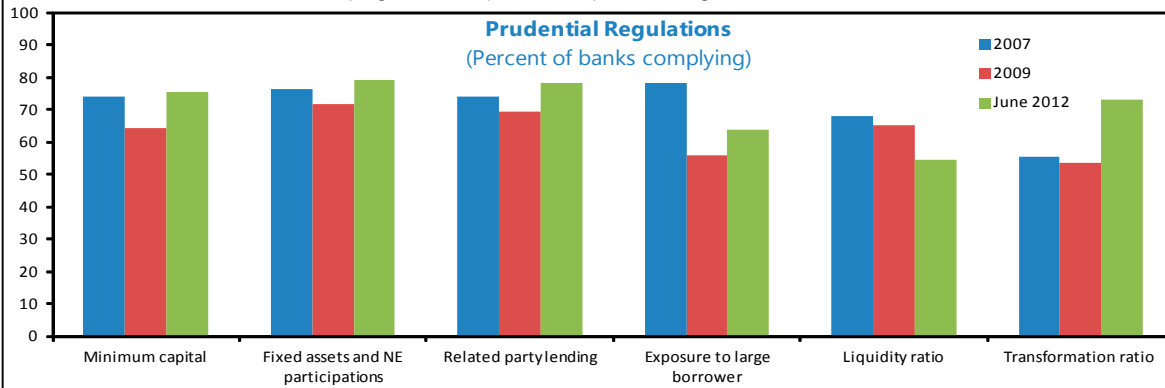
Non performing loans are high albeit trending downwards for some countries...

**Non-Performing Loans, 2005-2012**  
(Percent of Total Loans)



... and progress in compliance with prudential regulation has been limited.

**Prudential Regulations**  
(Percent of banks complying)



**Respect of Prudential Norms by Country, end-June 2012**

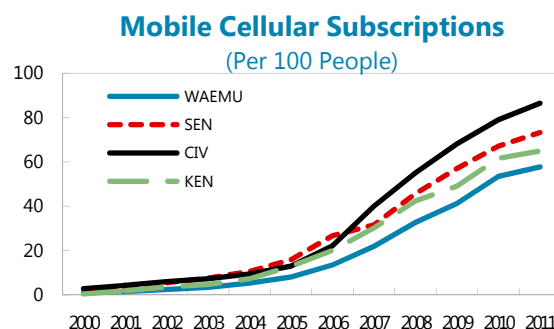
| Number of Banks per country | Solvency Ratios |                                    | Other Prudential Ratios    |                    |                       |                           |                 |
|-----------------------------|-----------------|------------------------------------|----------------------------|--------------------|-----------------------|---------------------------|-----------------|
|                             | Capital ratio   | Fixed assets and NE participations | Exposure to large borrower | Concentration risk | Related Party Lending | Transformation ratio >50% | Liquidity ratio |
| Benin (12)                  | 10              | 9                                  | 5                          | 10                 | 9                     | 5                         | 7               |
| Burkina (12)                | 9               | 10                                 | 6                          | 10                 | 11                    | 10                        | 7               |
| Côte d'Ivoire (23)          | 13              | 16                                 | 12                         | 16                 | 16                    | 11                        | 18              |
| Guinea Bissau (4)           | 3               | 3                                  | 3                          | 3                  | 3                     | 2                         | 1               |
| Mali (13)                   | 12              | 11                                 | 9                          | 12                 | 10                    | 7                         | 5               |
| Niger (10)                  | 7               | 8                                  | 8                          | 8                  | 8                     | 5                         | 3               |
| Senegal (19)                | 16              | 18                                 | 14                         | 18                 | 16                    | 8                         | 10              |
| Togo (12)                   | 9               | 8                                  | 10                         | 9                  | 9                     | 4                         | 6               |
| WAEMU (105)                 | 79              | 86                                 | 65                         | 87                 | 82                    | 52                        | 57              |

Sources: BCEAO, IMF, African Development database, and Regional Economic Outlook database.

Note: The transformation ratio (stable resources/M&L term loans) was lowered from 75 percent to 50 percent early 2013, the data reported for 2012 takes the 50 percent into account.

### Box 2: Mobile Banking in the WAEMU

**Mobile banking has not picked up significantly in the WAEMU.** Mobile banking in East Africa has greatly improved access to finance, in particular in remote rural areas. While the number of mobile phone subscriptions in the WAEMU is comparable to that in East Africa—with Côte d'Ivoire and Senegal even outperforming Kenya—mobile banking services in the WAEMU have not followed a similar trajectory. Despite the regional consultation organized by the BCEAO on mobile banking in 2011—after which the BCEAO created the legal framework and set up an action plan—there appears to be limited interest by the private sector in engaging this market. Only one bank has acquired a mobile banking license and a second license is held by a telephone company. According to the BCEAO, MFIs (which lack a license for money transfer) have not shown interest in participating in the distribution process either. This is a conundrum as this activity could be very profitable.



**Mobile banking costs are generally higher for clients in the WAEMU and services are more limited.** Although amounts below \$10 can be transferred at lower costs in selected West African countries than in Kenya, costs are higher for transfers above \$50. Fees diverge significantly for (relatively) large transfers: mobile banking clients in Senegal pay 10 times more than clients in Kenya (using M-Pesa) for a transfer of equivalent to \$200. The fee for withdrawing funds is much more expensive for larger amounts in the WAEMU. Interestingly, the payment schedule adopted by Orange Kenya is closer to M-Pesa's than that of its West African sister companies. Also, while Kenya's M-Pesa allows for sending money to outside its network (at a surcharge), this option is not offered in the WAEMU.

### Kenya and WAEMU: Mobile Banking Fees, 2013

|                                       | Kenya    |        | WAEMU          |                   |
|---------------------------------------|----------|--------|----------------|-------------------|
|                                       | M-Pesa   | Orange | Orange Senegal | Orange Cote d'Iv. |
|                                       | (in USD) |        |                |                   |
| Transaction Amount (USD) <sup>1</sup> |          |        |                |                   |
| 0.15                                  | 0.03     | N/A    | N/A            | 0.21              |
| 1                                     | 0.06     | N/A    | 0.03           | 0.21              |
| 5                                     | 0.29     | 0.34   | 0.15           | 0.21              |
| 10                                    | 0.34     | 0.34   | 0.30           | 0.21              |
| 100                                   | 0.57     | 0.34   | 3.00           | 1.03              |
| 200 <sup>2</sup>                      | 0.57     | 0.34   | 6.00           | 2.07              |
| 800 <sup>3</sup>                      | 1.14     | 0.46   | N/A            | 3.10              |
| Withdrawal Amount (USD)               |          |        |                |                   |
| 0.15                                  | N/A      | N/A    | 0.01           | 0.31              |
| 1                                     | 0.11     | N/A    | 0.04           | 0.31              |
| 5                                     | 0.29     | 0.29   | 0.20           | 0.31              |
| 10                                    | 0.29     | 0.29   | 0.40           | 0.31              |
| 100                                   | 1.14     | 0.86   | 4.00           | 2.07              |
| 200 <sup>2</sup>                      | 1.83     | 1.66   | 8.00           | 4.13              |
| 800 <sup>3</sup>                      | 3.43     | 2.57   | 32.00          | 16.53             |

Source: Companies website, IMF staff calculations

<sup>1</sup> Transaction to subscribed user of the same telecommunication company. Only M-Pesa and Orange Money Kenya allow for transfer to non-registered users at a surcharge.

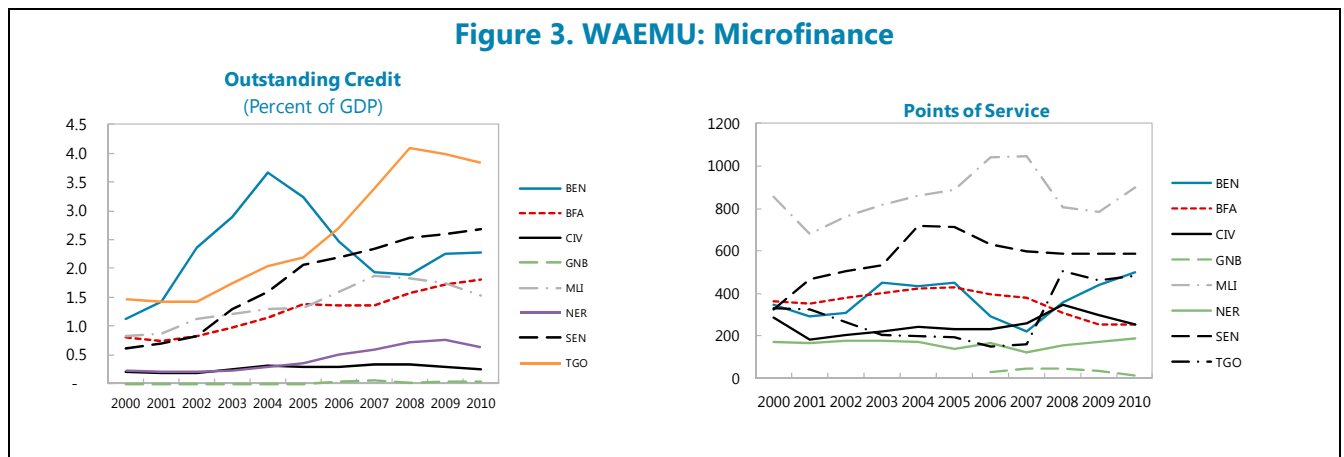
<sup>2</sup> Maximum amount of Orange Money Senegal

<sup>3</sup> Maximum amount of M-Pesa. The maximum amount of Orange Kenya is USD 1,140 and of Orange CIV USD 1,000.

## C. Microfinance

### 9. Following a rapid expansion, the microfinance sector is consolidating in many countries.

The quick expansion of microfinance networks in the early 2000s was welcome from the perspective of access to finance<sup>5</sup>. However it led to a proliferation of often small and unprofitable MFIs, which have partially operated out of the authorities' control. Consolidation is ongoing in most countries both through mergers and acquisitions amongst MFIs and at the initiative of the authorities. Some countries are well advanced in the consolidation process—more than 100 institutions have been closed in Senegal—while others still registering existing networks – a survey conducted in Benin in 2011, for example, revealed that 721 MFIs were operating then in the country but only 226 were licensed. Overall, the number of branches or points of service in the WAEMU has remained broadly constant since 2004. Outstanding credit, however, has increased significantly in most countries (see Figure 3). Microfinance is particularly developed in Senegal (see Senegal pilot for a more detailed description).



### 10. The authorities have started to address governance and profitability problems of the sector.

The MFI sector is profitable overall, but the situation varies greatly depending on the size of the institutions, with the largest being the most profitable; NPLs are on an increasing trend and governance problems are frequent due to a lack of accountability.<sup>6</sup> A regulatory reform initiated in 2008–09 has led to a reorganization of supervisory responsibilities, with the larger institutions holding assets and/or deposits of more than CFAF 2 billion now supervised by the WAEMU Banking Commission. Smaller institutions remain supervised by national authorities, typically ministries of finance, and countries have started to build up their capacity in this area. Many MFIs report access to refinancing as a major issue given their relatively high transformation ratio, short term resources (cash deposits) and an increasing demand for longer term financing. Larger MFIs are able to get refinancing from banks, and these loans have recently become eligible for refinancing at the BCEAO; however, smaller MFIs cannot avail themselves of this option. The BCEAO is also considering how to include MFIs in the payment system as the current MFI license does not allow for money transfer. Mobile banking is just starting in the WAEMU (Box 2).

<sup>5</sup> For example in Benin, authorized MFIs serve 1.5 million customers in a total active population of 4.5 million.

<sup>6</sup> This follows from the mutual structure which raises collective action problems particularly for institutions with a large number of members. Also management skills and training seem less developed than in the banking system.

## D. Regional Markets

**11. Despite signs of development, interbank market activity remains limited.** Interbank loans have amounted to less than 2 percent of total bank loans in the past five years. Loan maturity has tended to increase in recent years and the slope of the implicit, yet imperfect, yield curve has become positive; it was virtually flat a decade ago. Moreover, the interbank rate has remained broadly within the policy rate corridor since 2009 (Figure 4). However, the interbank market does not yet perform a major role in the reallocation of liquidity. Despite excess reserves at the banking system level, the BCEAO still needs to inject massive amounts of liquidity to a large number of banks that cannot get this liquidity from the market. This phenomenon is another illustration that the banking system is highly heterogeneous and segmented. In the absence of collateralized operations, highly liquid banks—in general, though not exclusively the subsidiaries of large foreign banks, which also happen to be the more profitable ones—are reluctant to lend to others. As a result, most interbank loans take place within banking groups, to avoid any counterparty risk. Because access to the BCEAO's standing facility for liquidity provision is not yet fully electronic and therefore entails significant transaction costs, some operations on the interbank market still take place at rates greater than the higher policy rate of the BCEAO. These operations may also reflect implicit profit transfers between banks belonging to a same group.

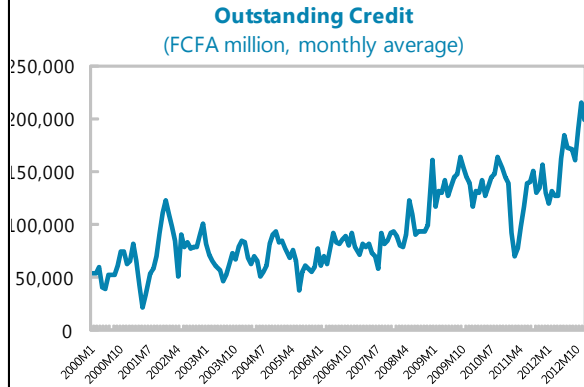
**12. The regional debt market has developed rapidly in the past years, mostly for government paper** (Figure 5). Securities can be issued by private companies and governments on the regional stock exchange (referred to as BRVM, its French acronym). The BRVM has 46 bond lines, of which 28 are from private issuers and the rest from 4 sovereigns. Government bond issues represented 75 percent of all issuance by syndication in 2011, with Côte d'Ivoire and Senegal the most active issuers. The average interest rate on sovereign bonds was at 6.7 percent in 2011 (average duration 5.5 years), while the average interest rate on listed bonds issued by private corporations was 6.8 percent (at similar duration). Interest rates, however, do not provide a full account of differences in the cost of financing between the public and private sector. Private sector issuance required until recently a 100 percent guarantee by a certified institution (e.g. BOAD), which added the equivalent of 1-2 percentage points to issuance costs. Overall, the BRVM debt market remains small. Its total capitalization stood at about 2 percent of GDP at end-2012. It is not a significant source of financing for the private sector. There is no significant secondary market.

**13. Most government debt, however, is still issued to banks through auctions organized by the BCEAO.** This segment has been very dynamic in recent years and outstanding government debt issued on this market is about ten times larger than that issued at the BRVM. Debt issued this way is mostly in the form of T-Bills; it has a relatively short average maturity and can be used for refinancing at the BCEAO. There is no significant secondary market for this type of government debt.

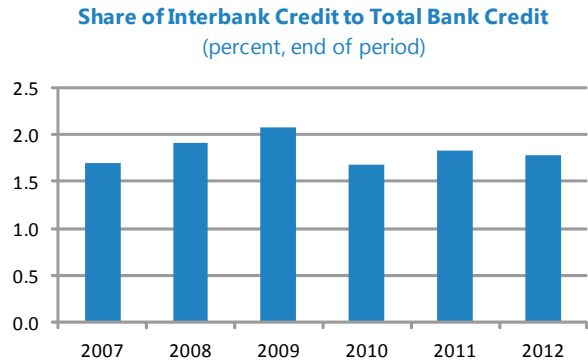
**14. The regional equity market remains shallow** (Figure 6). Launched in 1998, the BRVM started off with 36 listed companies carried over from the previous stock exchange in Abidjan. The number of companies listed has remained broadly stable, with 37 in early 2013, as new listings broadly offset the number of companies taken off the list. Market capitalization increased from 4.3 percent of GDP in 2002 to 10.1 percent of GDP in 2012. Foreign investors are allowed in, and their stakes in Sonatel and ETI (Ecobank) are reportedly fairly large. The average market return in 2011 was 8.6 percent in local currency, and 27 companies paid dividends. BRVM is supervised by the regional council for public savings and financial markets (referred to as CREPMF, its French acronym).

**Figure 4. WAEMU: Interbank Market**

The amount of outstanding credit has increased from 2007 onwards ...

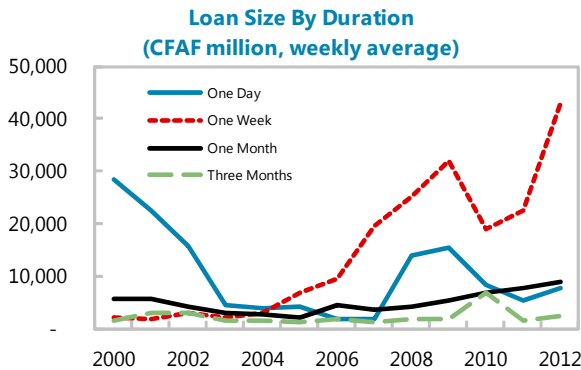


...while the share of credit on the interbank market to total bank credit has remained broadly constant at low levels.

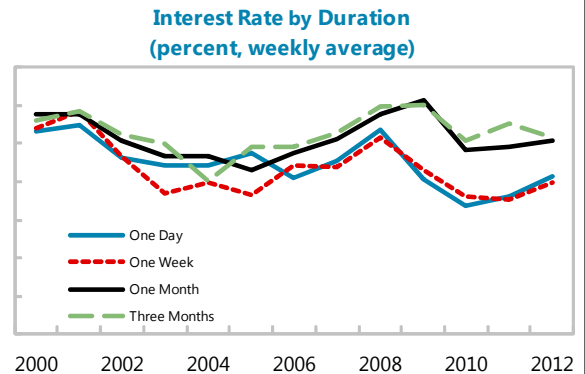


Note: 2012 refers to end September

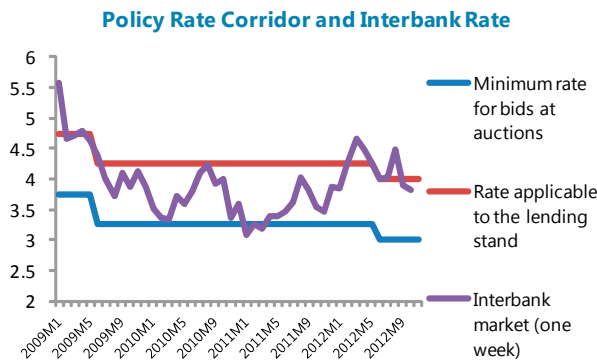
One-day contracts have been replaced with one-week contracts...



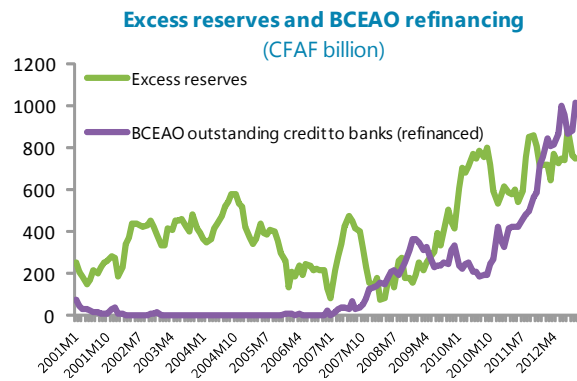
...and interest rates increasingly reflect term structure.



The interbank rate has broadly remained within the policy rate corridor.



However, the interbank market does not sufficiently absorb and reallocate liquidity in the system and banks increase borrowing from the BCEAO.



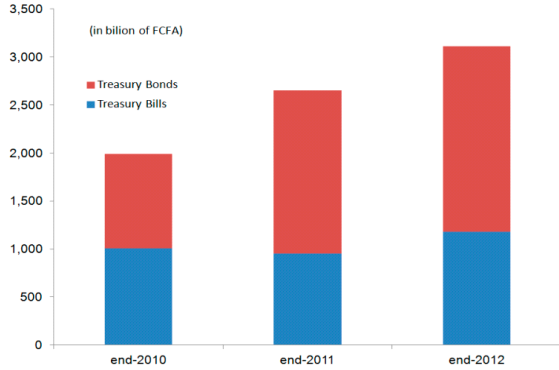
Note: excess reserves are defined as the difference between required reserves and actual reserves at the BCEAO.

Source: BCEAO, IMF staff calculations

**Figure 5. WAEMU: Debt Markets**

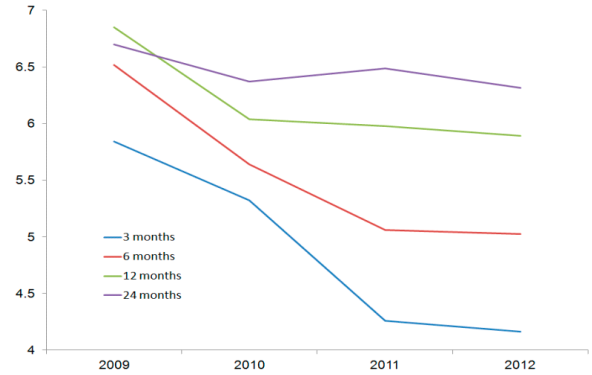
The stock of longer term debt is on the rise...

**Bond and T-Bill Issuances by Auction, 2010-2012**



...with the average cost of borrowing on the decline.

**Interest Rates by Maturity, 2009-2012**



Cote d'Ivoire dominates the few issuances by syndication...

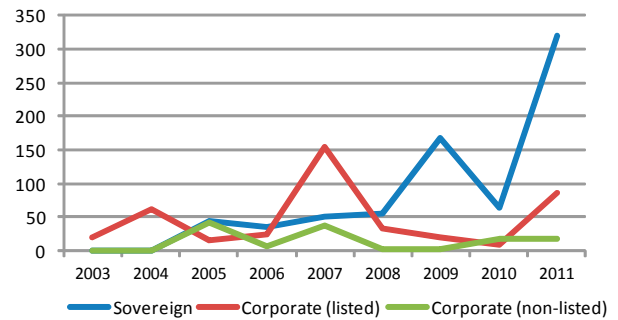
**Sovereign Issuances by Syndication, 2003 - 2011**

| Country        | Interest Rate (in percent) | Amount (FCFA bn) | Duration (years) | Year of subscription |
|----------------|----------------------------|------------------|------------------|----------------------|
| Senegal        | 5.50                       | 45.0             | 5                | 2005                 |
| Togo           | 6.50                       | 36.3             | 5                | 2006                 |
| Cote d'Ivoire  | 6.00                       | 51.7             | 3                | 2007                 |
| Senegal        | 5.50                       | 55.2             | 5                | 2008                 |
| Cote d'Ivoire  | 6.25                       | 61.2             | 4                | 2009                 |
| Cote d'Ivoire  | 6.95                       | 107.3            | 5                | 2009                 |
| Cote d'Ivoire  | 6.25                       | 64.8             | 3                | 2010                 |
| Senegal        | 6.75                       | 76.8             | 5                | 2011                 |
| Cote d'Ivoire  | 7.00                       | 22.9             | 7                | 2011                 |
| Togo           | 6.50                       | 60.0             | 5                | 2011                 |
| Cote d'Ivoire  | 6.50                       | 160.2            | 5                | 2011                 |
| <b>Average</b> | <b>6.34</b>                | <b>67.4</b>      | <b>4.7</b>       |                      |

Source: BRVM

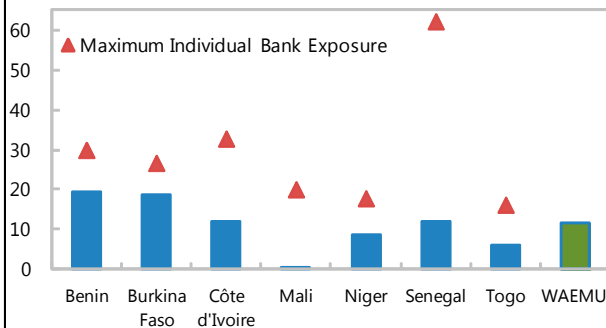
...but corporate issuances risk being crowded out by sovereign activity.

**Debt Issuances by Syndication, 2003-2011 (FCFA bn)**



Exposure of the banking sector to sovereign debt is significant...

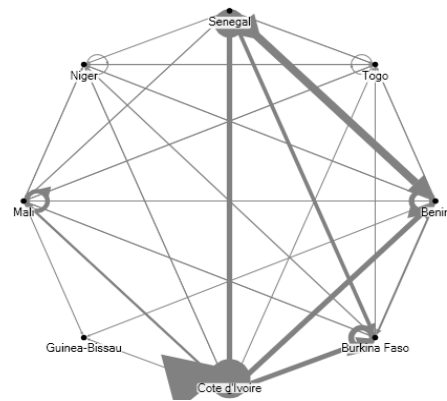
**Government & BCEAO Securities in Bank Balance Sheets, 2011 (Share of Total Bank Assets)**



Source: BCEAO, BRVM, IMF staff calculations

...and extends across borders, with banks from Benin and Senegal financing Ivorian debt.

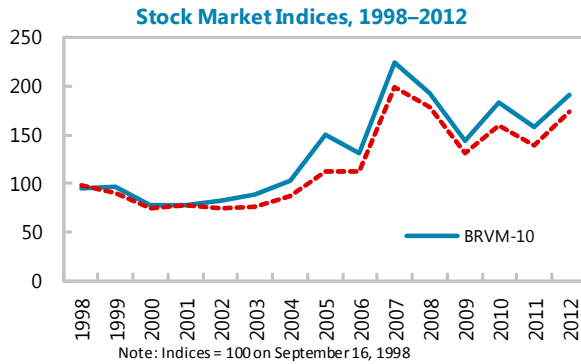
**Crossborder Sovereign-Banking Nexus**



Note: Dots represent the sovereign, and links to dot are purchases of banks from other countries

**Figure 6. WAEMU: The BRVM – Stock Market**

While trending upward both BRVM indices experienced downturns during the global financial crisis and the 2011 Ivorian crisis.



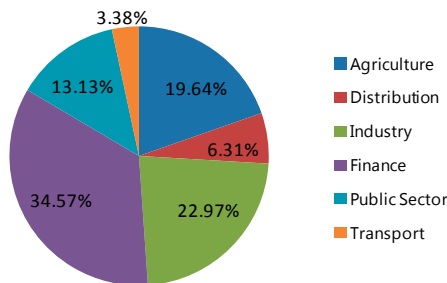
From 1998 to 2012, eleven companies entered the market, mainly in finance and telecommunications...

| Corporations      | Admission to BRVM | Sector            |
|-------------------|-------------------|-------------------|
| SONATEL           | Oct-98            | Telecommunication |
| SIVOA             | Apr-99            | Industry          |
| PALM CI           | Oct-99            | Agriculture       |
| SERVAIR Abidjan   | Mar-00            | Distribution      |
| NEI               | Apr-00            | Industry          |
| BOA-BENIN         | Nov-00            | Finance           |
| BOA-NIGER         | Dec-03            | Finance           |
| ETI               | Sep-06            | Finance           |
| ONATEL            | Apr-09            | Telecommunication |
| BOA-COTE D'IVOIRE | Apr-10            | Finance           |
| BOA-BURKINA FASO  | Dec-10            | Finance           |

Source: BRVM

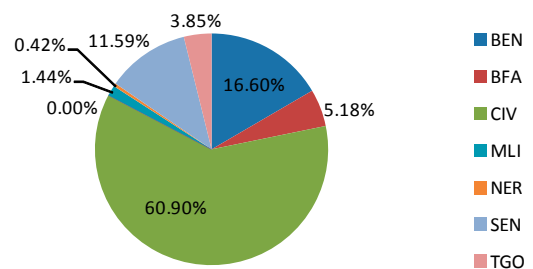
...which leaves capitalization dominated by companies from finance and industry titles, closely followed by agriculture.

**Capitalization by Sector, February 2013**

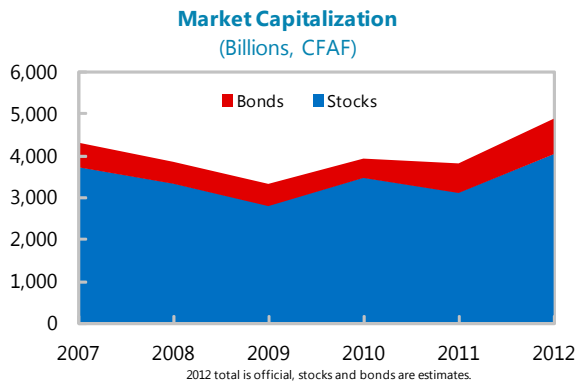


The big majority of investors' accounts is located in Côte d'Ivoire.

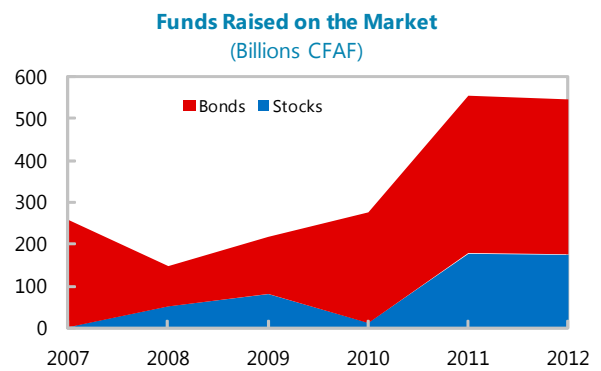
**Accounts by Country, 2011**



Capitalization has increased again in 2012...



...but activity is concentrated on bond issuances, mostly by governments.



Sources: BRVM, CREPMF

## E. Systemic Risk and Surveillance of the Financial System

**15. Systemic risk is defined as any threat of disruption to financial services that is caused by an impairment of all or parts of the financial system and that has the potential to have serious negative consequences for the real economy.** It is a form of negative externality that occurs when a bank failure, market seizure, or breakdown of the infrastructure can have serious adverse implications for market participants. Systemic risk can be decomposed into time-series and cross sectional risk. In the time-series dimension, the build-up of risk over time interacts with the macroeconomic cycle. Financial institutions and borrowers may take on excessive amounts of leverage in the upswing of an economic cycle only to become overly risk-averse in a downswing. This amplifies the boom and bust cycle in the supply of credit and liquidity—and by extension in asset prices—which can be damaging to the real economy. In the cross-sectional dimension, the growing size and complexity of the financial system is raising interconnectedness and common exposures which may increase contagion when problems arise. As a result, the failure of one institution—particularly, one of significant size or with strong interconnections—can threaten the system as a whole.

**16. The Senegal pilot suggests that time-series systemic risk might be limited at this juncture in the WAEMU, though some cross-section risks are present.** No sector seems highly leveraged in Senegal. Banks tend to finance mostly prime borrowers with short-term credit such as trade finance, implying that risks to the financial system, besides from exogenous shocks, are likely to be low, except for concentration risk. Capital inflows and outflows are limited. Many of these features likely apply to other WAEMU countries.

**17. However, some systemic linkages are evolving rapidly that could change this assessment in the near future:**

- **Cross-sector linkages**—those that exist between the financial and non-financial sectors—are on the rise as banks are increasingly lending to sovereigns through the regional market;
- **Cross-border linkages**—those between the financial system of the WAEMU and the world economy, but also those within the WAEMU—are intensifying as large WAEMU banks and foreign banks, especially from Morocco and Nigeria, seek opportunities within the WAEMU and the region.
- **Cross-institution linkages**—those that exist between bank and non-bank financial institutions. The Senegal pilot showed the increasing linkages between banks and insurance companies and MFIs, whether through equity ownership, debt holdings or deposits.

**18. Financial stability in the WAEMU also faces particular challenges.** In a heterogeneous monetary union, business cycle synchronization is limited, as is the case in the WAEMU (see main paper, Appendix IV). In such circumstances, monetary policy may not necessarily act as a stabilizing force to all the national financial systems, as a focus on average regional inflation might imply that monetary policy is too accommodative in some parts of the union that have high inflation levels and too tight in others that have low inflation levels. Limited financial development also means that the scope for countercyclical fiscal policy is reduced, as it may be difficult to issue large amounts of government paper in a shallow market during a downturn (see Senegal pilot), although such policy should play a



critical role in absorbing asymmetric shocks (and even symmetric ones given the limited effectiveness of monetary policy). With limited shock absorption mechanisms, a robust financial crisis prevention and resolution framework is even more critical.

**19. As indicated in the Senegal report, there is in principle a clear division of labor between national and regional authorities on the supervision of the financial system.** The banking sector and MFIs with more than CFAF 2 billion in deposits or loans are supervised by the WAEMU Banking Commission. Smaller MFIs are supervised by national authorities. The regional financial market is under the supervision of CREPMF. Ministries of Finance, together with the regional regulator (CIMA), supervise the insurance sector. Finally, the Financial Stability Committee (FSC) is responsible for macroprudential supervision and to guarantee the stability of the overall financial system at the regional level. As banking licenses are provided by the BCEAO—after a qualified opinion is issued by the WAEMU Banking Commission—following request from the national governments, there is an understanding that banks and subsidiaries that are in trouble will have to be supported by the governments of the countries in which they are located, and not of the country of the parent company.

## INTRA-WAEMU AND INTERNATIONAL COMPARISONS OF FINANCIAL SECTOR DEVELOPMENT

### A. Methodology

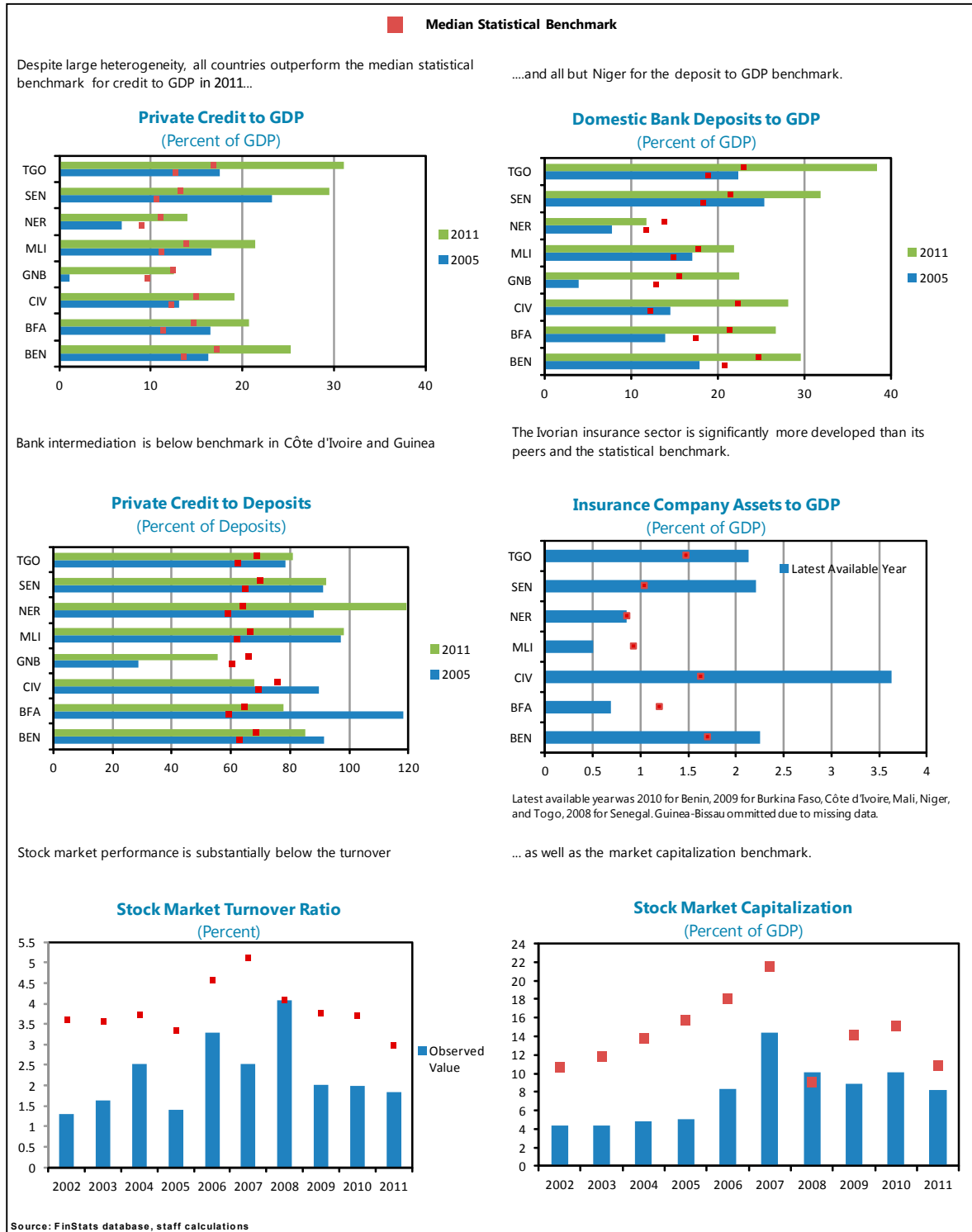
**20. The benchmarking exercise allows an assessment of the zone's financial sector performance with respect to depth, breadth, and access.**<sup>7</sup> For each country and each key financial sector indicator, a structural benchmark is estimated based on the country's economic and structural characteristics.<sup>8</sup> The difference between the observed value and the benchmark then needs to be interpreted. A negative difference suggests scope for policy action, while a positive difference could reflect successful reforms. A positive difference, however, should not be construed as absence of scope for further development; the benchmarks are not optimal levels, but rather an indication of where countries with similar characteristics stand with regard to financial development. The analysis was carried out using data from 1995 onwards, where available, and the tool developed by the World Bank for this purpose.

**21. Comparisons are also made with selected countries outside the WAEMU, namely Ghana and Kenya, as well as the average and median for sub-Saharan Africa (SSA).** The eight financial sectors of the WAEMU were assessed according to their depth, breadth and access to financial services. Ghana is a natural comparator for many WAEMU countries given its characteristics and geographic proximity. Kenya is an example of an SSA economy with a rapidly developing financial sector. The mean and median for SSA (including South Africa) reflect the development of the rest of the continent.

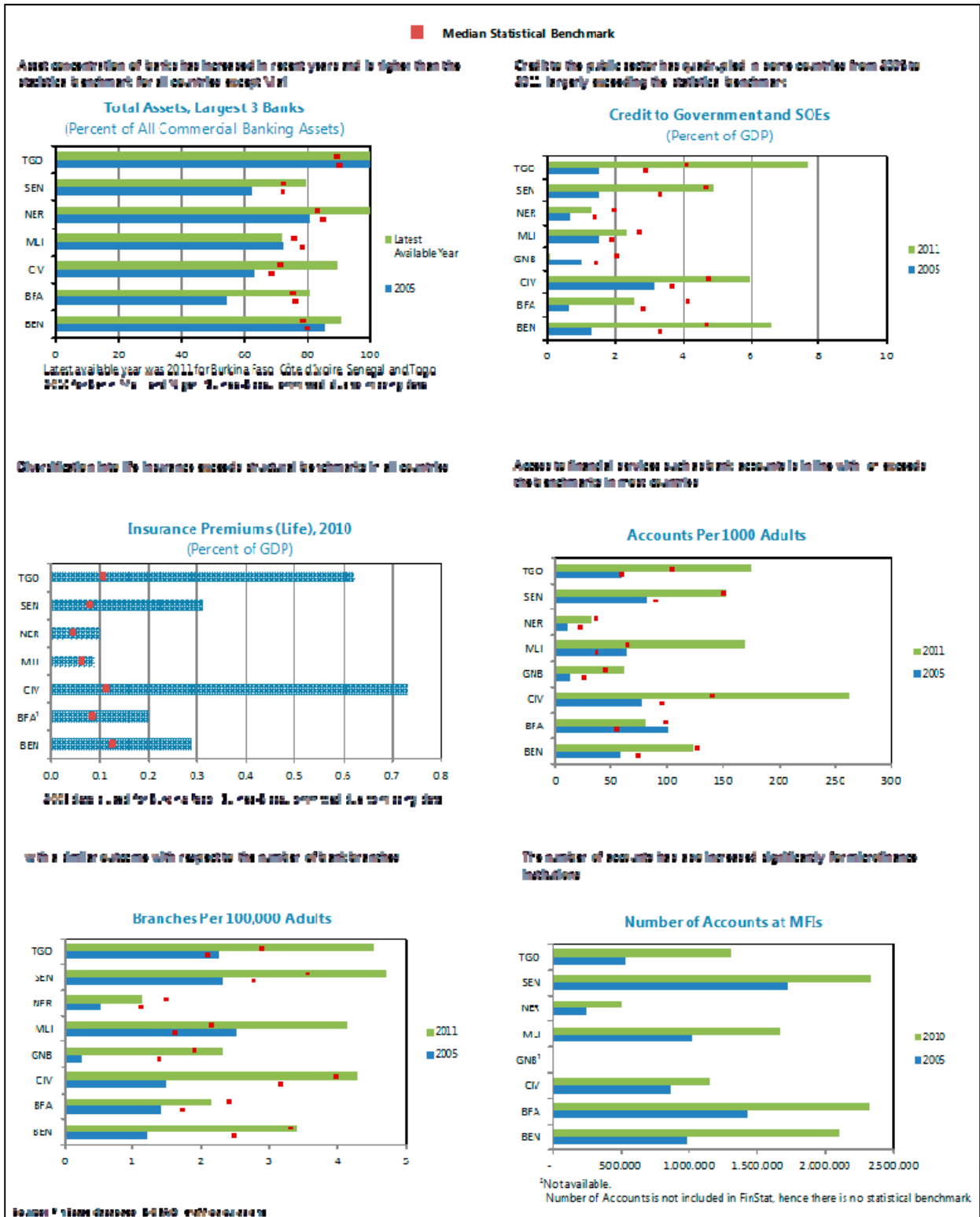
<sup>7</sup> This exercise only considers the banking market, debt and equity markets as well as some non-bank financial institutions. Due to limitations in the dataset, microfinance could not be benchmarked against the statistical median.

<sup>8</sup> The structural benchmarks are calculated based on Al-Hussainy et al. (2010) and FinStats from the World Bank. Using a large dataset of countries, each financial indicator was regressed on a set of structural characteristics, such as GDP per capita and its square, population size and density, the age dependency ratio and country-specific dummies and year fixed effects. These regressions are expected to be updated regularly.

**Figure 7. WAEMU: Selected Indicators on Financial Sector Depth**



**Figure 8. WAEMU: Selected Indicators on Breadth and Access in WAEMU**



## B. Financial Sector Development in the WAEMU and Countries' Structural Characteristics

**22. Banking systems have significantly deepened in all WAEMU countries in recent years and most of them meet or exceed the main statistical benchmarks for depth.** Togo, Senegal and Benin have the deepest banking systems in the region (in absolute terms, not relative to benchmarks), while Guinea-Bissau and Niger have the shallowest ones. Depth of the nonbank financial sectors is very heterogeneous across countries. The equity market is clearly underdeveloped relative to structural characteristics. Figure 7 provides more detail by country and over time.

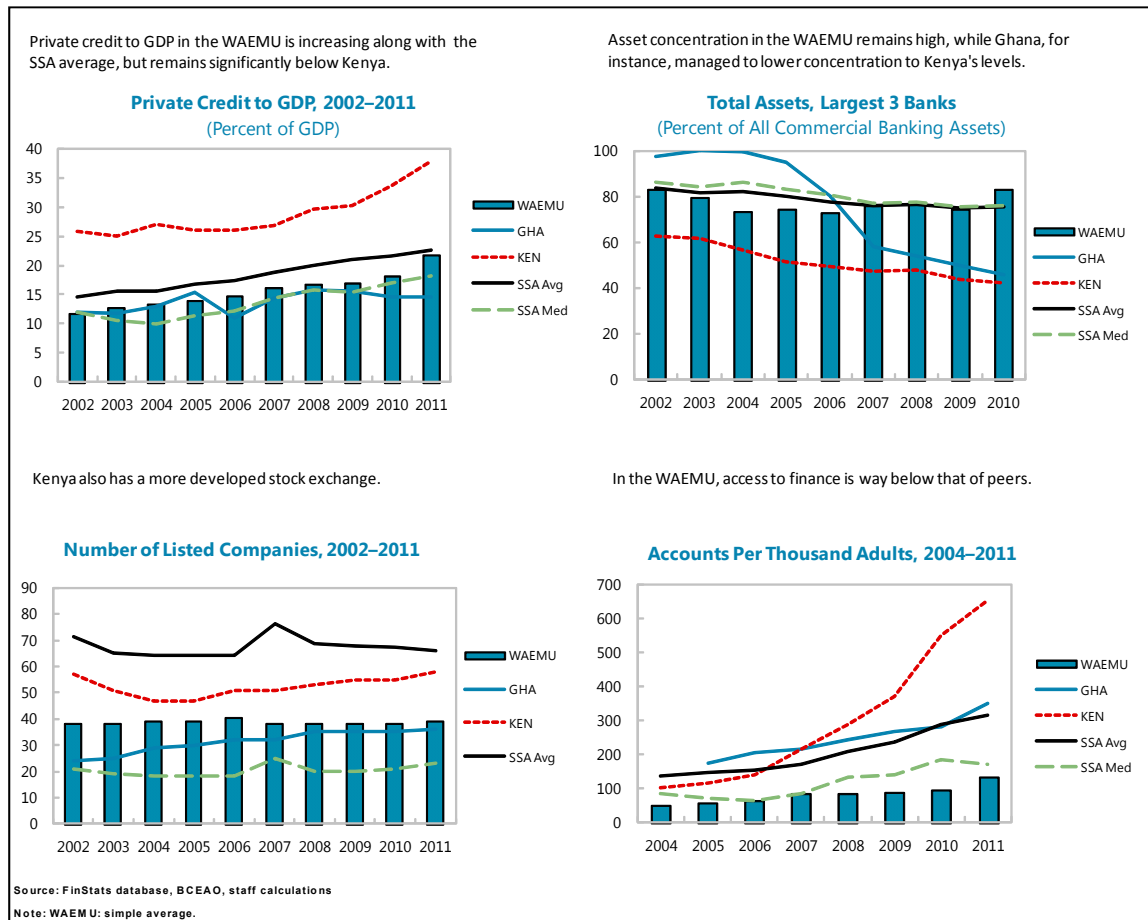
**23. Breadth of the banking sector—assessed through the range of products, markets and providers—is generally limited in the WAEMU.** Competition in the banking system, proxied by the asset concentration of the three largest banks, appears relatively low in all countries and seems to have decreased in recent years. Credit to the public sector to GDP has increased substantially, a trend that is usually not interpreted positively in terms of breadth, but which reflects in the WAEMU the end of central bank advances to governments and the development of the regional market. Life insurance is more developed than indicated by the benchmarks, suggesting diversification of the range of financial products. The number of companies whose stock is listed at the BRVM is very low compared to the benchmark. In addition, active trading is limited to a few of them. Figure 8 provides more detail by country and over time.

**24. Access to finance has increased substantially in all countries and is in line or exceeds structural benchmarks in most of them.** Both banks and MFIs contributed to this development, with MFIs playing an important role in Benin, Togo and Senegal. Figure 8 provides more detail by country and over time.

## C. Scope for Further Deepening

**25. While statistical benchmarking shows that the WAEMU is not lagging in terms of financial sector depth and access, direct comparison to selected peer countries suggests substantial scope for further development.** An agenda for further research would be to understand what drives differences with comparators, and in particular whether certain reforms could be replicated in the WAEMU.

- **Depth.** Private credit to GDP in the WAEMU is on average comparable to the SSA average. It is larger than in Ghana, but significantly lower than in Kenya; in the latter, the increase has also been faster than in the WAEMU.
- **Breadth.** While Ghana has managed to reduce significantly asset concentration in the banking system and has reached a level comparable to Kenya's, concentration remains high in the WAEMU. The stock market is also broader in Kenya.
- **Access.** Access is an area where the WAEMU is lagging behind all comparators. Kenya and, to a lesser extent, Ghana have made impressive progress in this area in recent years.

**Figure 9. WAEMU: Comparing the WAEMU to Selected Benchmark Countries**

## CONSTRAINTS ON MONETARY POLICY FROM SHALLOW FINANCIAL MARKETS

**26. A shallow financial system has important implications for macroeconomic policies in the WAEMU.** First, it limits scope for counter-cyclical fiscal policies. While the regional market has developed substantially, there are limits to the amounts governments can raise on it. This is a significant constraint since fiscal policy is the main instrument to address asymmetric shocks, which are frequent in the region. A shallow financial system also has an adverse impact on rollover risk, borrowing costs, and public investment financing.<sup>9</sup> Second, shallowness also has implications for monetary policy (below). Third, it makes it more difficult for firms and households to access financial services, leading to higher consumption volatility, lower investment and therefore lower growth. Despite overall excess liquidity in the banking system, banks that have excess liquidity may not want to purchase more government paper, as they may already be close to their existing sovereign exposure limits.

<sup>9</sup> See Box 1 in the staff report and the Senegal pilot for a more detailed discussion on these issues.

**27. Under the current exchange rate arrangement, the BCEAO has scope for an active monetary policy in the short-to-medium term.** Empirical analysis conducted by Fund staff suggests that money supply changes have been mainly driven by changes in net domestic assets, not net foreign assets, and therefore that the BCEAO can control its balance sheet to some extent.<sup>10</sup> This likely reflects limited capital mobility partly due to capital controls on outward flows. In addition, the BCEAO has at its disposal a set of adequate instruments (policy interest rates, liquidity auctions and standing facilities, and reserve requirements) and has substantial weight in the banking system to allow for an active monetary policy, as its balance sheet represents about a third of the balance sheet of the banking system. Therefore, the BCEAO can, in principle, exercise significant influence on liquidity conditions in the zone.

**28. The transmission of monetary policy signals largely depends on the depth, breadth, and reach of financial markets.** The transmission mechanism of monetary policy can be presented as illustrated in Figure 10.<sup>11</sup> In the pursuit of its objectives, the central bank sets the policy rate or injects liquidity with a view to controlling certain financial market variables, which may be viewed as intermediate targets. These intermediate targets in turn need to be related to the ultimate objective, which is in the case of the BCEAO is price stability and, to a lesser extent economic and financial development. Four transmission channels are generally distinguished: The bank lending channel; the interest rate channel; the asset price channel; and the exchange rate channel. To be efficient, all channels require functioning financial markets.

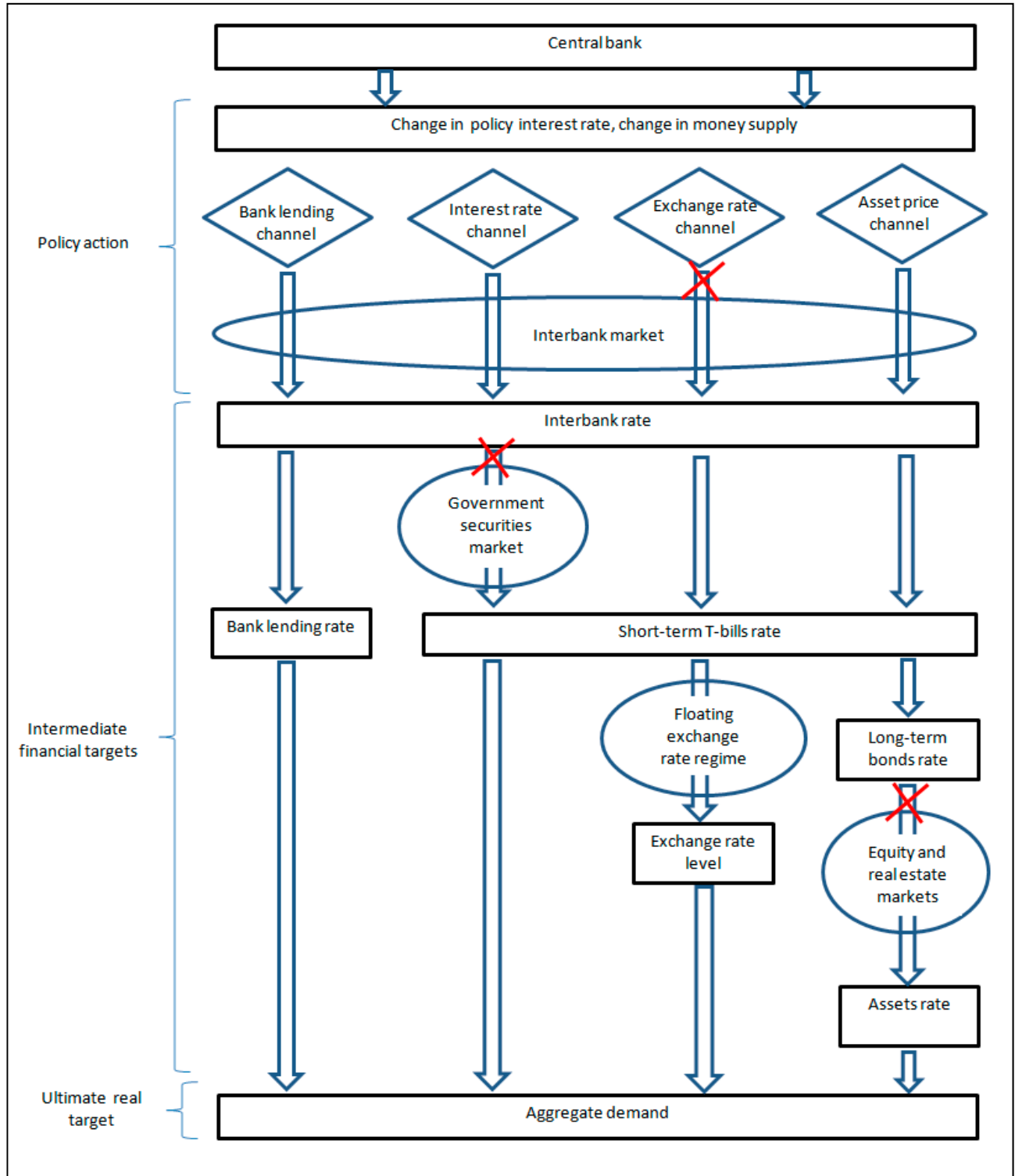
**29. Only a few of the transmission channels are active in the WAEMU.** Recent econometric work, including by the BCEAO, suggests that inflation is determined mostly by non-monetary factors. This may reflect the fact that the channels of monetary policy transmission are either ineffective or simply are not relevant in the WAEMU given the fixed exchange rate arrangement. The bank lending channel seems the most effective channel of transmission, as an increase of 100 basis points in the BCEAO's policy rate is found to reduce private credit growth by about 3 percentage points one quarter later and by 4 percentage points (cumulative) after one year (see staff report, Appendix IV). Changes in policy rates and liquidity injections should also affect the interbank market rate and eventually bank lending rates. However, while the correlation between policy rates and the interbank rate is about 0.5, the correlation between the money market rates and bank lending rates are small with respect to the WAEMU average, very heterogeneous and even negative in some countries (see Figure 11)<sup>12</sup>. Other transmission channels, such as the interest rate and asset prices, do not seem fully effective, as there is little evidence of a statistically significant impact of policy rates changes on T-bill rates and asset prices.

<sup>10</sup> This could also reflect the fact that the BCEAO did not need to use intensively its foreign exchange reserves to defend the peg under the existing exchange rate arrangement.

<sup>11</sup> Based on a stylized presentation for LICs in Mishra, Prachi, Peter J. Montiel, and Antonio Spilimbergo (2012), "Monetary Transmission in Low-Income Countries: Effectiveness and Policy Implications," *IMF Economic Review* 60, 270–302.

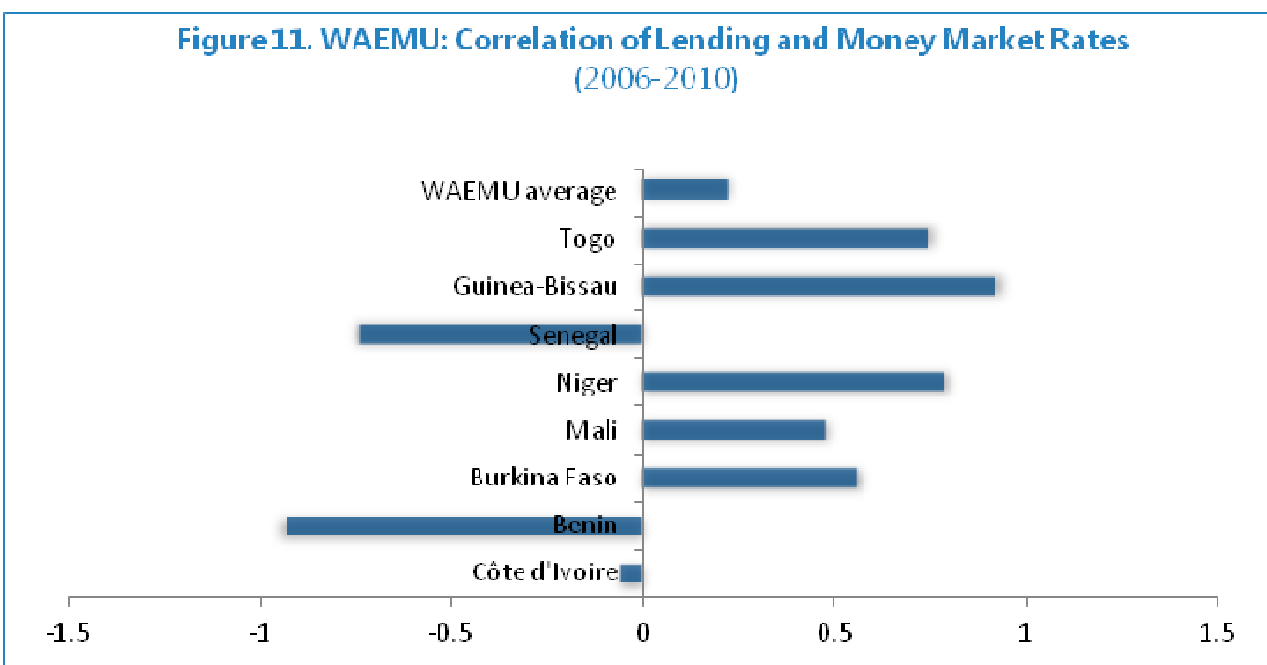
<sup>12</sup> Lending rates in Senegal and Benin, the two countries with negative correlations, are the lowest (Senegal) and the highest (Benin) in the region (see Figure 1), suggesting than other factors than policy rates have an important impact on interest rate formation. The lower level of lending rates in Senegal, for instance, can be partially explained by stronger competition in the Senegalese banking market (relative to the region). Benin experienced a crisis in the banking system and the breakdown of a Ponzi scheme in the late 2000s.

**Figure 10. Monetary Transmission Mechanism in the WAEMU**



Source: Kireyev (2013).

**30. Shalowness of financial markets and the absence of the exchange rate channel are the most likely reasons why the transmission mechanism of monetary policy is not fully effective in the WAEMU.** Research on monetary transmission in LICs (Mishra, Montiel, and Spilimbergo, 2012) showed that for all the channels to be effective, a country should have a strong institutional setup, an independent central bank, a high degree of capital mobility, a floating exchange rate, and a well-functioning interbank, government securities, equities and real estate markets. While some preconditions are met in the WAEMU (the institutional setup and central bank independence) and others are constrained by the institutional setup (limited capital mobility and a fixed exchange rate), the low level of development of financial markets is an impediment for monetary policy effectiveness in the WAEMU. As discussed above (section I-D), the WAEMU interbank market is under-developed, which likely explains why the bank credit channel is not fully effective. At the same time, there is virtually no secondary market for government securities, which does not allow the interest rate channel perform its transmission function. Finally, while the stock exchange is also shallow, which impedes the functioning of the asset price channel. As a result, the chain of monetary policy transmission breaks at the links marked by crosses on Figure 10.



Source: Kolerus and Zdzienicka, 2013.

**31. There are several additional factors hindering the effectiveness of the transmission mechanism of monetary policy:**

- **Persistent excess liquidity:** The WAEMU banking system is highly heterogeneous and segmented, including with regard to the distribution of liquidity. The reluctance of banks to trade liquidity means that liquidity needs from illiquid banks need to be met by injections from the BCEAO. In addition, banks also tend to hold large precautionary excess reserves due to weaknesses with the payments system (e.g., remote branches may need to hold large cash balances due to transportation problems). Such a context makes it very hard for the BCEAO to focus on overall liquidity management.



In turn, the BCEAO also gets very limited signals from the shallow interbank market. A change in liquidity injections or in the policy rates will have a large impact on liquidity-constrained banks but a very limited one on the banks that do not need liquidity from the BCEAO. Developing the interbank market and mopping up excess liquidity will be preconditions for a more effective credit channel.<sup>13</sup>

- **Credit rationing:** Imperfect information is an important issue in the WAEMU, in particular for smaller firms and the sizable informal sector. When a financial institution raises its lending rates following a change in policy rates, it may increase the riskiness of new lending due to adverse selection. If unwilling to accept higher risk, the bank may ultimately decide to keep its lending rates unchanged, muting the impact of monetary policy decisions.
- **Limited bank competition and the presence of state-owned banks:** A number of factors, such as high average interest and profit margins and segmentation, suggest that competition in the banking market may not be very strong. In such circumstances, monetary policy changes might be partly and temporarily absorbed by changes in profitability. The presence of state-owned banks may also blunt the transmission channel, as preferred lending practices are frequent with these institutions; these practices mean that certain customers will get credit at a given rate irrespective of the level of policy rates.

## FURTHER DEEPENING WITH STABILITY: OBSTACLES AND RECOMMENDATIONS

**32. The development of the financial system should be pursued forcefully in a way that preserves financial stability.** The previous sections showed that there is substantial scope to further develop the financial system in the WAEMU. This section discusses obstacles to further financial development in the WAEMU and how to address them. It will also discuss how to strengthen crisis prevention and resolution frameworks as financial development will inevitably bring new risks.

**33. Strong financial crisis prevention and management frameworks are critical in a region like the WAEMU.** WAEMU countries are affected by frequent and often asymmetric shocks. As shock absorption mechanisms are limited, economic agents face substantial macroeconomic volatility which can test the stability of the financial sector. Other issues, such as asymmetric information and weak judicial and business environments, impose extra risks for financial institutions. Such a context requires a strong microprudential framework, adapted to the risky environment, and strong bank supervision to enforce it and detect problems early. They should be completed by adequate macroprudential surveillance to address systemic risks.

<sup>13</sup> Another reason for the high average liquidity in the banking system may have been the design of the transformation ratio, which constrained longer-term lending.

## A. Issues and Recommendations for Obstacles to Further Financial Development

**34. The obstacles have been well identified by the authorities and described in detail in the pilot studies on Senegal and Benin.** They include: imperfect information on borrowers, due to limited availability of audited company statements and absence of credit bureaus, leading to adverse selection and moral hazard issues, and ultimately to credit rationing; weak business and judicial environments, including the absence of formalized property rights in large parts of the countries which increases the difficulty of using land as collateral in lending; a tax regime which is not favorable to financial activities; and insufficient financial skills and expertise. The responsibility for addressing many of these obstacles rests with the national authorities (e.g., improving judicial systems). The rest of this section will focus on obstacles where the responsibility rests to a large extent with the regional authorities.

**35. The BCEAO and staff agree that the development of key regional markets, such as the interbank market and the secondary government debt market is a priority.** The BCEAO expects major reforms in this area to be launched by mid-2013. These reforms include the introduction of collateralized operations (repos) to address the reluctance of liquid banks to lend to illiquid ones; the rollout of an electronic platform to auction and trade liquidity and government paper (“application Trésor”); and the introduction of primary dealers, which should accelerate the development of the secondary government debt market. A regional debt agency (“Agence UMOA-Titres”) will also be launched, with the main mission to advise national treasuries on debt management, improve issuance coordination, and contribute to the development of the government debt market. It is expected to facilitate liquidity management. Broadening the investor base in the government debt market is highly desirable; governments will face lower rollover risks and interest rates and might be able to extend maturities.

**36. Policies aimed at the development of the government debt market may have hampered that of the private debt market and led to mispricing of risks, two issues that will need to be addressed.** Distortions include tax advantages for sovereign paper, zero risk weighting for government bonds and eligibility for refinancing at the BCEAO. Now that the (primary) government debt market has taken off, a more balanced approach may need to be considered. At a minimum, governments should avoid providing new incentives/distortions in favor of government paper. A more level playing field with regard to taxation and riskiness would be desirable.

**37. Recent reforms are expected to contribute to financial market development.** The CREPMF recently introduced a set of measures to (i) improve the quality of financial information; (ii) develop skills and awareness towards equity finance of economic actors; (iii) lower the high entry costs to the equity market. More specifically:

- **Introduction of ratings.** Before 2012, corporations that wanted to issue bonds on the regional market were required to provide a 100 percent guarantee to investors. Those guarantees added about 1–2 percentage points to interest rate costs. The reform abolished the guarantee requirement if the company is rated investment grade or higher. For companies with lower ratings the guarantee

requirement remains but may be less than 100 percent. Currently, all private issuances are from companies that are rated lower than (local) investment grade.<sup>14</sup> As the problems with rating agencies during the subprime crisis have illustrated, ratings are no panacea, but they can help in other circumstances (in particular, to reduce information asymmetries); they have yet to be fully accepted in the region as companies are reluctant to disclose information and data.

- **Enabling mortgage refinancing and securitization operations.** Two financial agents<sup>15</sup> have been granted securitization licenses in early 2013. According to the BCEAO, the WAEMU member states are currently reviewing options in this area.
- **More competitive pricing.** Commissions and fees on equity issuance, which were previously at very high levels even in international comparison, have been significantly reduced to improve access to the market and attract new clients.
- **Introduction of a new electronic data management system,** including a surveillance mechanism of the secondary market.
- **Promoting innovative forms of banking,** including mobile banking (and products) that are adapted to the local environment.

**38. Further reforms to improve market infrastructure and access are to be implemented in 2013,** such as the shift to continuous trading and the introduction of a market for (S)MEs with lower fees and less stringent rules (e.g., on accounting records). The supply of financial assets can also be increased if governments list public companies, and ensure that the 20 percent floating requirement—at least 20 percent of the company's stock must be listed—be strictly enforced. In addition, the BRVM is in talks with the stock exchange of Ghana and Nigeria for closer cooperation.

**39. Information quality and dissemination are critical for the development of financial activities.** From this perspective, ongoing work on the establishment of credit and guarantee bureaus is welcome and should be accelerated. Staff noted that the willingness of having a regional approach to this issue, while understandable, should not lead to excessive delays. Efforts at all levels to improve data quality, coverage, and timeliness should continue. The data should be widely shared at the national and regional levels between the authorities and with the public. Also market abuse regulations—such as against insider information—currently under discussion should be introduced as soon as possible.

**40. Close coordination between the national and regional levels is required to ensure that the regional policy framework is sufficiently responsive to new needs.** As indicated in the Senegal report, these new needs are likely to emerge first at the national level. When a country is at the forefront of financial sector reform, the need to develop or amend the policy framework at the regional

<sup>14</sup> There are, however, a number of companies in the WAEMU which are rated above investment grade. These companies currently use their ratings to improve their credit conditions vis-à-vis banks rather than issuing on the securities market.

<sup>15</sup> One private institution based in Abidjan and BOAD, the region's development bank.

level may slow financial development in this country. While there are positive externalities for other countries from a regional approach, the time needed for developing it should be limited to a minimum.

## B. Issues and Recommendations for Microprudential Regulation and Supervision

**41. Compliance with microprudential norms needs to increase through strengthened supervision.** The persistence of a situation of partial compliance suggests enforcement weaknesses and poses a reputational risk to the Banking Commission. Part of the problem is insufficient resources, which for instance do not allow the Banking Commission to meet its objective of an on-site inspection for each bank every two years. The recent increase in staff resources should contribute to improving the situation, although it may not be sufficient. The Banking Commission will also need to have the power to impose sufficiently elevated pecuniary penalties that would deter inappropriate behavior of banks. The supervision of state-owned banks will also need to be reviewed and strengthened to eliminate any (even apparent) political interference. Finally, it is critical to improve reporting (below), including for supervision purposes.

**42. A number of regulatory standards and practices will need to be introduced or brought closer over time to best international practice.** More specifically, the following areas need to be covered :

- **Concentration risk.** The current ratio sets a limit to single risk exposure at 75 percent of capital, rather than the international norm of 25 percent. Stress tests clearly show that concentration risk is the main threat to the banking system. The 75 percent limit needs to be brought down progressively to international norms.
- **NPL classification and provision.** While international norms classify a loan as nonperforming after 90 days of non-payment, a looser definition of 180 days is used in the WAEMU. This suggests that the NPL situation could be even worse than implied by the current high ratios. Provisioning requirements may also need to be tightened, as currently no provisioning is needed for two years for NPLs when the initial credits were provided with guarantees. The authorities may want to take advantage of the planned changes in bank accounting and transition to IFRS standards to change these rules.
- **Sovereign risk weighting in capital requirements.** The recent crises in Côte d'Ivoire, Guinea-Bissau and Mali clearly show that sovereign debt cannot be seen as riskless in the region.
- **Broadening application of capital requirements.** This would allow for the inclusion of other risk categories besides counterparty risks, such as market risks (even though still limited at this juncture) and operational risks, which seem to be relatively high in the WAEMU.
- **Timeliness and transparency of information.** The quality and timeliness of data collected for analytical and prudential purposes need to improve, and must be disseminated to the markets.

- **Ensuring adequate regulatory perimeter.** It will be important that the regulatory net be cast wide enough so that borrowers and lenders do not shift their activities to markets that are unregulated or insufficiently regulated. Pyramid schemes, such as those discussed in the Benin pilot, could thereby be more easily prevented.

**43. The authorities intend to address many of these issues in the context of the transition to Basel II.** They expect to launch this multi-year project shortly and expressed interest in technical assistance from the IMF in this area. Progress was made in reforming two prudential norms that were of questionable effectiveness (Section I.B). With regard to the concentration risk, a concern is that it reflects the fact that the formal sector remains relatively narrow. Lowering the risk division ratio should therefore be done gradually in a way that does not affect the provision of financing to key economic sectors.

**44. Risk will need to be monitored on a consolidated basis to capture the full spectrum of activities undertaken by large, complex financial groups.** The Banking Commission currently has limited capacity to conduct prudential oversight of complex and rapidly expanding pan-African banking groups. Consolidated supervision is also hampered by the Banking Commission lacking powers to supervise financial holding companies. These shortcomings must be addressed forcefully. The authorities are aware of these issues, which have also been identified recently by the FSC. A study on how to move towards consolidated supervision is being prepared.

**45. Adequate supervision of cross-border groups also requires a strengthening of collaboration with other supervisors.** There are currently a few cross-border cooperation agreements (e.g., with France, Guinea, and Morocco), with several ones being worked out.<sup>16</sup> Such agreements are welcome. However, the effectiveness of such agreements is not assured in a crisis context, as illustrated in other regions during the international financial crisis. Improved collaboration with foreign supervisors would require: (i) signing cooperation protocols with the full range of foreign supervisors of parent banks and subsidiaries of lending institutions located in the Union (at present only half a dozen protocols have been drawn up and signed); (ii) setting up a schedule of regular meetings with foreign supervisors structured according to types of risks; (iii) instituting a regular sharing of information between supervisors, in particular regarding the assessment and monitoring of risks and internal auditing within corporate entities; (iv) in collaboration with foreign supervisors, clarifying the actual responsibilities of parent companies in recapitalizing their branches and subsidiaries, especially when problems arise. The authorities could therefore consider: (i) taking the lead in proposing and organizing supervisory colleges for each of the pan-African banking groups; (ii) coordinate with the Nigeria supervisory authorities the formation of college groups for Ecobank and the United Bank for Africa; (iii) head a review of the legal obstacles that may hinder the sharing of information across different supervisory bodies. At the WAEMU level, the existing college of supervisors is essentially a working group that can share information and promote harmonization, but not a supervisory college with the

<sup>16</sup> Nigeria's recent decision to adopt a regulation forbidding its banks to support their subsidiaries in case the capital requirements of the subsidiaries are to be increased and/or when they are making losses casts doubt on the effectiveness of some of these arrangements.

mandate, power, organization and capacity to monitor and inspect the activities of each banking group headquartered in the region.

### C. Issues and Recommendations for Macroprudential Regulation

**46. An important lesson from the global financial crisis is the need to supplement microprudential policies with macroprudential ones.** Taken together, these policies help enhance the shock absorbers in the financial system in terms of capital and liquidity, place constraints on overall leverage and extend the regulatory perimeter to all systemically important institutions, markets and instruments (Table 4).

**Text Table 2: Comparison Between Macroprudential and Microprudential**

|   | Macroprudential                            | Microprudential   |
|---|--|---|
| Proximate objective                     | Limit financial system-wide distress       | Limit distress of individual institutions (solvency risk) |
| Ultimate objective                      | Minimize output costs                      | Consumer (investor/depositor) protection                  |
| Model of risk                           | (in part) endogenous                       | Exogenous   |
| Interconnectedness and substitutability | Important                                  | Irrelevant  |
| Calibration of prudential controls      | In terms of system-wide distress; top-down | In terms of solvency risk; bottom-up                      |

Source: International Monetary Fund, 2010

**47. Macroprudential surveillance is recent in the WAEMU and needs to be strengthened.**

- **Early warning systems.** The BCEAO has initiated work on this issue, but is facing a number of data and methodological issues. Financial data are scarce and their informational content might be limited because of the shallowness of markets. In addition, the past might be a poor guide to estimate an early warning system, as a number of banking/financial crises in the region may have been caused by (exogenous) shocks difficult to foresee (e.g., political crisis, governance issues).
- **Coverage.** Sectoral balance sheets (household, corporate, financial institutions and public sectors) are often critical for financial stability analysis but are not readily available in the WAEMU. This gap could be partially filled through the use of targeted surveys of firms, households and corporations. Cross-border linkages also need to be monitored more closely and analyzed. Financial network risk analysis could be used for the map of risks in the financial sector that the authorities are currently designing. Finally, coverage of other nonbank financial institutions, such as insurance companies and pension funds, will need to expand.

- **Disaggregation of information.** The use of aggregated data can sometimes mask pockets of vulnerabilities. For that reason, financial stability analysis should also rely on disaggregated data to estimate the distribution of risks across sectors. For example, analyzing the breakdown of borrowing by industry and region can be informative. Analysis of disaggregated data on banks can also be critical given the heterogeneity of the banking system, and could be used actively by the Banking Commission to develop risk-based supervision.
- **More active use of stress testing.** The regional authorities have decided to develop their capacity in this area. Once they have become familiar with basic stress-testing and improved the quality and timeliness of data, they could explore ways to refine the exercise, including by incorporating macro-economic variables and developing a range of plausible scenarios.
- **Publication of information.** The FSC could consider producing and publishing a financial stability report to communicate and convey to economic agents the risks and challenges faced by the financial system. Consideration could be given to making disaggregated data publicly available.

**48. The range of macro-prudential instruments will need to be expanded.** Reserve requirements are presently the only instrument available to the authorities.<sup>17</sup> The authorities will therefore need, at some point, to consider broadening their toolkit with other instruments. Given the limited correlation between macroeconomic variables and financial ones—business cycles in WAEMU countries are often driven by weather-related or political shocks that cannot be forecasted—introducing instruments to address these risks (such as countercyclical capital requirements) would not necessarily be effective at this juncture. In staff’s view, while macro-prudential could play a very useful role in an heterogeneous region, more urgent tasks for the authorities include: (i) developing a monitoring system, which is a pre-requisite; and (ii) improving micro-prudential regulation and supervision.

## D. Issues and Recommendations for Crisis Management

**49. In a financial crisis, emergency liquidity assistance (ELA) may need to be provided to illiquid but solvent institutions.** ELA is distinguished from the normal provision of liquidity to individual institutions under the central bank’s standing facilities. While standing facilities are available on demand and the rules of access are clear “ex-ante,” ELA is typically available only in exceptional circumstances at the discretion of the central bank, with adequate but unconventional collateral.

**50. The BCEAO currently does not have an explicit mandate to provide ELA.** The ambiguity arising from this situation may be a double-edged sword. While the absence of a mandate protects in principle the BCEAO’s balance sheet, historical evidence suggests that it is hard for a central bank to avoid getting involved in a systemic liquidity crisis. Once this happens, the risk to the central bank’s balance sheet might actually be much more difficult to contain. To avoid such a situation, it would be desirable for the BCEAO and the national governments to discuss *ex ante* how the BCEAO could get

<sup>17</sup> They have been harmonized a few years ago and therefore cannot be used to address asymmetric shocks.



involved in the provision of ELA and how it would be indemnified by the governments for this activity should losses arise.

**51. Where a financial institution's problems extend beyond short-term liquidity and are more deep seated, recourse to recovery or resolution strategies is needed.** A recovery strategy in which regulators and management work together to address the underlying problems and so maintain the firm as a "going concern"; and, if this fails, a resolution strategy to close the firm, in a structured and orderly way. The objective in each case will be to minimize the impact on the rest of the financial system and by doing so help sustain the provision of essential services to the economy. In both cases, the cost to the budget will also be an important consideration.

**52. The Banking Commission needs to improve detection of early problems and to rely more on prompt and forceful corrective action.** An effective supervisory framework requires that problems are detected early on and followed by early intervention in the form of prompt corrective action (PCA) to restore an institution's health. As discussed earlier, the authorities need to use financial and prudential information from institutions much more actively so as to be able to anticipate better problems and move to risk-based supervision; this will also require better reporting. Their track record suggests that problems have been permitted to persist longer than desirable. Many banks in the WAEMU have indeed been insolvent for long periods without being resolved. These 'zombie banks' have incentives to gamble for resurrection and can have an adverse impact on other banks. More forceful action would therefore be desirable in the future, including with a view to reducing intervention costs. Absent a robust and effective resolution regime, the WAEMU authorities have little choice but to bail out such banks at great public expense—which perpetuates moral hazard.

**53. In case a bank cannot be recovered, it must be closed down, but the WAEMU resolution regime lacks key attributes recommended by the Financial Stability Board (FSB) (Table 4).** Adopting some of the FSB recommendations would require strengthening the powers of the regulator. For instance, the Banking Commission, acting within a well-defined framework that protects the rights of depositors and creditors, would be able without undue delay to order the transfer of assets and liabilities, undertake mergers, and decide on changes in shareholders.

**54. Some of the difficulties to resolve banks could reflect coordination failures between the regional and national authorities.** The resolution of a bank involves the Banking Commission, which takes the decision, and the concerned national government, which needs to approve that decision. In case of a disagreement, the government can appeal to the WAEMU Council of Ministers to reverse the decision. Ex-ante burden-sharing arrangements could be designed to overcome some of the issues of delaying bank resolution. The authorities should also pursue the explicit support from parent companies with respect to their branches or subsidiaries when a request for a banking license is examined, with a view to obtaining substantial resources for intervention from shareholders should the need arise. As public banks in some of the countries have often been a source of problems, privatization may also be worth considering.



**55. To avoid moral hazard problems, a systematic investigation of the responsibilities of directors, shareholders, and auditors involved in a bankruptcy should be conducted.** This should be particularly the case in instances where public funds were engaged. Conclusions should be drawn from investigations with regard to the suitability of the concerned stakeholders for future jobs in the financial sector. Inappropriate behavior should be prosecuted to the full extent of the law.

**Text Table 3: WAEMU: FSB Key Attributes of Effective Resolution Regimes for Financial Institutions: Which ones are Available?**

|  |  |   |  |  |
|--|--|---|--|--|
| <b>Essential Features for Resolution Regimes</b> | ensure continuity of systemically important financial services, and payment, clearing and settlement functions   | protect, where applicable and in coordination with the relevant insurance schemes and arrangements such as depositors, insurance policy holders and investors as are covered by such schemes and arrangements, and ensure the rapid return of segregated client assets;   | allocate losses to firm owners (shareholders) and unsecured creditors in a manner that respects the hierarchy of claims;   | not rely on public solvency support and not create an expectation that such support will be available; |
| <b>WAEMU</b>                                     | Not Clear  | No  | Yes  | No   |
| <b>Essential Features for Resolution Regimes</b> | avoid unnecessary destruction of value, and therefore seek to minimise the overall costs of resolution in home and host jurisdictions and, where consistent with the other objectives, losses for creditors; | provide for speed and transparency and as much predictability as possible through legal and procedural clarity and advanced planning for orderly resolution;  | provide a mandate in law for cooperation, information exchange and coordination domestically and with relevant foreign resolution authorities before and during a resolution;                                    | ensure that non-viable firms can exit the market in an orderly way;                                    |
| <b>WAEMU</b>                                     | No   | No  | No   | Not Clear  |
| <b>Essential Features for Resolution Regimes</b> | be credible, and thereby enhance market discipline and provide incentives for market-based solutions.  | stabilisation options that achieve continuity of systemically important functions by way of a sale or transfer of the shares in the firm or of all or parts of the firm's business to a third party, either directly or through a bridge institution, and/or an officially mandated creditor-financed recapitalisation of the entity that continues providing the critical functions; | liquidation options that provide for the orderly closure and wind-down of all or parts of the firm's business in a manner that protects insured depositors, insurance policy holders and other retail customers. |  |
| <b>WAEMU</b>                                     | Not Clear  | No  | Not Applicable   |  |

Source: FSB (2011) "FSB Key Attributes of Effective Resolution Regimes for Financial Institutions"

**56. Well designed financial safety nets are critical to an effective crisis management system.** Their mere existence may go a long way to stabilizing financial systems in times of stress. Deposit insurance systems are an important part of financial safety nets, particularly to address smaller (idiosyncratic) banking crises if not systemic ones. Credible systems are those that have appropriate coverage, timely payouts, and adequate funding.

**57. The authorities are working on a deposit insurance system.**<sup>18</sup> They are still considering some aspects of coverage, payouts, and funding but expect the system to be launched in 2013. It would cover

<sup>18</sup> The authorities are also working on an insurance fund to guarantee all payments made through the RTGS system.

deposits with banks and MFIs. Staff suggested that the authorities consider giving a role to the deposit insurance system in bank recovery, as is the case in a number of countries. This might allow reducing the final cost, as recovery is often less expensive than liquidation.

**58. Finally, the authorities are working on a Financial Stability Fund (FSF), whose main goal would be to avoid possible debt payment incidents by sovereigns facing liquidity problems.** Work is still ongoing on a number of key issues, such as financing of the FSF and terms of the FSF financing. Staff flagged a number of issues to be considered, such as the identification of the nature of shocks (temporary vs. permanent, which is, for instance, particularly difficult to assess in the case of political instability), how to address moral hazard (is there a role of conditionality? Should financing be provided on market or concessional terms), and the seniority of FSF financing (which could raise issues if a restructuring is eventually needed).

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**IMF Executive Board Concludes 2013 Discussion on  
Common Policies of Member Countries of the  
West African Economic and Monetary Union**

On March 25, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the annual Discussion<sup>1</sup> on Common Policies of Member Countries of the West African Economic and Monetary Union (WAEMU).

**Background**

The WAEMU faced new political and security challenges in 2012. Military coups occurred in Guinea-Bissau and Mali and caused economic disruption in these countries. The northern part of Mali was taken over by terrorist groups, which led to large refugee flows to neighboring countries and triggered a military intervention to restore territorial integrity. On the upside, the sociopolitical situation in Côte d'Ivoire improved significantly, and a peaceful and democratic changeover took place in Senegal.

Regional economic activity rebounded in 2012. After a large decline in 2011 to about 1 percent of gross domestic product (GDP) because of the drought in the Sahel and the post-electoral crisis in Côte d'Ivoire, regional growth is estimated to have reached 5.8 percent of GDP in 2012. Growth was driven mainly by the post-crisis recovery in Côte d'Ivoire, the rebound of agricultural

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<sup>1</sup> 1/ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>

production in a number of countries, and the start of oil production in Niger. A few countries faced inflationary pressures, mainly on domestic prices for food and petroleum products. Nevertheless, average regional inflation remained low, at about 2.5 percent.

The area-wide fiscal deficit stabilized around 4 percent of GDP in 2012, while the overall debt situation improved thanks to debt relief to Côte d'Ivoire. Compared with 2011, fiscal deficits increased in Burkina Faso, Niger, and Togo, stabilized in Côte d'Ivoire, and decreased in the other countries. With Côte d'Ivoire reaching the [Heavily Indebted Poor Countries](#) Initiative's completion point in 2012, all WAEMU countries have benefited from substantial relief on their external debt. The average nominal debt for the region now stands at about 40 percent of GDP. All countries have public debt ratios substantially below the 70 percent of GDP ceiling set by the regional surveillance framework; they also have low or moderate ratings for the risk of debt distress according to recent debt sustainability analyses (DSAs), reflecting prudent fiscal policies and sustained growth.

Monetary policy was eased modestly in 2012. Despite relatively strong growth of credit to the private sector and government, money growth remained moderate in 2012 (at about 8 percent year-on-year) because of a significant contraction in net foreign assets (NFA). In a context of continued moderate inflation and a sharp contraction in bank liquidity (related, to a large extent, to the evolution of NFA) leading to pressures on interest rates, the Central Bank of West African States (BCEAO) injected substantial amounts of liquidity to banks. It also cut the policy rates by 25 basis points to respectively 3 and 4 percent and lowered the reserve requirement ratio to from 7 to 5 percent.

The region's current account deficit widened significantly in 2012. This outcome reflects a number of exceptional factors, such as higher imports of intermediate and capital goods by Côte d'Ivoire related to reconstruction efforts and by Burkina Faso and Niger for mining and hydrocarbon projects, higher food imports to make up for the impact of the 2011 drought, and unfavorable terms of trade. The higher current account deficit, combined with temporary delays in repatriating export proceeds (mostly by Côte d'Ivoire), led to a deficit in the overall balance of payments and a decline of official reserves, which stood at about 5 months of regional imports and 98 percent of short-term domestic liabilities at end-2012.

Progress in fiscal convergence has been limited. The key convergence criterion on the basic fiscal balance was missed by five of the eight countries in 2012. Following debt relief, the debt criterion is now met by all countries.

## Executive Board Assessment

Executive Directors welcomed the maintenance of macroeconomic stability in the region and the prospects for continued robust growth with moderate inflation. Given the continuing challenging environment and downside risks, it will however be important to reconstitute policy buffers and to ensure the full implementation of growth-enhancing policies, including to promote financial deepening and regional integration.

Directors considered the current macroeconomic policy mix appropriate and welcomed the planned fiscal consolidation in the countries with higher deficits. They called for additional efforts to raise revenue and improve the quality of public spending. Directors emphasized the need to strengthen debt management at the country level, paying close attention to domestic debt levels, given less favorable terms. In light of the outlook for inflation, Directors viewed the recent easing of monetary policy as appropriate. They noted that official reserves remain adequate but stressed that their recent decline requires close monitoring.

Directors stressed the importance of better coordination of fiscal policies to help preserve debt sustainability and the stability of the Union in the medium term. They welcomed the intention to conduct a comprehensive review of the regional surveillance framework. They supported a reconsideration of the convergence criteria on public debt and the fiscal deficit and a strengthening of the institutional framework to increase adherence and traction.

Directors encouraged further measures to develop the financial system to help raise growth, mitigate the impact of volatility, increase inclusion and improve the effectiveness of macroeconomic policies. The completion of ongoing reforms to develop the interbank and secondary government debt markets will be critical. Directors noted that banks are on average relatively well capitalized and liquid, although there is substantial heterogeneity among them. Risks arise from high lending concentration and uneven asset quality, and from banks' increasing exposure to sovereigns in the region and the emergence of regional groups. In this context, Directors urged the acceleration of ongoing work to strengthen bank supervision and regulation, notably to improve observance of prudential rules while bringing some of these rules closer to international standards. They also welcomed efforts to strengthen the crisis prevention and resolution framework.

Directors noted that the area-wide real exchange rate appears to be in line with fundamentals. To improve non-price competitiveness and growth prospects, Directors called for concerted regional and national efforts to strengthen institutions, governance, infrastructure, and trade integration. They also encouraged continued efforts to enhance the quality, coverage, and timeliness of data as well as the sharing of data widely at the national and regional levels.

The views expressed by Executive Directors today will form part of the Article IV consultation discussions on individual members of the WAEMU that take place until the next Board discussion of WAEMU common policies.

**Public Information Notices (PINs)** form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

**WAEMU: Selected Economic and Financial Indicators, 2009—2017**

|  | 2009   | 2010   | 2011   | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   |
|--|--|--------|--------|--------|--------|--------|--------|--------|--------|
|  |  |        |        | Est.   | Proj.  | Proj.  | Proj.  | Proj.  | Proj.  |
|  | (Annual percentage change)                                     |        |        |        |        |        |        |        |        |
| <b>National income and prices</b>                            |  |        |        |        |        |        |        |        |        |
| GDP at constant prices                                       | 2.9  | 4.8    | 1.1    | 5.8    | 6.0    | 6.3    | 6.1    | 5.9    | 5.8    |
| GDP per capita at constant prices                            | 0.1  | 1.8    | -1.1   | 2.9    | 3.2    | 3.4    | 3.2    | 3.1    | 3.0    |
| Broad money to GDP   | 9.7  | 8.6    | 5.5    | 4.1    | ...    | ...    | ...    | ...    | ...    |
| Consumer prices (average)                                    | 0.4  | 1.4    | 3.9    | 2.4    | 2.4    | 2.4    | 2.2    | 2.1    | 2.3    |
| Terms of trade   | 4.3  | -4.7   | -0.4   | 1.5    | -0.2   | 0.6    | 0.2    | -0.4   | -0.4   |
| Nominal effective exchange rates                             | 0.9  | -4.3   | 1.7    | -2.2   | ...    | ...    | ...    | ...    | ...    |
| Real effective exchange rates                                | 0.2  | -6.3   | 0.9    | -2.5   | ...    | ...    | ...    | ...    | ...    |
|  | (Percent of GDP)   |        |        |        |        |        |        |        |        |
| <b>National accounts</b>                                     |  |        |        |        |        |        |        |        |        |
| Gross domestic savings                                       | 15.3   | 14.1   | 15.5   | 13.0   | 14.4   | 15.5   | 16.0   | 16.5   | 15.9   |
| Gross domestic investment                                    | 18.7   | 18.8   | 18.6   | 20.2   | 21.4   | 22.0   | 22.1   | 21.9   | 22.0   |
| <i>Of which:</i> public investment                           | 7.1  | 6.4    | 6.3    | 7.8    | 9.1    | 9.6    | 9.7    | 9.6    | 9.5    |
|  | (Annual changes in percent of beginning-of-period broad money) |        |        |        |        |        |        |        |        |
| <b>Money and credit</b> <sup>1</sup>                         |  |        |        |        |        |        |        |        |        |
| Net foreign assets   | 5.8  | 3.1    | 1.0    | -5.5   | ...    | ...    | ...    | ...    | ...    |
| Net domestic assets  | 8.9  | 12.6   | 9.7    | 13.9   | ...    | ...    | ...    | ...    | ...    |
| Broad money  | 14.7   | 15.7   | 10.7   | 8.4    | ...    | ...    | ...    | ...    | ...    |
|  | (Percent of GDP, unless otherwise indicated)                   |        |        |        |        |        |        |        |        |
| <b>Government financial operations</b> <sup>2</sup>          |  |        |        |        |        |        |        |        |        |
| Government total revenue, excl. grants                       | 17.4   | 17.9   | 16.7   | 19.0   | 19.1   | 19.3   | 19.5   | 19.7   | 19.8   |
| Government expenditure                                       | 23.9   | 23.3   | 23.2   | 25.5   | 26.5   | 25.7   | 25.7   | 25.6   | 25.5   |
| Overall fiscal balance, excl. grants                         | -6.5   | -5.4   | -6.5   | -6.5   | -7.3   | -6.4   | -6.2   | -5.9   | -5.7   |
| Official grants  | 3.0  | 2.3    | 2.5    | 2.7    | 3.1    | 3.4    | 3.3    | 3.2    | 3.0    |
| Overall fiscal balance, incl. grants                         | -3.5   | -3.1   | -4.0   | -3.8   | -4.2   | -3.0   | -2.9   | -2.7   | -2.7   |
| Basic fiscal balance, incl. grants & HIPC                    | -1.3   | -0.6   | -2.1   | -2.0   | -0.6   | -0.6   | -0.4   | -0.3   | -0.3   |
| <b>External sector</b>                                       |  |        |        |        |        |        |        |        |        |
| Exports of goods and services <sup>3</sup>                   | 27.0   | 29.4   | 29.9   | 27.8   | 28.9   | 29.1   | 29.0   | 28.8   | 28.8   |
| Imports of goods and services <sup>3</sup>                   | 32.7   | 36.5   | 34.5   | 36.4   | 37.2   | 36.9   | 36.3   | 35.5   | 35.2   |
| Current account, excl. grants <sup>4</sup>                   | -5.6   | -6.7   | -4.3   | -8.8   | -8.9   | -8.4   | -7.9   | -7.3   | -7.1   |
| Current account, incl. grants <sup>4</sup>                   | -3.6   | -4.9   | -3.1   | -7.3   | -7.2   | -6.9   | -6.5   | -5.9   | -5.8   |
| External public debt   | 35.9   | 32.3   | 31.5   | 29.1   | 28.8   | 28.7   | 28.6   | 28.4   | 28.0   |
| Total public debt  | 45.4   | 43.4   | 43.5   | 40.9   | 39.3   | 38.8   | 38.5   | 37.9   | 37.1   |
| Broad money  | 32.3   | 35.0   | 37.0   | 38.5   | ...    | ...    | ...    | ...    | ...    |
| <b>Memorandum items:</b>                                     |  |        |        |        |        |        |        |        |        |
| Nominal GDP (in billions of CFA francs)                      | 32,560   | 34,671 | 36,468 | 39,589 | 42,770 | 46,483 | 50,529 | 54,919 | 59,753 |
| Nominal GDP per capita (in US dollars)                       | 722  | 714    | 775    | 750    | 783    | 822    | 861    | 901    | 944    |
| CFA franc per US dollars, average                            | 472  | 495    | 472    | 511    | ...    | ...    | ...    | ...    | ...    |
| Euro per US dollars, average                                 | 0.72   | 0.76   | 0.72   | 0.78   | ...    | ...    | ...    | ...    | ...    |
| Foreign exchange cover ratio <sup>5</sup>                    | 98.9   | 99.9   | 97.2   | 97.7   | ...    | ...    | ...    | ...    | ...    |
| Reserves in months of imports<br>(excl. intra-WAEMU imports) | 5.9  | 6.5    | 5.9    | 5.2    | 4.9    | 4.8    | ...    | ...    | ...    |

Sources: IMF, African Department database; World Economic Outlook; IMF staff estimates.

<sup>1</sup>The estimates for 2012 refer to annual change at end-Sep, with the beginning-of-period referring to end-Sep 2011.

<sup>2</sup>Fiscal data for 2013 reflect a strong increase in the fiscal deficit of Niger following a new project in the hydrocarbon sector.

<sup>3</sup>Excluding intra-regional trade.

<sup>4</sup>Data up to 2011 are corrected for intra-regional trade discrepancies by BCEAO.

<sup>5</sup>Gross official reserves divided by short term domestic liabilities (IMF definition). For 2012, the estimate refers to end-Sep.

**Statement by Mr. Assimaidou on WAEMU  
Executive Board Meeting  
March 25, 2013**

My WAEMU authorities would like to thank staff for the fruitful discussions held with the regional institutions and which allowed a broad overview of the achievements of the economic and monetary union as well as the policy challenges facing the region. My authorities consider the thrust of the report as a fair reflection of the discussions, and would like to reiterate their full commitment to continue to work towards achieving a more stable and prosperous union. In this regard, they will step up their efforts in critical areas including the coordination of fiscal policy, the deepening of the financial sector and the structural transformation of the economies to entrench growth, bolster trade and provide employment opportunities.

**I. Recent Developments, Fiscal Policy and Convergence**

After declining significantly in 2011 due to the post-election crisis in Côte d'Ivoire and the drought in the Sahel, regional growth is estimated to have rebounded strongly at 5.8 percent in 2012. The main drivers of this growth were the recovery in Côte d'Ivoire –the largest economy of the Union – the rebound of agricultural production in a number of countries, the dynamism of the tertiary sector and the start of oil production in Niger. Inflation in the region was subdued to 2.5 percent, lower than in 2011, though some countries faced some upward pressures due to high food and fuel prices.

The situation in Mali has had an adverse impact on the domestic economy and triggered large refugee inflows in neighboring countries and a humanitarian crisis. Nevertheless, the effect on the area-wide economy has been kept in check. My authorities would like to express their gratitude to the partners who have helped to restore the full territorial integrity of Mali.

The coordination of fiscal policy and the monitoring of convergence criteria set accordingly is an important agenda for my WAEMU authorities. The end-2012 assessment showed that overall compliance with the regional surveillance framework was mixed. Most countries missed the key criterion on fiscal deficit, but the situation on arrears improved significantly. Likewise, the drastic reduction of transfers and subsidies positively impacted public finances, as had debt relief under the HIPC and MDRI initiatives. Going forward, my authorities have initiated a thorough analysis on the relevance of the convergence criteria in light of recent 2 major developments. In this regard, they view as critical the setting of a new criterion that ensures debt sustainability.

The overall agenda of harmonizing the practices in public finance management is proceeding well. Member countries' authorities are working towards transposing in their national frameworks the WAEMU directives on public financial management. These directives are meant to harmonize within the Union, the rules for the preparation, submission, approval, execution and control of budgets, and to encourage efficient and transparent management of public finances in all countries.



## **II. Development of Financial Markets and Monetary Policy**

Membership in the Franc Zone, which has a common currency pegged to the Euro, has been beneficial to the countries as it has been a source of stability. Thanks to a stable exchange rate which remains in line with fundamentals, my authorities have used appropriately monetary policy in their efforts to stabilize the macroeconomic framework. Yet, they are cognizant of the weaknesses of the financial system that still impede the proper transmission of monetary policy and hence limit the ability of the BCEAO's instruments to control inflation. The central Bank has initiated a variety of reforms to modernize and strengthen the financial markets in this regard. One critical reform to be launched by mid-2013 aims to deepen the interbank market including by introducing collateralized operations to address the reluctance of liquid banks to lend to illiquid ones.

The BCEAO has also taken steps to better organize and develop the government debt market. Measures underway include: (i) the rollout of an electronic platform to auction and trade liquidity and government paper ("application Trésor"); (ii) the introduction of primary dealers, which should accelerate the development of the secondary government debt market; and (iii) the establishment of a regional debt agency, which will advise national treasuries and help improve issuance coordination.

My authorities are committed to continue to take measures aimed at deepening and strengthening the financial system which remains dominated by banks to date. Though the banks are liquid and well capitalized, my authorities are aware of the main challenges of the sector, as evidenced in the pilot studies on Benin and Senegal. Critical weaknesses include shallowness of the sector, high concentration of credit, insufficient transparency and informational asymmetries, weak business environment and legal and judicial frameworks, and regulatory and supervision issues.

My authorities have stepped up actions on many fronts to address these weaknesses. The BCEAO has recently overhauled some key prudential ratios. As an example, at the request of banks, the transformation ratio now requires that only 50 percent of long term deposits should finance long term lending, compared to the previous ratio of 75 percent, which was a major obstacle to lending. In the same vein, the central bank has also launched the preparatory work to establish a credit bureau, which will gather information on customers and facilitate lending in the Union. The BCEAO-initiated reforms are being complemented by national initiatives. Many governments have adopted financial sector development 3 strategies with the view to improve financial inclusion and enhance credit to the private sector, especially SMEs. The improvement of the overall business climate in most countries of the Union has attracted new banks to the region and the ensued competition has benefited the consumers, especially the formerly unbanked segments of the population.

## **III. Structural Transformation and Growth**

In addition to conducting a sound policy mix to maintain macroeconomic stability and reforms to deepen the financial sector to support the private sector, my WAEMU authorities

pay due regard to policies aimed at engineering a structural transformation of the Union's economies and further unleash area-wide growth.

Output is expected to remain robust in 2013 and at about 6 percent in the medium term. This trend should be backed by the member countries' planned large public investments. Most countries, including Cote d'Ivoire and Niger, have recently unveiled national development plans to be implemented over the coming years and which are geared on buoyant investment from the public and private sectors. These plans have secured large support from official donors and private investors. Closing the infrastructure gap remains one of the key elements of the country authorities' agendas. A concerted effort is underway in this area, and national efforts are well complemented by intraregional infrastructure projects. The WAEMU Commission is working on a vast array of transportation corridors, which will connect capital cities within the Union, and thus facilitate integration between the economies and boost areawide growth.

My authorities have also worked expeditiously to address the energy issue. The regional fund created in this regard has helped finance urgent projects to address electricity shortages in most of the Union member countries. My authorities continue to work on long-term projects capable of increasing the energy supply and reduce its costs for states' budgets. Progress on these fronts of transportation and energy should help boost the price and nonprice competitiveness of the region, and advance integration. Likewise, the second phase of the Regional Economic Program should help lift barriers to trade, enhance regional integration and harness its growth dividends. Furthermore, it should avail additional resources to complement national efforts to support enterprises and hence broaden the industrial base and increase the share of manufactured goods in the region's exports. In so doing, the economies of the Union should be able to bolster trade and create highly needed employment opportunities.

## **Conclusion**

Despite new political and security challenges in 2012, the WAEMU region has harnessed the peace dividends from Cote d'Ivoire and benefited from buoyant activity in key sectors. This trend is expected to hold and growth should continue to be robust in 2013 and over the medium term. My WAEMU authorities are fully aware of the challenges still facing the region's economies and are committed to implement the appropriate policies for these favorable prospects to materialize.

For the period ahead, my authorities will step up their efforts to revamp the regional surveillance framework with the view to enhancing compliance of member countries and prevent risks. The conduct of macroeconomic policies will go hand in hand with structural reforms to deepen the financial sector and make it a vibrant support to private activity. In the same vein, the WAEMU authorities will leverage regional instruments to accompany the structural transformation of the region's economies, strengthen the private sector and enhance area-wide employment.