INTERNATIONAL MONETARY FUND

IMF Country Report No. 16/272

CENTRAL AFRICAN REPUBLIC

SELECTED ISSUES

August 2016

This Selected Issues paper on the Central African Republic was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed on July 8, 2016.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

CENTRAL AFRICAN REPUBLIC

SELECTED ISSUES

July 8, 2016

Approved by
The African Department

Prepared by Haiyan Shi with technical assistance from Maggie Attey

CONTENTS

This paper examines the underlining causes of Central African Republic's (C.A.R.) "fragility trap" and sheds light on the factors linked to building resilience. The persistence of fragility in C.A.R. is attributed to multiple factors: lack of political cohesion and state weakness that led to protracted political crises and conflicts, weak capacity and poor commitment to build economic institutions and implement pro-growth policies and reforms, and an inability to generate or appropriately use fiscal buffer. By looking into the experiences of seven SSA countries that have managed to make progress towards exiting fragility, the findings underscore the need for promoting peaceful and inclusive societies, strong international support, and building effective, accountable and inclusive institutions especially fiscal institutions—as a foundation for building resilience in C.A.R. to exit fragility.

A. Introduction

1. **This paper examines the history and sources of fragility in C.A.R. and sheds light on the factors linked to building resilience by looking into seven SSA countries that have managed to make progress on building resilience towards exiting fragility**. C.A.R. is a unique case where conflicts and political instability have been a permanent feature since independence. Understanding some of the factors contributing to such a fragile environment will help better shape policy options and choices. The findings highlight that political inclusion, which maintains peace and limits political conflicts, fiscal buffers and sound fiscal institutions and scaling up development aid are critical to build resilience and exit fragility.

2. **The rest of the paper is organized as follows**: Section II reviews the history and sources of fragility in C.A.R. Section III assesses factors linked to building resilience by looking into a few other SSA's experience on building resilience necessary for exiting fragility. Section IV concludes and provides policy recommendations for C.A.R.

B. History and Sources of Fragility in C.A.R.

3. **The political situation in the C.A.R. has been characterized by recurrent instability, with a long string of coups and civil conflicts since independence (Box 1).** Since independence the country experienced political and military conflicts, coup attempts and humanitarian crises. Each crisis escalated further with the most serious ones taking place over the last decades. The latest crisis, in 2012, went one step further, as it gave rise to an ethnic and religious fracture. Widespread lawlessness and violence led to a humanitarian crisis, pushing ¼ of the population to internally displaced persons (IDPs) and refugee camps. The destruction of an already poor infrastructure, the disintegration of state authority, and the fragmentation of the social fabric along religious lines pushed the country further into fragility. The economy collapsed and the gains on the poverty front made during the previous decade were reversed.

4. **Sources of fragility in C.A.R. are multiple.** C.A.R.'s main sources of fragility (World Bank, 2016) include: (i) a lack of common vision and inclusiveness that would facilitate a political arrangement with strong leadership to adopt the set of policies that promote economic and political stability; (ii) weak governance, ineffective institutions, and low capacity;

(iii) underdevelopment, lack of education and employment opportunities; and (iv) a lasting state of political instability, conflicts and insecurity.

5. **These sources of fragility interactively reinforce each other in C.A.R. and keep C.A.R. in a persistent "fragility trap", i.e., a vicious circle of political instability and conflicts, underdevelopment, and weak state capacity.** Protracted political crises and conflicts led to a deficit of institutions, the disintegration of the state, and a permanent state of fragility in C.A.R. The persistent political instability and social unrest undermined efforts to develop the country's rich and diverse endowment and set the economy on a sustainable development path. The outcomes have been economic declines, pervasive poverty, rampant corruption and further political and social fragmentation which reinforce and keep C.A.R. in a fragility trap.

Box 1. Central African Republic: Key Political Events Since Independence

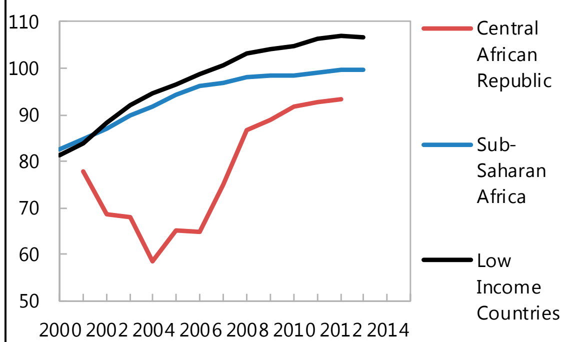
1960 - The C.A.R. becomes independent with David Dacko as president. He turns country into a one-party state.
1965 - Dacko ousted by the army commander, Jean-Bedel Bokassa, who declares himself emperor of the "Central African Empire".
1979 - Bokassa ousted in a coup.
1981 - Army commander Andre Kolingba seizes power.
1993 - Ange-Felix Patasse wins presidential elections, ending 12 years of military rule.
2003 - Rebel leader and former army commander Francois Bozize seizes power.
2009 - Clashes between government and rebels are ongoing. UN Security Council agrees to creation of UN peace building office for C.A.R. to address ongoing insecurity.
2012 - November—New Seleka rebel coalition rapidly overruns north and centre of country, and eventually the capital.
2013 - Turmoil as rival Muslim and Christian fighters are accused of killing hundreds of people.
2014 - Michel Djotodia—coup leader who headed the Seleka coalition—quits as president. Catherine Samba-Panza takes over as interim leader.
2015 - Pope Francis visited Bangui November 29–30. Referendum on constitutional changes in November, followed by first round of presidential election.
2016 - Tension ahead of second round of presidential election which, however, passes off peacefully. Constitutional court had earlier annulled parliamentary election results, citing irregularities

Source: http://www.bbc.com/news/world-africa-13150040

6. **The long history of fragility and conflict in C.A.R. has kept the country in extreme poverty with the lowest ranking of social and economic development in the world, despite its vast natural resources (Figure 1).** With a per Capita GDP of US$332 in 2015, C.A.R. is one of the poorest countries in the world. Even before the onset of the 2013 political and security crisis that devastated the country's economy, the poverty rate in C.A.R. (62 percent) was one of the highest in the world. Social indicators place C.A.R. among the least developed countries in the world. The 2015 Human Development Report ranked C.A.R. at 187 out of 188 countries, with a Human Development Index significantly lower than the average Sub-Saharan Africa. Life expectancy (51 years) remains among the lowest in the world, and infant and maternal mortality rates have deteriorated over time. Significant regional-and gender-based disparities in education, health, and the continued loss of economic opportunities have reduced the country's growth potential.

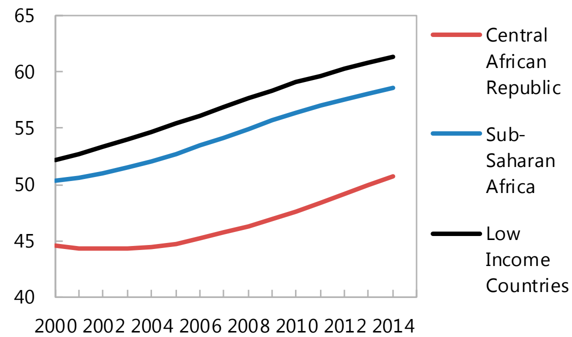
Figure 1. Central African Republic: Comparison of Social and Economic Indicators, 2000-14

Gross Enrollment Ratio, Primary, Both Sexes (%), 2000-2013



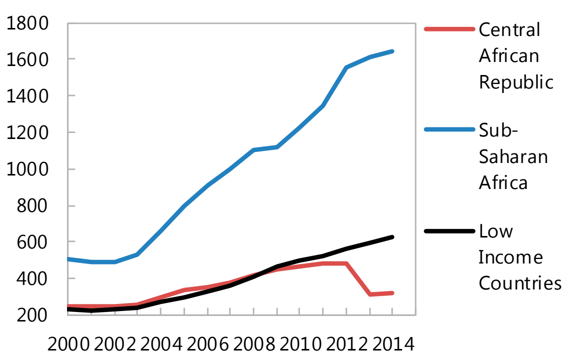
Source: World Development Indicators, World Bank

Life Expectancy at Birth, Total (years), 2000-2014



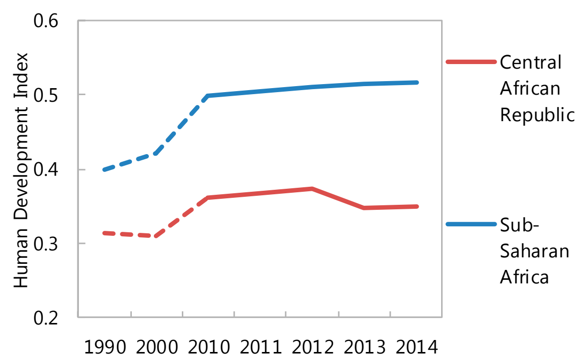
Source: World Development Indicators, World Bank

GNI (current US$), 2000-2014



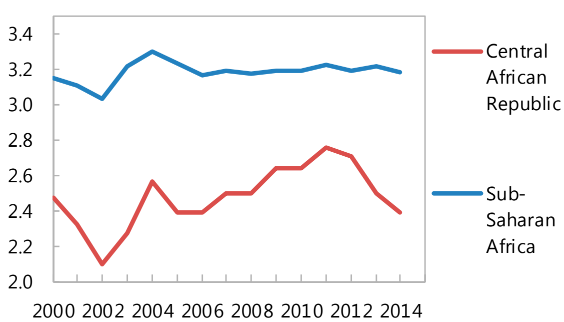
Source: World Development Indicators, World Bank

HDI trends, 1990-2014



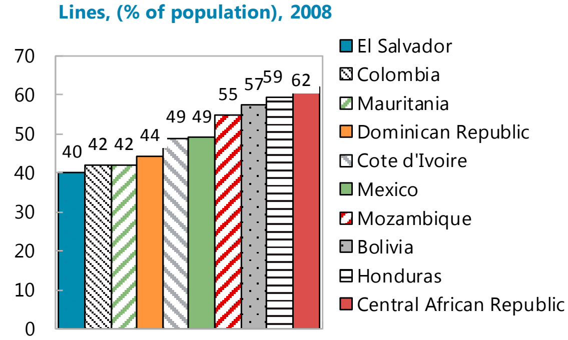
Source: 2015 Human Development Index, UNDP

Country Policy and Institutional Assessment, 2000-2014



Source: World Development Indicators, World Bank

Top Ten Poorest Countries: Poverty Headcount Ratio at National Poverty Lines, (% of population), 2008



Source: World Development Indicators, World Bank

C. Experience of Seven Sub-Saharan African Countries (SSA) in Exiting Fragility

7. **According to a recent study by IMF (2015a), seven SSA countries have built resilience toward exiting fragility.** The study examined the 44 SSA countries by using the World Bank's Country Policy and Institutional Assessment (CPIA) ratings and incidents of conflicts to define fragility. If one country's average score of on the CPIA ratings are below 3.2 or experienced conflicts in the 1990s, it is considered as fragile. When a country improves its rating above 3.2, it is defined as out of fragility. If a country is deemed fragile in the 1990s but not in 2011–13, it is considered to be "becoming resilient". Seven countries have been identified as "becoming resilient": Cameroon, Ethiopia, Mozambique, Niger, Nigeria, Rwanda and Uganda. Using the same methodology of defining fragility, the most fragile period for each country was identified (Table 1). The study also finds that the process of building fragility is not rapid and fragility is persistent and it took about seven years on average for these seven countries to exit fragility.

Table 1. Seven SSA Countries: Most Fragile Period and Years of Exiting Fragility

	Most fragile year	CPIA score of: The most fragile year	CPIA score of: 2014	Years of exiting fragility
Cameroon	1993	2.0	3.1	10
Ethiopia	1991	2.2	3.5	3
Mozambique	1985	2.4	3.5	3
Niger	1993	2.0	3.4	11
Nigeria	1994	1.9	3.5	13
Rwanda	1994	1.4	4.0	5
Uganda	1985	1.2	3.7	4
Average		1.9	3.5	7

Sources: IMF(2015a), World Bank, and author's calculations.

8. **A panel regression model of the seven countries is used to identify the role of fiscal institutions and buffers, development aid, and social spending in building resilience.** The model regresses the CPIA index of the seven countries on the following independent variables: development aid, tax revenue and current expenditure, education and health expenditures (all in percent of GDP). Following IMF (2015b), three variables - inflation, growth of real GDP per capita, and terms of trade - are used as control variables. The sample period covers 14 years from the most fragile year for each country.

9. **The estimation results suggest that maintaining macroeconomic stability, building strong fiscal institutions and creating fiscal buffers, scaling up development aid and social spending can help the countries in building resilience towards exiting fragility (Table 2).** The results show that maintaining macroeconomic stability (higher growth and lower inflation) will contribute to build resilience. Both the coefficients (Table 2, column 1) are significant at 1 percent

level and have the correct signs. Looking at the effect of fiscal institutions and fiscal buffer (Column 2), both the coefficients of tax revenue and current expenditure in percent of GDP are significant at the 1 percent level and have the correct signs, indicating mobilizing domestical resources and containg current spending would contribute to building resilience. The coefficient of development aid in percent of GDP is significant in all specifications and has the positive sign (columns 3, 4 and 5), demonstrating that developmental aid is beneficial to helping countries exiting fragility. The coefficients of education and health spending in percent of total spending are significant in some specifications and have the correct sign (columns 3, 4, and 5).

Table 2. Panel Estimation Results: 14 Years from the Most Fragile Year

Variables	1	2	3	4	5
CPIA (t-1)				0.835***	0.785***
				(0.107)	(0.117)
Inflation	-0.004***	-0.002	0.006	0.001	0.001
	(0.001)	(0.002)	(0.006)	(0.004)	(0.004)
Real GDP per capita growth	0.018***	0.005	-0.013	-0.016*	-0.013
	(0.005)	(0.004)	(0.014)	(0.009)	(0.008)
Terms of trade		0.003***	0.002**	0.001*	0.001
		(0.000)	(0.001)	(0.001)	(0.001)
Development aid/GDP			0.018**	0.011**	0.017***
			(0.008)	(0.005)	(0.006)
Tax revenue/GDP		0.069***			
		(0.014)			
Current expenditure/GDP		-0.035***			
		(0.012)			
Education expenditure/total Exp.			-0.007	0.012**	0.012**
			(0.008)	(0.006)	(0.006)
Health expenditure/total Exp.			0.025*	0.005	0.003
			-0.014	(0.009)	(0.002)
Constant	3.356***	2.661***	2.720***	0.041	0.182
	(0.055)	(0.218)	(0.235)	(0.385)	(0.401)
Number of observations	141	121	47	46	46
R-square	0.6795	0.2822	0.4963	0.9764	0.9527
Wald Chi-square	27.88	62.27	24.33	114.27	118.07

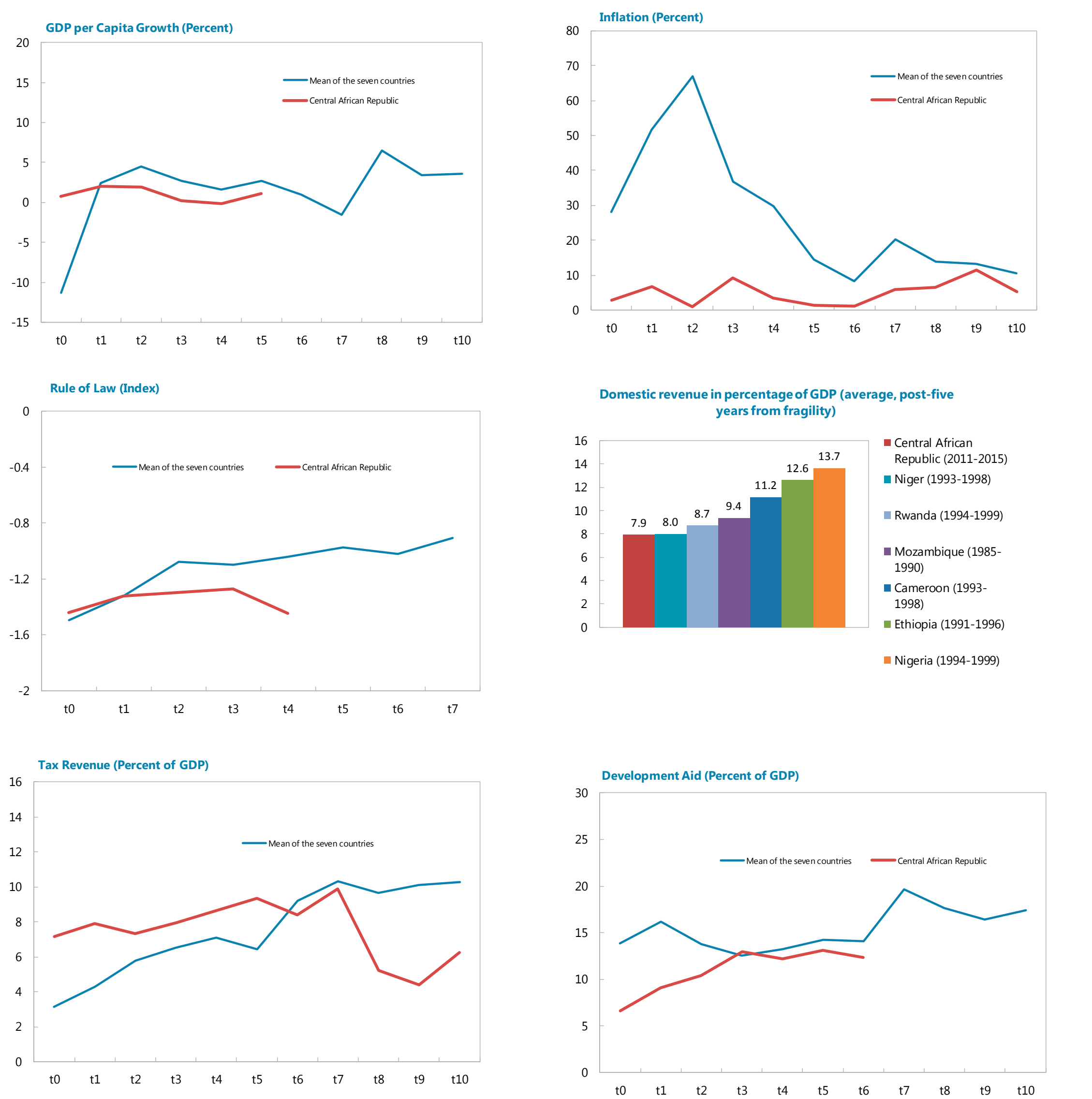
Source : Authors' calculations. The dependent variables is the CPIA rating (World Bank).
(***) indicates statistical significance at the 1 percent level, (**) at the 5 percent level, and (*) at the 10 percent level.

10. **Combining the model results with other qualitative specifications of the countries (Figure 2), we conclude that the key drivers to build resilience are the following:**

- Maintain macroeconomic and political stability. Macroeconomic and political situation improved in all seven countries significantly in the five years after the most fragile period as shown in

Figure 2. Growth is picking up and inflation is declining. Post-conflict stabilization in these countries focused on reaching a common vision that facilitated the adoption of economic policies and reforms which promoted economic stability and improved governance and enhanced the capacity and legitimacy of the state. The political stability is gradually established as indicated by the improvement of the rule of law index.

Figure 2. Selected Indicators Comparisons between the Seven Countries and C.A.R, Post Fragility



- Build institutions. Countries in the sample successfully improved the regulatory framework, transparency and effectiveness in public spending. These reforms help minimize rent seeking behaviors and government excesses.

- Build fiscal buffer. All seven countries made good progress in building fiscal buffer, measured here as improvement in tax revenue, and higher investment and social spending. Specifically, the seven countries successfully mobilized fiscal revenue, lowered current spending and debt services (through debt relief), and sustainably increased domestically financed capital expenditure and health and education spending.

- Tailor fiscal reform sequencing according to the specifics of each country. Generally, findings of Gupta et. al. (2007) point to a three-step process of strengthening fiscal institutions: (1) creating a sound legal framework, (2) establishing a central fiscal authority that acts as a coordinating body for foreign assistance, and (3) designing appropriate tax policies while simultaneously introducing simple tax administration and expenditure management arrangements. However, depending on country-specific factors, such as their stage of development, the sequencing of the fiscal reforms varies from country to country and some countries received substantial technical assistance in their reforms.

- Receive substantial external support from international organizations and aid agencies, in terms of budget support, aids, project grants, debt relief, and technical assistance in capacity building. Table 3 shows that the majority of these seven countries received substantial developmental aid in the first 10 years since the most fragile year, while CAR received, in the first two years following the 2012 crisis development aid well below 10 percent of GDP. On a positive note, development aid is expected to hover around 13.5 percent of GDP over the next five years. Expected financial assistance to support a critical security sector reforms (SSR) and a DDR would come in addition to the traditional development aid—and help address a key source of fragility.

Table 3. Seven SSA Countries: Developments Aid (% of GDP), First 5 and 10 Years Since the Most Fragile Year

	Average first 5 years	Average first 10 years
Nigeria	0.6	0.5
Cameroon	5.7	5.4
Uganda	7.7	12.1
Ethiopia	11.7	10.5
Niger	16.9	15.3
Mozambique	22.8	36.9
Rwanda	32.4	26.7

Source : UNCTADstat.

D. Policy Recommendations

11. **The immediate task for C.A.R. is to facilitate the basis for economic recovery by fostering long-lasting domestic security, maintaining political stability, and improving macroeconomic performance.** The peaceful presidential and parliament elections bodes well for C.A.R.'s return to democratic institutions and the restoration of peace and offer the new government a window of opportunity to implement economic and social reforms. If the political and macroeconomic stability can be sustained, it would engineer a rapid economic recovery that can increase employment, disarm and reintegrate combatants into civilian roles, and potentially prevent resurgence of political and security instability and avoid reversal to fragility trap. Furthermore, it is crucial to build partnerships and a strong coordination mechanism between the United Nations, European Union and other donors, and political and security partners to ensure a lasting peace in C.A.R.

12. **Public expenditure should be oriented to priority spending such as health, education and security expenditures and public investment that are essential for engineering inclusive growth and maintaining political stability.** Higher health and education spending would contribute to human capital investment and improve the odds of building resilience. Higher spending on social, security, and capital investment can consolidate the basis for economy recovery and boost private sector development which is crucial for creating more job opportunities.

13. **At the same time, it is critical for the government to build strong fiscal institutions that improve governance, transparency, and accountability.** The goal for the government is to foster development to achieve sustained improvements in livelihoods through an inclusive growth process. Stability and development can only be achieved by mobilizing sufficient domestic revenues and improving public expenditure management. To mobilize more tax revenues, it is important for the government to review and implement the action plans designed with the support of FAD and AFRITAC, with an immediate focus on some low hanging fruits, such as the adopting a revised price structure for petroleum product taxation and forestry exports. In the medium term, streamlining of tax exemptions and a simplification of the tax systems would increase revenue and improve collection. To improve public financial management, it is critical to restore normal budget procedures and put strict limits on the use of emergency expenditure, restore the single treasury account, strengthen the Central Accounting and Treasury Agency (ACCT), which is critical to improve transparency in the budget execution and treasury operations, and rationalize wage expenditure. In the context of the low capacity of the government, the sequencing of implementing these action plans is also important. Efforts and resources should first focus on low "hanging fruits" such as strengthening cash management, VAT and petroleum taxation and implementing single treasury account. In addition, the process of building effective fiscal institution needs to be supported by substantial technical assistance from international community.

14. **Scaling up external budget assistance and technical support in capacity building can help C.A.R. address their daunting challenges of overcoming persistent fragility.** As

the process of building resilience to exit persistent fragility in C.A.R. is a long process and subject to risks of relapses, effective engagement from the international community in financing essential spending in areas of social service and security is crucial to promote security, enhance the provision of key public services and reconstruction. In Figure 2, a comparison with the seven countries indicates that there is an urgent need to boost development aid for C.A.R. To sustain the long-lasting peace and meet the development needs, C.A.R. needs more devoting efforts and resources from international community in improving institutions and governance, encouraging private sector development, and attracting foreign direct investment. International community can provide the much-needed technical assistance aimed at building capacity and supporting domestic processes in the design and implementation of C.A.R.'s national economic and security reform agenda.

15. **The implementation of an ECF supported program can contribute to exit fragility through several dimensions, identified here as critical.** First, in addition to the financial support provided directly by the Fund, an ECF supported program serves as a catalyst to mobilize donors' support. Second, the design of the government structural agenda aims at addressing some of weaknesses that contributed to fragility—in particular in its objective to improve transparency and strengthen the budget process. Third, the focus of the program at improving revenue collection and support spending in critical sectors such as education, health and infrastructure can further support exiting fragility at a time when revenue collections are still low.

References

Gupta, Sanjeev, Shamsuddin Tareq, Benedict Clements, Alex Segura-Ubiergo, and Rina Bhattacharya, June 2007, "Postconflict Countries: Strategy for Rebuilding Fiscal Institutions," (United Nations University: World Institute for Development Economics Research).

International Monetary Fund (2015a), *Building Resilience in Sub-Saharan Africa's Fragile States*, African Department Paper 15/05, (Washington, D.C.: International Monetary Fund).

——————— 2015b, "Exiting from Fragility in Sub-Saharan Africa: The Role of Fiscal Policies and Fiscal Institutions," IMF working paper 15/268, (Washington, D.C.: International Monetary Fund).

World Bank, 2016, "Central African Republic Fragility Assessment", (Washington, D.C.: the World Bank Group).