



# CENTRAL AFRICAN ECONOMIC AND MONETARY COMMUNITY (CEMAC)

## SELECTED ISSUES

October 2014

This Selected Issues paper on the Central African Economic and Monetary Community (CEMAC) was prepared by a staff team of the International Monetary Fund. It is based on the information available at the time it was completed on July 11, 2014.

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](mailto:publications@imf.org) Web: <http://www.imf.org>  
Price: \$18.00 per printed copy

**International Monetary Fund**  
**Washington, D.C.**



# CENTRAL AFRICAN ECONOMIC AND MONETARY COMMUNITY (CEMAC)

## SELECTED ISSUES

July 11, 2014

Approved By  
The African Department

**Prepared By:** Zaki Dernaoui, Mariam El Hamiani Khatat,  
José Gijon, Nathalie Pouokam, Boriana Yontcheva and  
Aleksandra Zdzienicka

## CONTENTS

<b>IMPROVING LIQUIDITY MANAGEMENT AND THE OPERATIONAL FRAMEWORK OF MONETARY POLICY</b>	<b>3</b>
A. Current Challenges for Regional Monetary Policy	3
B. Toward more effective monetary policy operations	9
<b>FIGURES</b>	
1. Current Account Shocks, BEAC Balance Sheet and Credit Dynamics in CEMAC	5
2. BEAC Interventions and Interbank Market Activity	7
3. Reserve Requirements (RR) & Excess Reserves (ER)	8
4. Monetary Operations Infrastructure: the Building Blocks	10
<b>FINANCING PUBLIC INFRASTRUCTURE INVESTMENTS</b>	<b>12</b>
A. The Infrastructure Gap	12
B. Tapping into Private Finance	12
C. International Experience	16
<b>BOX</b>	
1. Recommendations for the Mitigation of Non-Financial Constraints to Infrastructure Financing	15
<b>FIGURES</b>	
1. Common Models of Public-Private Partnerships	13
2. Bottlenecks to Private Participation in Africa's Infrastructure Projects	14

<b>PUBLIC INVESTMENT SCALING-UP, GROWTH AND DEBT DYNAMICS</b>	<b>17</b>
<b>BOX</b>	
1. Key Model Features	17
<b>FIGURES</b>	
1. Baseline Scenario	19
2. Alternative Scenarios for Efficiency and Return to Public Investment	20
3. Alternative Scenario: Shocks to Oil Resources	21
<b>GROWTH AND COMPETITIVENESS IN CEMAC</b>	<b>22</b>
A. Role of External and Domestic factors	22
B. Role of Business climate, Governance, and Competiveness	25
C. Policy actions and Reforms	29
<b>BOX</b>	
1. The World's Economic Forum Global Competitiveness Index (GCI)	29
<b>FIGURES</b>	
1. Growth Performance	23
2. External Environment	23
3. Macroeconomic Environment	26
4. Business Institutional Environment	27
5. Productivity and Structural Competiveness	28
<b>TABLE</b>	
1. Growth Regression	24
<b>REFERENCES</b>	<b>31</b>
<b>FINANCIAL INCLUSION IN THE CEMAC</b>	<b>32</b>
A. Introduction	32
B. Financial Development and Inclusion in the CEMAC: Benchmarking and Cross Country Comparisons	33
C. Microfinance and Mobile Banking Services	37
D. Financial access and inequality	37
E. Policy Recommendations	38
<b>FIGURE</b>	
1. Benchmarking Access to Financial Services	35
<b>REFERENCES</b>	<b>39</b>

# IMPROVING LIQUIDITY MANAGEMENT AND THE OPERATIONAL FRAMEWORK OF MONETARY POLICY<sup>1</sup>

## A. Current Challenges for Regional Monetary Policy

### Excess liquidity and the conduct of monetary policy

**1. In the CEMAC region, structural excess liquidity stems not only from a monetary expansion as a result of the surge in oil revenues but also from liquidity management weaknesses.** While excess liquidity has not affected price stability in the CEMAC region, it constrains money market development and the reliance on market-based monetary policy. The BEAC's main monetary policy rate is currently set at 3.25 percent while lending rates are reaching 13 percent in some CEMAC countries. Disconnected policy and lending rates reflect the ineffective interest rate channel of monetary policy transmission while the shallow domestic banking system and the underdeveloped financial markets induce weaknesses of both the credit and asset price channels. Further, the peg of the Franc CFA to the Euro leaves little room for the exchange rate channel to play a role in the monetary policy transmission mechanism.

**2. The exchange rate policy combined with Government subsidies and other policies aimed at containing high costs of living contribute to inflation stabilization.** Yet, with capital controls in place, the BEAC has some leeway in terms of strengthening its monetary policy efficiency and control over inflation stabilization through an orderly move to a more market-based monetary policy. In doing so, the BEAC should continue its efforts of curtailing its direct financing to governments, and consider that in the presence of exogenous shocks and developing capital markets, the relation between money and inflation may experience some instability calling for an overall revision of its monetary policy framework.

**3. In the absence of an efficient interest rate channel, liquidity plays an important role in the conduct of monetary policy.** The CEMAC economy is vulnerable to external shocks and its banking system potentially exposed to liquidity shocks. Oil revenues determine Governments expenditures, which in turn affect banks resources and liquidity. With lack of appropriate instruments for liquidity management, banks hold excess reserves to withstand liquidity shocks. Inefficient liquidity management of individual banks, high counterparty and credit risk, and lack of collateral explain the high lending rates. Liquidity shocks combined with distortions in credit supply and demand result in unstable credit growth rates (Figure 1). On the supply side, the inability of banks to assess risks together with weak guarantees and collateral schemes impose constraints on the flow of credit to the private sector.

<sup>1</sup> Prepared by Mariam El Hamiani Khatat.

**4. In this context, BEAC's interventions have contributed to injecting liquidity in a system already in liquidity surplus.** While observing excess liquidity in the banking system, the BEAC is at the same time refinancing a few banks in need. Excess reserves represented in 2013 around 200 percent of reserves requirements. In order to incentivize banks to recycle liquidity through the interbank market, the BEAC stopped its liquidity withdrawing operations in June 2012, but the interbank market has remained even more sluggish than few years ago. There were no interbank volumes reported from August to December 2013, against monthly averages of 23, 16 and 9 billion FCFA reported in 2001, 2005 and 2010 respectively.

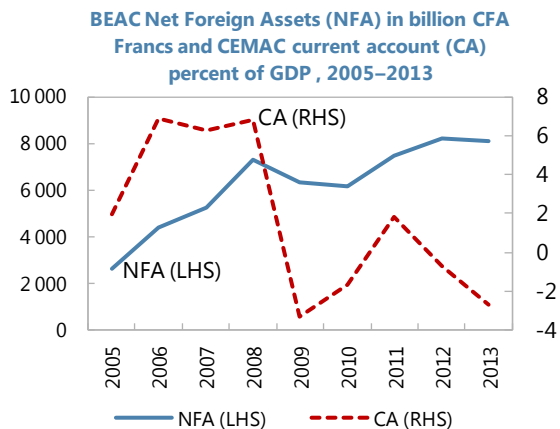
**5. Successful monetary policy implementation requires a set of appropriate instruments to cope with various liquidity shocks.** The origins of the surplus liquidity should be well known upfront and addressed with a suitable combination of measures, including foreign exchange, fiscal and financial system development policies. A close coordination between the BEAC, Governments and market operators is necessary in addressing the situation through an optimal combination of reserve requirements and Government bonds market development. In the case of CEMAC, excess liquidity may reflect various factors, including increased oil revenues converted in government expenditures, inefficient liquidity management, lack of money markets instruments, and a shallow domestic banking system.

**6. A streamlined and well-understood operational framework eases banks liquidity management and fosters interbank trading.** Conventional monetary policy implementation means that the Central Bank is intervening in the market, on a multilateral basis rather than on a bilateral basis, and is thus responding to the net liquidity demand of the banking system. The Central Bank should either provide or sterilize liquidity depending on the overall banking system liquidity situation. The BEAC has in the past intervened by providing and withdrawing liquidity at the same time as a result of lack of confidence among market operators. Simultaneous liquidity injection and provision constrains money market development, as the BEAC is substituting the market. In order to incentivize commercial banks to recycle liquidity within the banking system, the availability of BEAC support should be in one direction only.

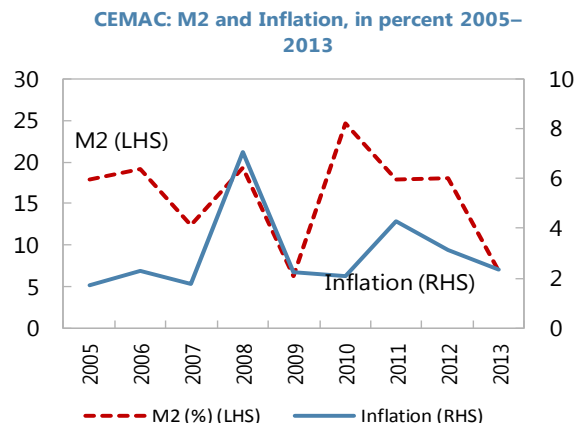
**7. Reserve requirement ratios are currently not harmonized across the CEMAC region, which reflects a differentiated monetary policy stance across countries.** Indeed, limited financial flows between countries and differences between their macro-economic situations resulted in differentiated reserves requirements. The BEAC differentiates countries according to their liquidity situation and imposes three different levels of reserve requirements to three groups of countries: Group I (Congo and Equatorial Guinea) are countries with abundant liquidity, Group II (Cameroun and Gabon) are considered with a satisfactory liquidity situation and Group III (Chad) is seen as having a fragile liquidity situation. Considering its current troublesome situation, the banks in the Central African Republic are currently exempt from reserves requirements. In the absence of an effective interest rate channel, the reserve requirement ratio becomes one of the main policy instruments during the transitional phase to a market-based monetary policy. Therefore, the reserve requirement system plays an important role in the CEMAC region's monetary policy framework and requires moving towards harmonized ratios across countries, thereby reflecting a unified BEAC policy stance. Nevertheless, harmonization of reserves requirements presupposes progress in developing a regional money market, and the ability of the BEAC to manage overall liquidity conditions in the region effectively.

**Figure 1. CEMAC Countries: Current Account Shocks, BEAC Balance Sheet and Credit Dynamics in CEMAC**

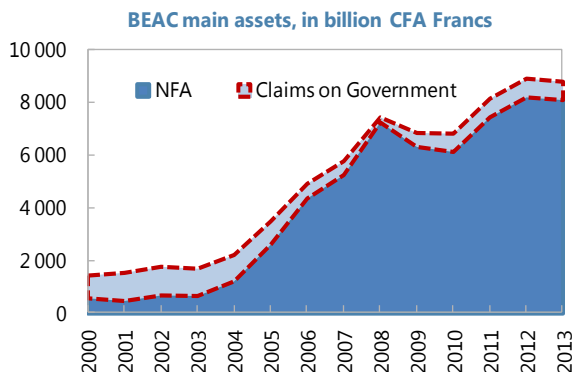
During the current account positive shocks ...



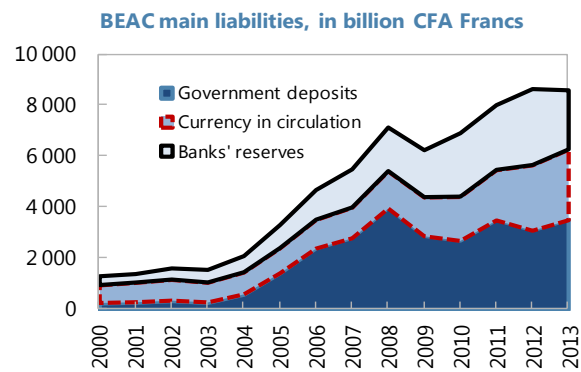
...money growth was high, while inflation overall contained with only one hike in 2008...



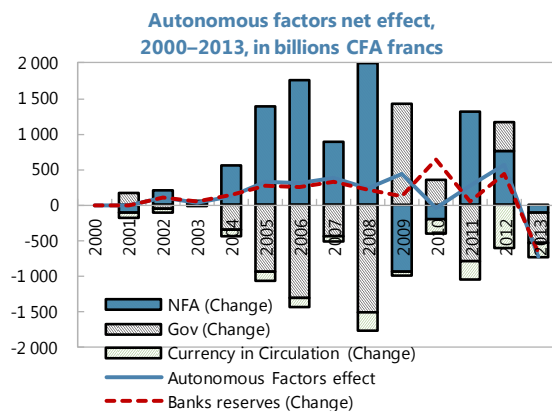
...and BEAC's balance sheet expanded...



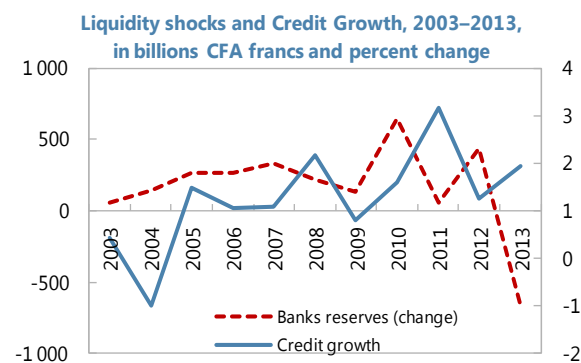
...increasing liquidity on Governments and banks accounts



... unsmoothed liquidity shocks...



...resulted in volatile credit growth



Source: BEAC and staff estimates.

## BEAC's monetary policy operational framework

**8. The ultimate objective of the BEAC's monetary policy is to ensure monetary stability.** At the same time, the BEAC supports the general economic policies elaborated in the Monetary Union.<sup>2</sup> The BEAC operates a monetary programming framework from which it derives the banks' refinancing ceilings and uses several liquidity injection and absorption instruments as well as reserve requirements for the conduct of its monetary policy. BEAC statutes also specify a foreign exchange coverage ratio, defined as the ratio between average BEAC net foreign assets and its average short-term liabilities which cannot be less than 20% over three consecutive months.

**9. Banks' refinancing is provided through two Windows (A and B), both operating as a permanent liquidity provision mechanism, as well as liquidity absorption instruments.**

Window A operations can be either conducted through a seven days auction or for a period of two to seven days. Window A also encompasses exceptional refinancing (*Avances exceptionnelles sous certificats de placements*), ad hoc interventions, as well as interventions at a penal rate. Window B is a permanent refinancing facility for longer-term loans which has been used to support the BDEAC in its efforts to finance regional infrastructure projects. Several liquidity withdrawing instruments have also been used by the BEAC over seven, twenty-eight and eighty-four days maturities.

**10. The BEAC's current operational framework is characterized by four main policy rates.**

The TIAO (*Taux d'Intérêt sur les Appels d'Offres*) is the bidding rate for BEAC's tenders and is presently set at 3.25 percent; the TIPP (*Taux d'Intérêt des Prises en Pensions*) is the rate for ad hoc liquidity injections and based on the TIAO plus 150 to 200 basis points; the interest rate on banks deposits (TISP) is related to liquidity withdrawing operations ('negative' tenders) and varies according to maturities (7, 28 and 84 days). A penalty rate (TPB) is also applied on the overdraft of banks accounts at the BEAC. Policy rates and CEMAC reserves requirements ratios are set and modified by the Monetary Policy Committee.

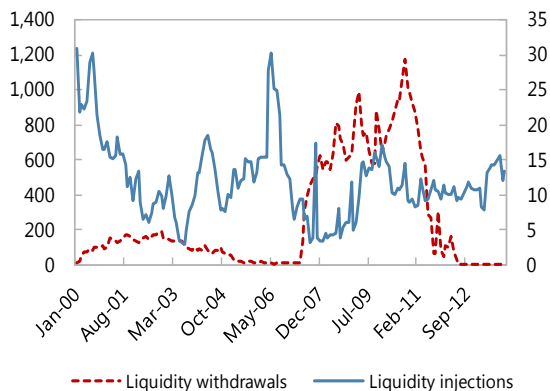
**11. The main challenge for the BEAC is to evolve from setting refinancing ceilings derived from monetary programming to a calibration of Central Bank interventions based on liquidity forecasting processes.** Allowing interest rates to play a larger role in the BEAC's monetary policy will require forward-looking liquidity management based on daily forecasts of autonomous factors. Successful liquidity forecasting is a cornerstone in the process of monetary policy transition to a market-based monetary policy, since it replaces refinancing ceilings by an active calibration of Central Bank interventions on money markets. Exogenous shocks as well as operations of Treasuries and the increase of currency in circulation are translated into liquidity shocks that need to be monitored and properly anticipated by the BEAC. Aware of its constrained monetary policy, the BEAC has drafted an ambitious reform plan of its monetary policy framework. The main challenges for the BEAC are currently (i) the transition to calibrating its interventions based on liquidity forecasting and (ii) streamlining monetary policy instruments.

---

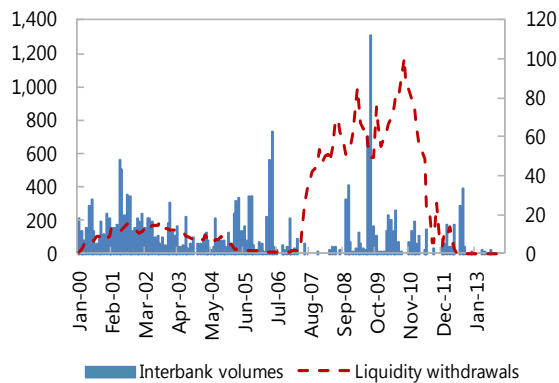
<sup>2</sup> Article 1 of BEAC statutes.

**Figure 2. CEMAC Countries: BEAC Interventions and Interbank Market Activity**

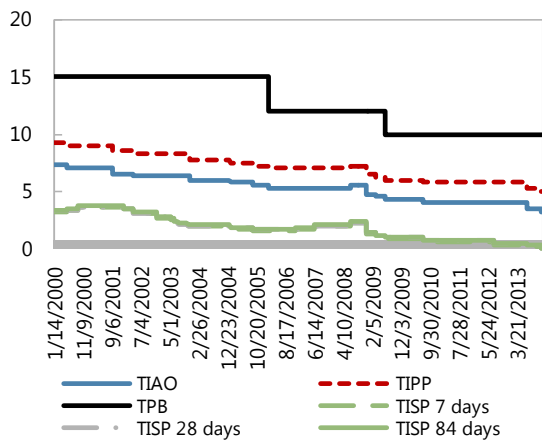
Until 2012, the BEAC was providing and absorbing liquidity at the same time...



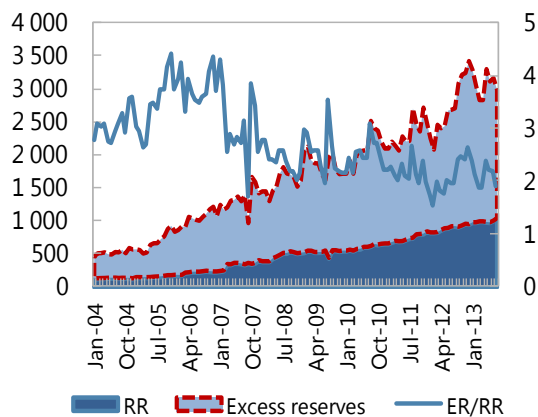
...substituting the market, and leaving the interbank market even more sluggish than few



... policy rates on an overall decreasing trend...

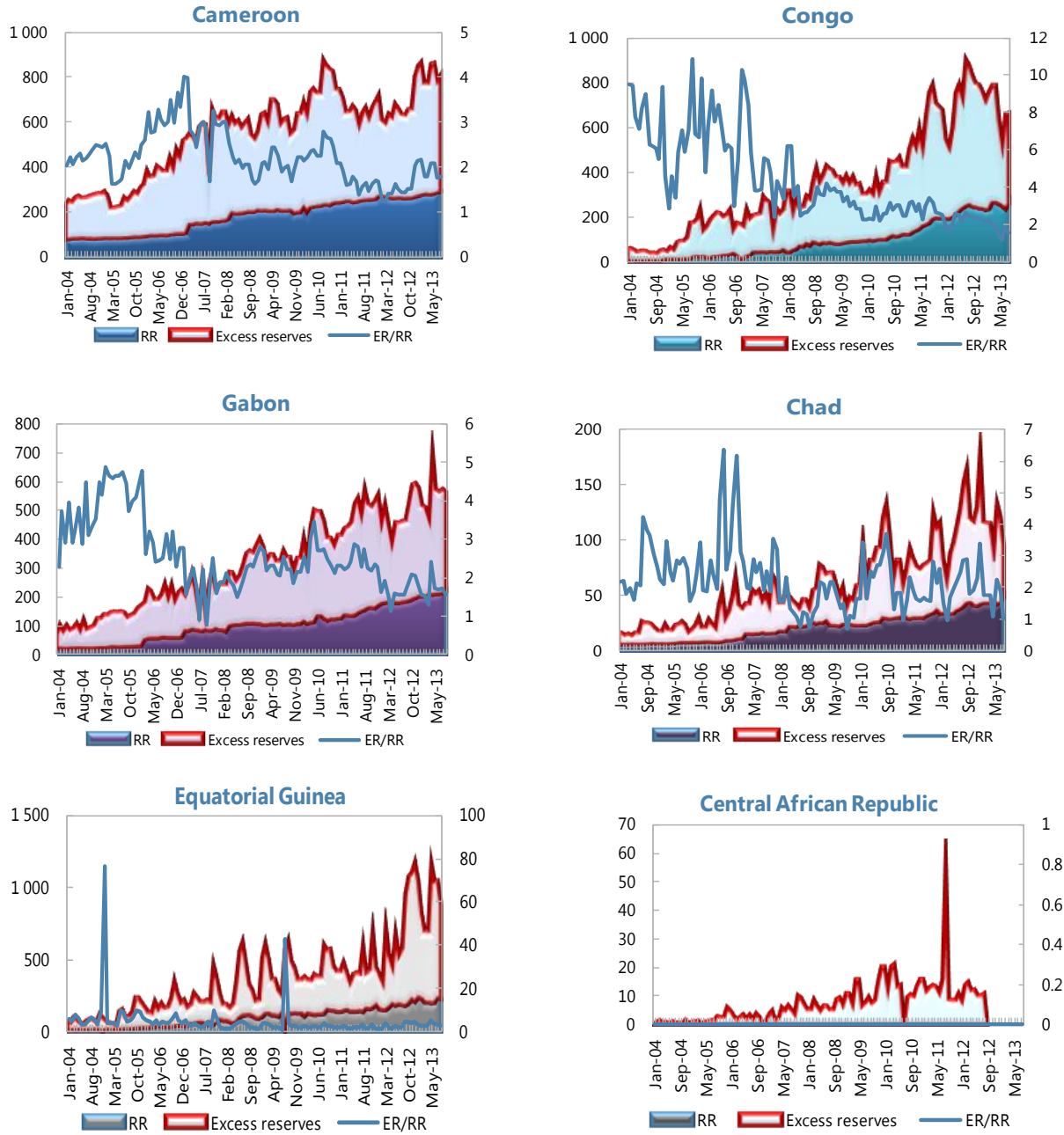


... as well as large unsterilized excess reserves on banks accounts.





**Figure 3. CEMAC Countries: Reserve Requirements (RR) & Excess Reserves (ER)**  
 (Oct. 2001-June 2013, in billions CFA franc )



Sources: BEAC.

## B. Toward more effective monetary policy operations

### Main principles for monetary operations basic infrastructure

#### 12. **Basic infrastructure for a properly functioning interbank market and conventional monetary operations consists of:**

(i) availability of money-market instruments such as repos or collateralized loans used both by commercial banks and the BEAC for liquidity management purposes; (ii) Government bonds in sufficient amount, available for collateral; (iii) active interbank markets; (iv) efficient operational framework; and (v) adequate payment and settlement systems (Figure 3). The operational framework should include not only '*structural*' operations, such as reserve requirements and purchases/sales of Government bonds, but also a set of '*temporary*' instruments needed to accommodate liquidity shocks over different maturities.

#### 13. **An efficient monetary policy needs a repo or collateralized loans market, which reduces both counterparty risks and Government bonds market risks.**

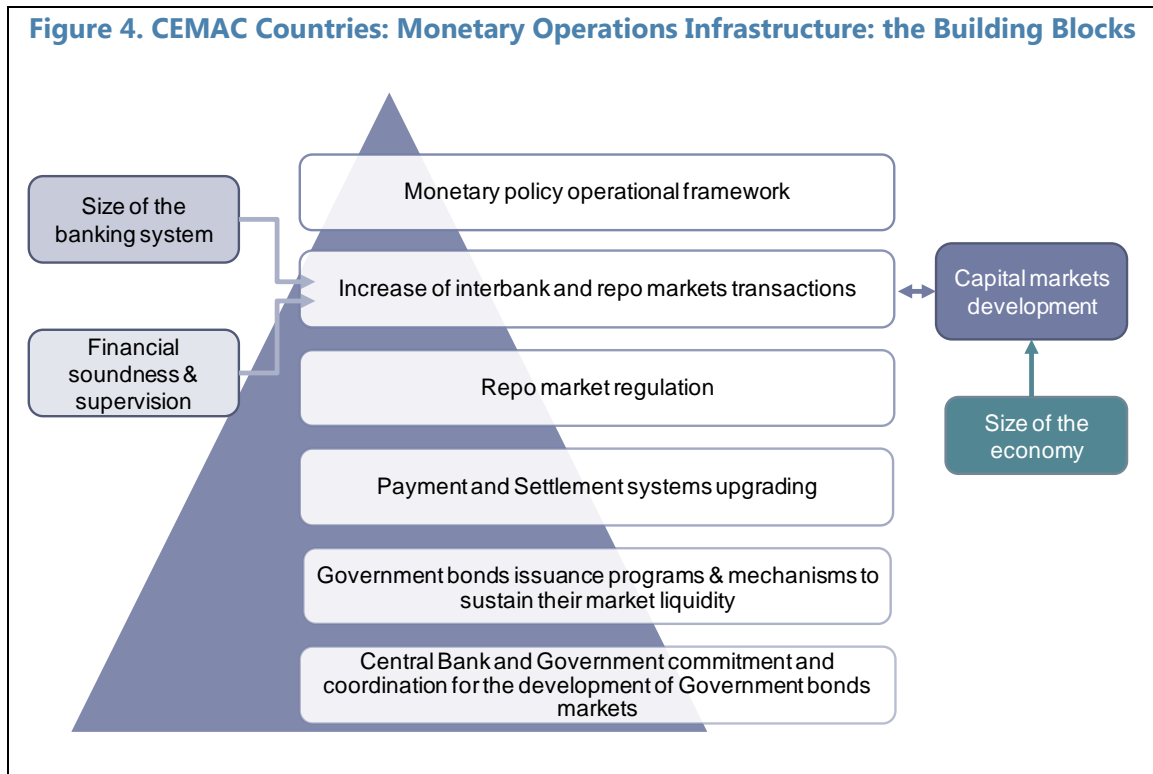
The repo market is an important bridge between money and capital markets not only because of the underlying financial assets but also because nonbank financial institutions can operate on this market and use repo contracts to manage their liquidity. Different categories of markets participants increase the volumes traded on the repo market and its activity can also be supported by financial markets development.

#### 14. **Not only developed money markets but also Government bonds markets are important for monetary policy implementation.**

From an operational point of view, the existence of a liquid, transparent Government securities market reduces the impact of individual transactions on price discovery, thereby easing the transmission of Central Banks actions. Developed Government bonds markets help reduce market risks as they are characterized by low bid-ask spreads and high turnovers. They also facilitate the use of Government securities as collateral not only for Central Bank operations but also between market operators, helping to the development of the repo market. Conversely, developed repo markets increase transactions in Government bonds and sustain their market liquidity.

#### 15. **In 2013, the Treasuries of Cameroon, the Central African Republic and Gabon started issuing Treasury bills (BTA) and Government bonds (OTA) which represents a good step in terms of market and collateral development as well as excess liquidity sterilization.**

Announced issuance volumes for BTA (348.5 billion FCFA in the three countries) were over-bid. Concerning Government bonds (OTA), three issuances were made, two by Cameroon and one by Gabon. The Treasury bills primary market was more active than the Government bonds one during 2013, allowing Cameroon and CAR Treasuries to raise 301 billion FCFA in Treasury bills, while only 49 billion FCFA of Government bonds were issued in 2013.



## Recommended reforms

**16. The BEAC has launched a comprehensive reform of its monetary policy framework but progress has been limited.** While BEAC has a good grasp of the main reform's components, the challenge will be to take actions and to provide the human and IT resources necessary to the reform. Coordination between the different stakeholders (Central Bank, Governments and market participants) is also an important component of the reform's success, taking into account that the BEAC will play a crucial role in money markets monitoring and development during the transitional phase.

**17. Key reform areas include the following:**

- **Structural Excess liquidity:** the BEAC should continue its efforts aiming to curtail its direct financing to governments and encourage governments to issue Treasury bills to repay their existing stock of claims to the central bank. Insolvent banks should be subject to an appropriate resolution regime and in the meantime to specific conditions for accessing BEAC's liquidity provision. A coordination framework should be established with the COBAC to assess the solvency and viability of monetary policy counterparties. Main liquidity provision and absorption volumes should be calibrated according to a region-wide liquidity forecasting process.
- **Monetary policy operational framework:** the number of instruments should be streamlined and a corridor established with floor and ceiling aligned on overnight deposit and lending facilities rates. Window B should be eliminated, and Window A transformed in main refinancing operation at the initiative of the BEAC; a liquidity absorption instrument over the same maturity (weekly) should be established with competitive auctions. The BEAC should avoid using weekly liquidity provision

and absorption instruments at the same time and preannounce the type of intervention to the market. The collateral policy and monetary policy counterparties eligibility criteria should be clearly defined in a BEAC notice.

- **Liquidity forecasting:** the BEAC should investigate all the means to centralize and analyze relevant information for autonomous factors forecasts, including daily operations of Treasuries and foreign exchange operations from its accounting system, as well as banknotes in circulation. Budget laws and Balance of Payment information should be exploited to establish Governments cash flows forecasts, and anticipate the supply and demand of foreign exchange. A close coordination with Treasuries of member States and main operators on the foreign-exchange market should be established. Liquidity forecasting and management processes should be designed to respond adequately to liquidity shocks on the banking system.
- **Money markets integration and development:** The BEAC should play a proactive role in the integration and development of the interbank, repo and Government bonds markets in the CEMAC region as the basis for successful market-based monetary policy and financial markets efficiency. A close monitoring of money markets should be established as well as a regular communication framework with primary dealers, markets operators, and Governments cash management entities. The BEAC should also pursue the work related to the upgrading of payment and settlement systems necessary to support money markets development and integration in the region.
- **Monetary policy analytical framework:** The construction of databases, the implementation of surveys on credit conditions and inflation expectations as well as a deeper knowledge of the monetary policy transmission mechanism should pave the way to macroeconomic modeling. Macroeconomic and financial analysis should be continuously refined to allow a comprehensive understanding of CEMAC growth and inflation determinants, and capture credit, inflation and growth dynamics under external shocks.
- **Human and IT resources:** the BEAC should make all efforts to provide the necessary human and IT resources to the ambitious and comprehensive transformation of its monetary policy framework, which encompasses not only building knowledge and capacities in terms of monetary policy but also financial markets development and infrastructure. Adequate resources are a key component of the success of such reform.

# FINANCING PUBLIC INFRASTRUCTURE INVESTMENTS<sup>1</sup>

## A. The Infrastructure Gap

**1. Like in most of sub-Saharan Africa, the infrastructure gap in the CEMAC remains large.** The World Bank's Africa Infrastructure Country Diagnostic (AICD) estimates<sup>1</sup> that USD 93 billion of yearly spending in public infrastructure (including maintenance costs) would have been needed from 2005 to 2015 for sub-Saharan Africa to fill its infrastructure gap during that period. In most of CEMAC region, basic infrastructure needs remain unmet. Based on AICD's estimates for sub-Saharan Africa and the population share of the CEMAC zone in sub-Saharan Africa, on average, USD 6 billion<sup>2</sup> per year over the next ten years would be needed to meet basic infrastructure needs in the CEMAC.

**2. In 2011–12, CEMAC governments spent USD 12–15 billion on infrastructure, using resources from national governments' revenues and external funding mainly from China and members of the Infrastructure Consortium for Africa (ICA).** According to ICA Annual Reports, during the period 2011–12, China's new commitments in infrastructure financing in Central Africa amounted to USD 11 billion (this included USD 9.7 billion worth contracts for projects in Chad and Cameroon), compared to USD 2.6 billion from ICA members. Between 2011 and 2013, the BDEAC (Development Bank of Central African States) committed about 1 USD billion in infrastructure projects mainly in the form of direct loans to public and private promoters. Projects financed by the BDEAC received co-financing from commercial banks and official development partners including the World Bank, the AfDB, and the French Development Agency. Private sector's contribution to infrastructure financing in the CEMAC remained scarce—in contrast, in 2011–12, the private sector committed nearly USD 20 billion in infrastructure financing in Africa, but mainly in Morocco and South Africa. In order to meet CEMAC's infrastructure needs, authorities should deepen the government securities market and facilitate access to private financing.

## B. Tapping into Private Finance

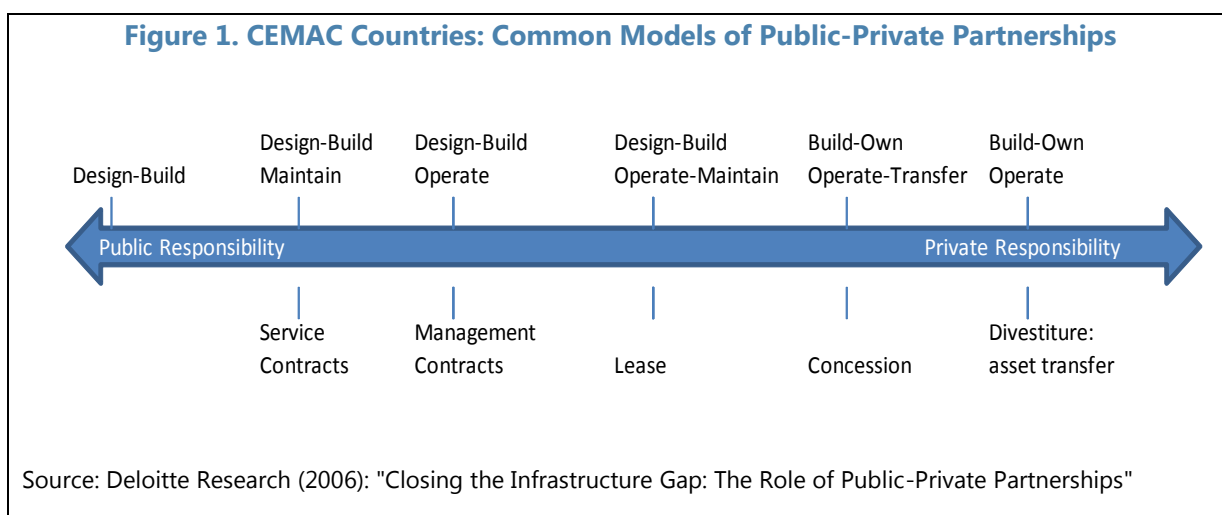
**3. In addition to traditional bonds issuance, market financing for infrastructure projects could also include project bonds for which interests are backed solely by project revenue.** Project bonds could be issued by special purpose vehicles (SPVs) whose liabilities

<sup>1</sup> Prepared by Nathalie Pouokam.

<sup>2</sup> The CEMAC's infrastructure gap is calculated as a population-weighted share of the infrastructure gap in sub-Saharan Africa, assuming a trend inflation rate of 2 percent for inputs used in the production of public infrastructure.

would not cause recourse to assets of the sponsoring agency in the event of a default<sup>3</sup>. With the implicit guarantee offered, project bonds help catalyze market funds when returns are high and the project is well designed.

**4. PPPs could help improve the efficiency of public investment, thereby enhancing the creditworthiness of projects.** To this end, PPPs should be designed to allow a transfer of risks to parties that can directly affect the risks' likelihoods. For instance, the public sector could assume demand related risks while the private sector focuses on quality and cost overruns risks.<sup>4</sup> A successful implementation of PPPs would require strengthening the institutional framework (Box 1) in order to improve project selection, contract design, and debt monitoring capacities. In particular, special care should be taken to ensure that contingent liabilities are fully included in the fiscal framework. The selection of a Public-Private Partnership model should reflect the extent to which the public sector wishes to engage the private sector in the production of public infrastructure. While models with relatively large private responsibility could help reduce public indebtedness, they would often require special provisions to minimize social distortions.



<sup>3</sup> African Development Bank Group Working Paper, 2012: "Accessing Local Markets for Infrastructure: Lessons for Africa".

<sup>4</sup> Deloitte Research (2006). "Closing the Infrastructure Gap: The Role of Public-Private partnerships" reports that completing the construction of segments of the Denver E-470 toll road with a PPP approach saved 30 percent of the original cost estimate.

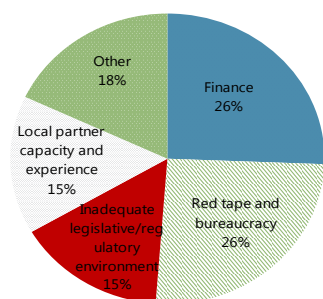
**5. Bank lending for infrastructure financing could be revamped with project restructuring.** Bank lending for infrastructure projects remains relatively scarce because infrastructure projects tend to be long-term and risky investments. To increase commercial banks' participation in infrastructure financing, projects could be unbundled<sup>5</sup> into successive sub-projects corresponding to different stages of maturity. In this setup, official development assistance could finance projects in their earlier and riskiest phases while short-term bank lending would serve mainly to finance maturing projects. At the regional level, subsequently re-bundling projects at comparable stages could further broaden risk diversification.

**6. De-risking infrastructure projects would help improve borrowing terms and open the door to new investors.** To this end, regional institutions could disseminate and encourage usage of credit guarantees and political risk guarantees offered by the Initiative for Risk Mitigation in Africa (IRMA) at the African Development Bank (AfDB). Credit guarantees insure against default induced by commercial or political events while political risk guarantees cover political risks, including risks related to breach of contract, confiscation, war and civil disturbance, and currency inconvertibility. Usage of guarantees would enhance risk mitigation and could help promote the participation of international pension funds that in some countries are prohibited to invest in African infrastructure projects considered too risky.

**Figure 2. CEMAC Countries: Bottlenecks to Private Participation in Africa's Infrastructure Projects**

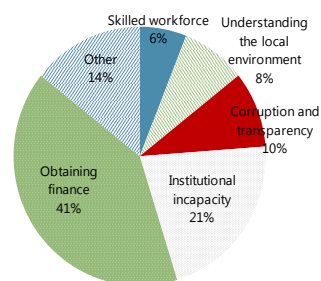
(2012 ICA Survey of Private Investors)

**Bottlenecks in Project Preparation**



74 percent of respondents to the 2012 ICA Survey of Private Investors listed non-financial constraints as the most important factor causing bottlenecks in project preparation.

**Greatest Challenges Facing Private Participants**



39 percent of respondents listed an institutional constraint as the single greatest challenge faced when participating in an African infrastructure project.

<sup>5</sup> Collier and Mayer (2014): "Unlocking Private Finance For African Infrastructure".

**7. CEMAC could deliver a more favorable environment for Africa’s infrastructure scaling up by ensuring a harmonized institutional framework based on best international practices.** Respondents to the 2012 ICA Survey of Private Investors viewed non-financial constraints as a major impediment to infrastructure projects in Africa. For 39 percent of respondents to the 2012 ICA Survey of Private Investors, institutional constraints were the greatest challenges faced when investing. When deciding to invest in an African infrastructure project, partner risk was given the greatest consideration, followed by the quality of the legal or regulatory environment. Country or political risk was ranked third, project risk or feasibility fifth, and finance came only sixth. Survey results suggest that providing investors with risk-mitigation tools and improving the institutional environment (Box 1) would open the door to new investors who so far have refrained from CEMAC’s infrastructure projects not because of unmet funding needs, but rather because of institutional barriers and risk aversion.

**Box 1. Recommendations for the Mitigation of Non-Financial Constraints to Infrastructure Financing**

- Establish credible PPP frameworks:
  - Design appropriate laws and regulations based on internationally accepted norms to implement PPPs, with clear specifications of rules governing allowable PPPs models, capital structure and project financing arrangements.
  - Ensure full disclosure of the bidding process and clear rules governing project cancelation; and put in place a competitive tender process to ensure sufficient competition.
  - Implement a transparent mechanism to allocate official development assistance and public finance support facilitating cost recovery for PPPs.
  - Establish an independent regulatory authority for tariffs and service quality.
  - Emphasize common standards for PPPs regulations within country contexts to facilitate greater cross-border private investments in infrastructure.
  - Define benchmarks for assessing contractual results and engage with end-users in monitoring service quality.
- **Improve capacity for project design and implementation and optimize project preparation** costs using bilateral donor support, development funds of multilateral development banks, and Project Preparation Facilities.
- **Unbundle production, transmission, and distribution** to enhance the efficiency of State Owned Enterprises (SOEs) and increase opportunities for private participation in markets dominated by SOEs.
- **Establish solid debt monitoring systems and improve debt management capacity** in local and national government agencies and public corporations to improve their creditworthiness.
- **Use suitable risk mitigating instruments against political risk.**



**8. The regional development Bank (BDEAC) should continue to strengthen its institutional capacities to play a greater role in the articulation of regional infrastructure projects.** The donor-supported institutional and technical assistance program of the BDEAC should strengthen institutional capacities. Stronger capacities would help bolster the role of the BDEAC as a central actor for regional development. In addition to providing direct financing, the BDEAC should also accompany CEMAC countries in the selection of projects to ensure that greater emphasis is put on the need to create synergies to develop the regional economy.

### C. International Experience

- **United States:** Historically, tax-exempt municipal bond markets have been the main source of funding for infrastructure projects in the United States. Recently, increasing concerns about rising public debt have motivated a shift toward a broader interest for PPPs which in the past were used almost exclusively in the utility, railroad and telecom sectors. This increasing interest in PPPs is reflected in a 2005 legislation amendment which made it possible for states to issue tax-exempt Private Activity Bonds (PAB) for privately developed and operated projects associated with highways and freight transfer facilities<sup>6</sup>.
- **Europe:** PPPs play a significant role in the European infrastructure market. According to the OECD's Pension Funds Investment in Infrastructure survey, the transport sector in Europe receives the largest share of infrastructure allocation<sup>6</sup>. The EIB has provided about EUR 30 billion in loans for PPPs since the late 1980s. The Europe 2020 Project Bond initiative of the EIB and the European Commission provide credit enhancement in the form of subordinated debt which helps to reduce credit risk in order to catalyze private financing from institutional investors. During its pilot phase (2007–13), the Europe 2020 Project Bond initiative was funded with EUR 230 million from EU budgetary resources from unused budget lines for existing programs.
- **South Korea:** As a consequence of tighter budget constraints after the East Asian crisis of 1997, South Korean enacted the Private Participation in Infrastructure Act which enhanced the risk-sharing mechanism associated with PPPs. This has contributed to a surge in private participation in infrastructure financing.
- **Latin America and Caribbean:** Until the late 1980s, infrastructure financing in Latin America was mainly funded by government debt. In the 1990s, the increasing debt burden led governments to seek for private financing as an alternative to public sector financing and international aid. In 1990–2004, 47 percent of infrastructure investment was done by the private sector, compared to 24 percent in East Asia and the Pacific, and 15 percent in Europe and Central Asia<sup>7</sup>.

<sup>6</sup> OECD—Pension Funds Investment in Infrastructure: A Survey (2011).

<sup>7</sup> World Bank: "Structured Finance in Latin America: Channeling Pension Funds to Housing, Infrastructure and Small Businesses" (2007).

# PUBLIC INVESTMENT SCALING-UP, GROWTH AND DEBT DYNAMICS<sup>1</sup>

## 1. In 2006, CEMAC governments embarked on a scaling up of public capital spending.

Public capital expenditure was relatively stable at around 5 percent of GDP in 2000–05 and surged to 7 percent of GDP in 2006, then increasing further in subsequent years, peaking up at 16–15 percent of GDP in 2012–13. Public capital spending was mainly financed with oil revenue which rose from an average of 11 percent of GDP in 2000–04 to 15 percent of GDP in 2005, reached 19 percent of GDP in 2011 and 2012, and stayed at around 17–16 percent of GDP in 2012–13. For the rest of the decade, the share of public capital spending in GDP is forecasted to decrease steadily, mirroring an expected fall in the ratio of oil revenue to GDP. This annex builds on the methodology suggested in Buffie, et al. (2012)<sup>2</sup> to study the dynamics for growth and public debt implied by public investment programs in the CEMAC.

### Box 1. Key Model Features

- The model has three production sectors: a non-traded goods sector, a non-oil traded goods sector, and a traded oil sector. Production in non-oil sectors uses public capital, private capital, and labor. Every period, the economy receives an exogenous oil endowment which is exported, with proceeds shared between the government, households, and foreign extracting firms.
- There are two types of households: savers and non savers. Savers may purchase government-issued bonds and may borrow with an exogenous risk premium in an international financial market, paying portfolio adjustment costs which limit their access to foreign borrowing. Non savers are hand-to-mouth households.
- Governments may borrow at an exogenous interest rate of 6 percent<sup>1</sup>. Governments finance public capital investment, debt services, and lump sum transfers to households with consumption taxes and oil revenues. Governments monitor the path of public debt using adjustments to the consumption tax rate and transfers.
- The capital formation process is subject to absorptive capacity constraints and government inefficiency. In the baseline, a public investment efficiency rate of 40 percent is assumed, implying that 1 million CFAF of public investment leads to 400,000 CFAF worth of public capital accumulation.<sup>2</sup>

<sup>1</sup> Gueye and Sy's (2010) estimates the average interest rate paid by sub-Saharan Africa, excluding Seychelles and South Africa to be 8.55 percent. 6 percent is hence a conservative value.

<sup>2</sup> Comparing investment flows to the physical measure variations of the public capital stock in Columbia and Mexico over the period 1981–95, Arestoff, F. and Hurlin, C. (2006) estimates that one peso of public investments created around 0.40 pesos of public capital. Pritchett, L. (1996) reports that in a typical developing country in earlier decades, less than 50 cents of capital were created for each public dollar invested.

<sup>1</sup> Prepared by Nathalie Pouokam

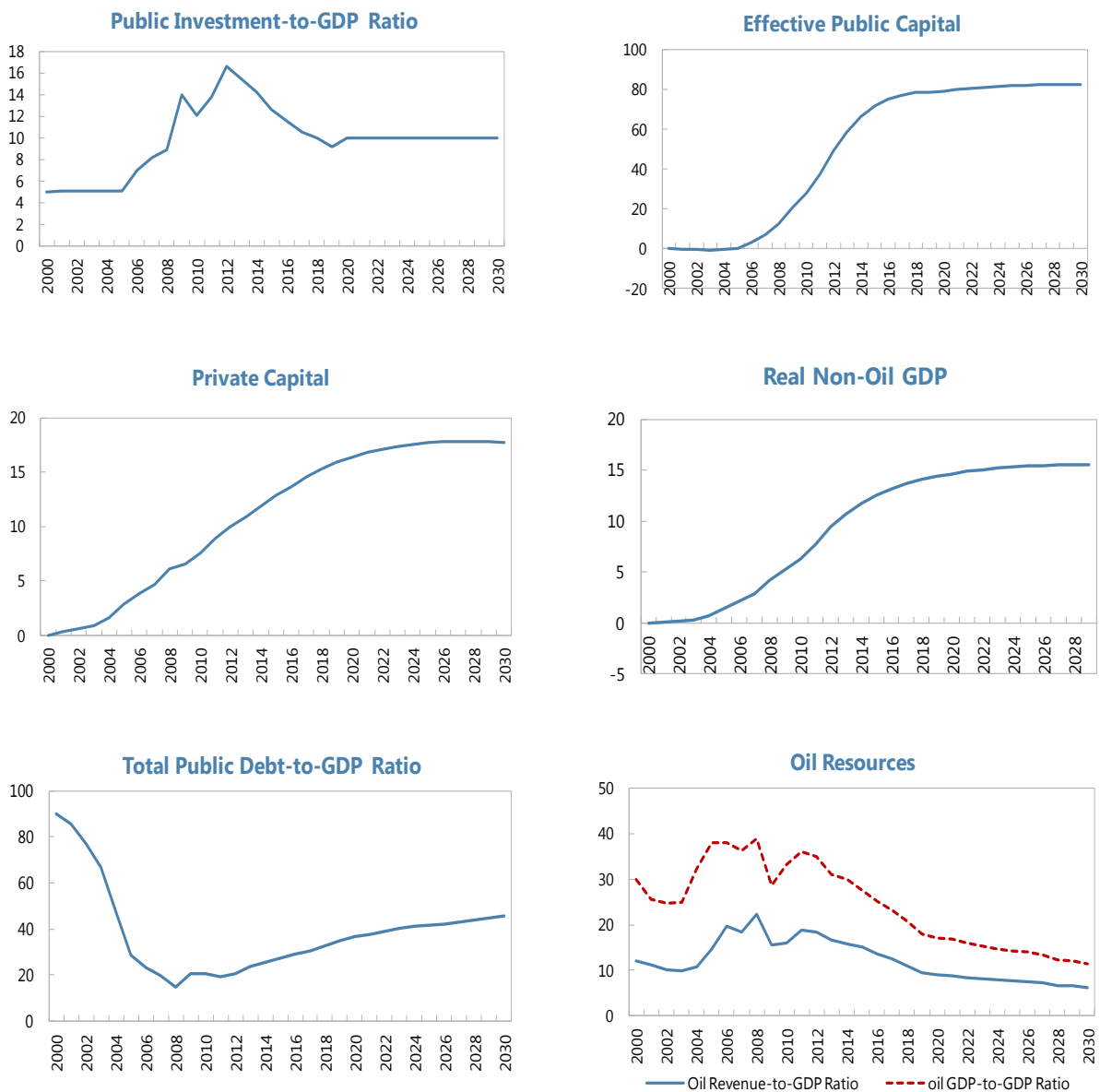
<sup>2</sup> Buffie et al. (2012): "Public Investment, Growth, and Debt Sustainability: Putting Together the Pieces", IMF Working Paper. The model was estimated with the assistance of W. Clark and M. Ghilardi (Research Department).

**2. Main findings are:**

- Given current forecasts for oil production, CEMAC's current public investment programs would lead to a public-debt-to GDP ratio of 46 percent in 2030 (compared to the current level of 22 percent). Beyond 2020 when the public investment scaling-up would be completed, public spending would still need to remain elevated in order to maintain the stock of public capital accumulated.
- Measures undertaken to improve the return of public capital (for instance by improving the collection of user charges on public infrastructure with better targeted subsidies) and the efficiency of public investment spending could significantly reduce public debt while enhancing non-resource GDP growth.
- Oil discoveries required to keep debt stable at around 30 percent of GDP beyond 2030 would need to be large enough to allow the oil revenue-to-GDP to rise by 4.5 percentage points above its baseline level, starting in 2015. A negative shock to oil revenue of the same magnitude would lead to an oil revenue-to-GDP ratio close to 60 percent in 2030.

**Figure 1. CEMAC Countries: Baseline Scenario**

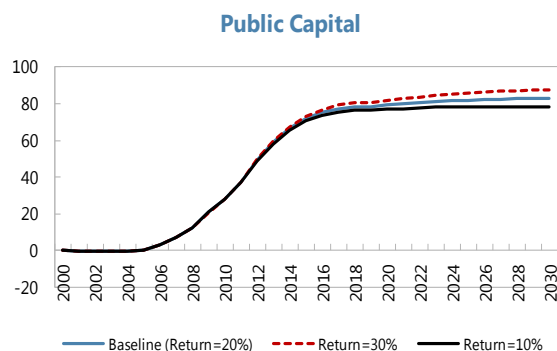
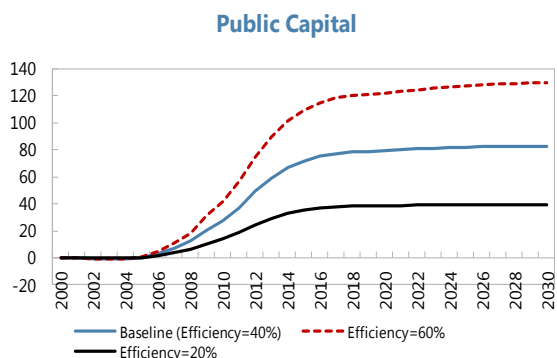
After peaking in 2013, the share of public investment in GDP gradually declines and then remains constant from 2020 onward. By 2020, the effective public capital stock has risen above its value in 2000 by 83 percent. Private capital and non-oil GDP grow quickly during the period of scaling up, but taper off afterward. Owing to falling oil revenue, public debt starts rising fast in 2015 to reach 46 percent of GDP in 2030.



**Figure 2. CEMAC Countries: Alternative Scenarios for Efficiency and Return to Public Investment**

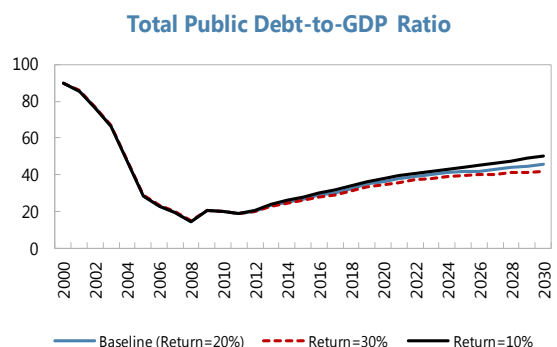
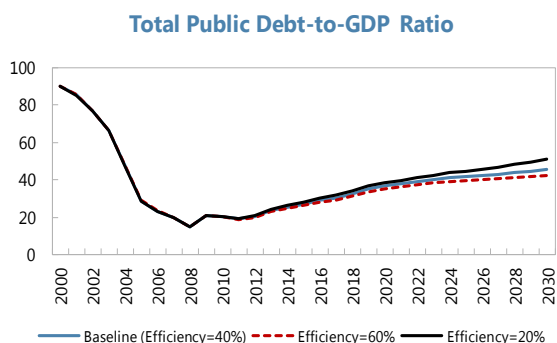
Everything else equal, with an efficiency of 60 percent, the public capital stock in 2030 is 130 percent above its 2000 value (Compared to 83 percent in the baseline scenario). When efficiency decreases to 20 percent, the public capital stock in 2030 is above its 2000 value by only 40 percent.

Everything else equal, with a return of 30 percent on public investment, the public capital stock in 2030 is 88 percent above its 2000 value (Compared to 83 percent in the baseline scenario). When efficiency decreases to 20 percent, the public capital stock in 2030 is above its 2000 value by only 78 percent.



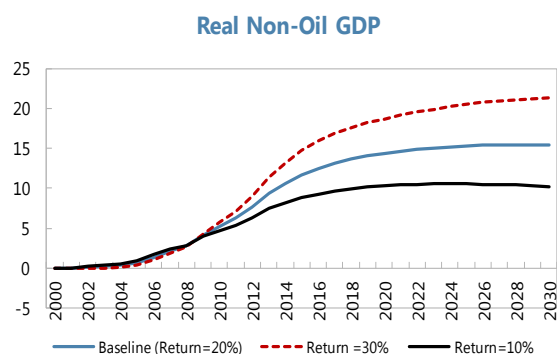
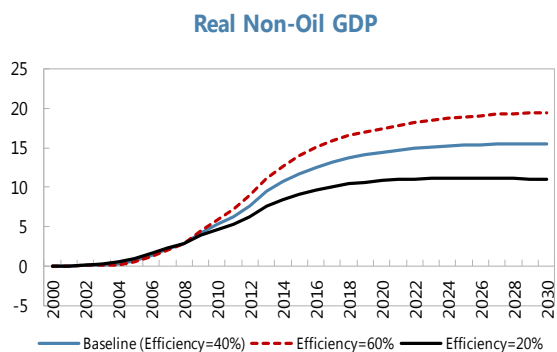
An efficiency of 60 percent (20 percent) leads to a public debt-to-GDP ratio in 2030 that is about 3 percent below (5 percent above) the baseline level.

A return of 30 percent (10 percent) leads to a public debt-to-GDP ratio in 2030 that is about 4 percent below (5 percent above) the baseline level.



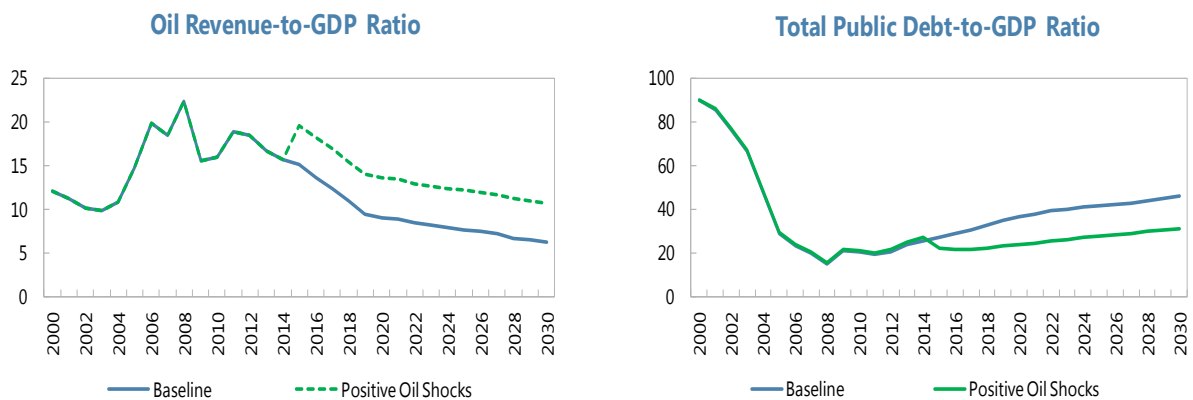
Real non-oil GDP increases with the efficiency level.

Real non-oil GDP increases with the return on public capital.

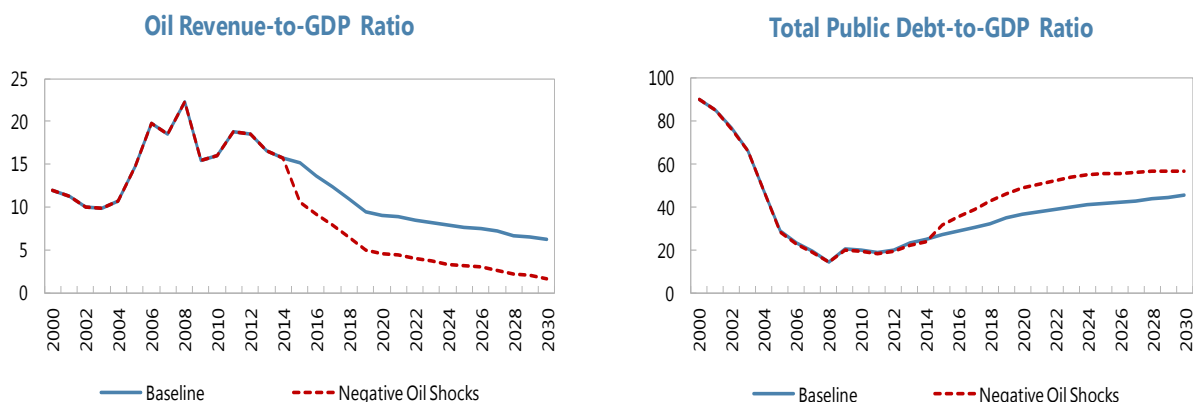


**Figure 3. CEMAC Countries: Alternative Scenario: Shocks to Oil Resources**

Everything else equal, for the public debt-to-GDP ratio to stabilize around 30 percent beyond 2030, the oil revenue-to-GDP ratio should be 4.5 percent above its baseline level, starting in 2015.



Symmetrically, if starting in 2015, the oil revenue-to-GDP falls below its baseline level by 4.5 percent, the public debt-to-GDP ratio would reach 57 percent of GDP in 2030.



## GROWTH AND COMPETITIVENESS IN CEMAC<sup>1</sup>

*While sub-Saharan frontier economies significantly improved their per capita growth since 1995, CEMAC performance improved only moderately. Structural factors (weak business climate and governance, infrastructure gaps, low total factor productivity and weak structural competitiveness) seem to be the main reasons behind this underperformance. Developing a new diversified economic model based on a dynamic private sector is key to ensure sustainable, strong, and inclusive growth.*

**1. Robust growth over the last two decades had a modest impact in CEMAC's economic development** (Figure 1). Oil discoveries and relatively steady growth in the non-oil sector have maintained real GDP growth at above 7 percent on average over the last 20 years. Real GDP per capita almost tripled over the same period. This performance, however, has been much more modest by excluding Equatorial Guinea, the CEMAC country where most oil discoveries took place during this period (Figure 1). In particular, while real GDP grew on average by about 4–5 percent since 1995, regional real GDP per capita –without Equatorial Guinea increased by less than 20 percent. This underperformance is even more evident when comparing CEMAC to a group of mainly non-resource rich SSA countries<sup>2</sup> with initial conditions similar which registered an increase of almost 70 percent in their per capita income since 1995.

**2. This annex tries to shed some light on the reasons behind CEMAC underperformance compared to a group of faster growing SSA economies.** First, it analyzes the role of external and internal factors using growth regressions and benchmarking exercise. It focuses then on structural issues, such as business climate, governance, and competitiveness. Finally, it concludes on the key challenges ahead to develop a new diversified economic model based on a dynamic private sector to ensure sustainable, strong, and inclusive growth.

### A. Role of External and Domestic factors

**3. External factors played a positive role in closing growth differentials between CEMAC and benchmark countries.** Empirical results (Table 1) show that an increase in trade openness by a percentage point of GDP in the CEMAC compared to benchmark countries generated about 0.1 percentage point more per capita growth in the region than in the benchmark. This is undoubtedly linked to increasing trade flows towards new emerging partners. For instance, an increase in export to China was associated with about 0.5 percentage point higher per capita growth in the CEMAC than in the benchmark countries (Figure 2). Average shocks synchronization with the rest of the world has been, however, relatively lower in the CEMAC than in the benchmarks countries (Figure 2). Finally, CEMAC countries have received, on average, more FDI than benchmarks ones and growth regressions corroborate that these inflows generated about 0.2 percentage point more per capita growth in the region.

<sup>1</sup> Prepared by Jose Gijon, Aleksandra Zdzienicka, and Zaki Dernaoui (AFR).

<sup>2</sup> A group of faster growing economies (thereafter benchmark), includes Botswana, Ghana, Kenya, Mozambique, Nigeria, Rwanda, Senegal, Tanzania, Uganda, and Zambia.

Figure 1. CEMAC Countries: Growth Performance

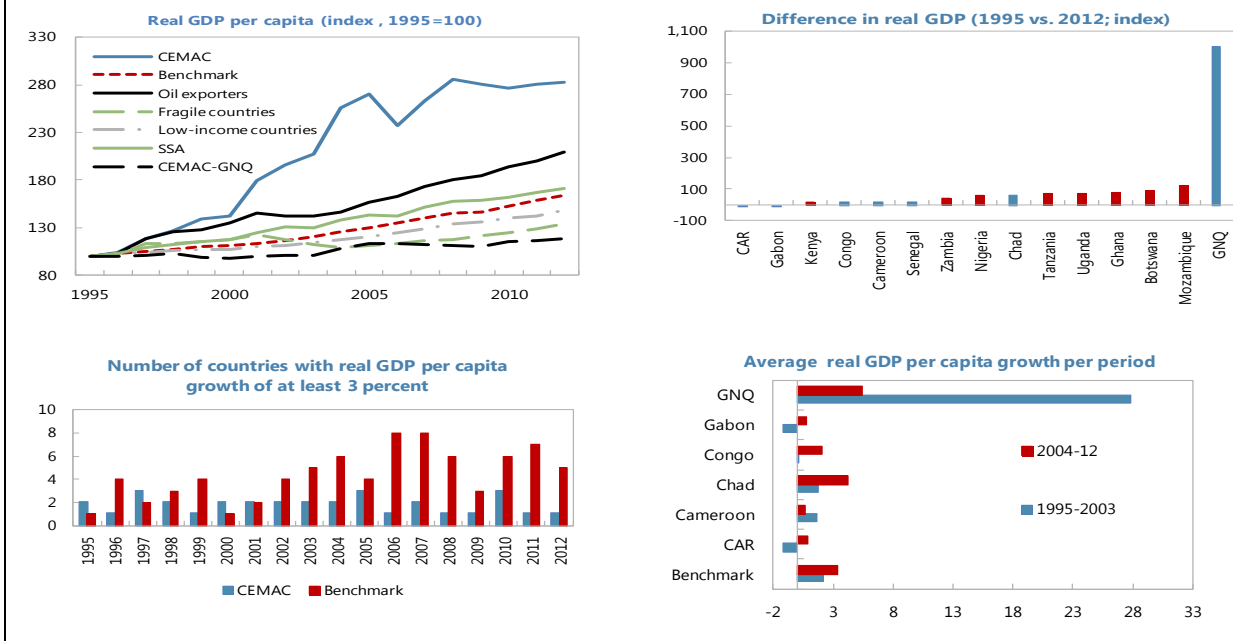
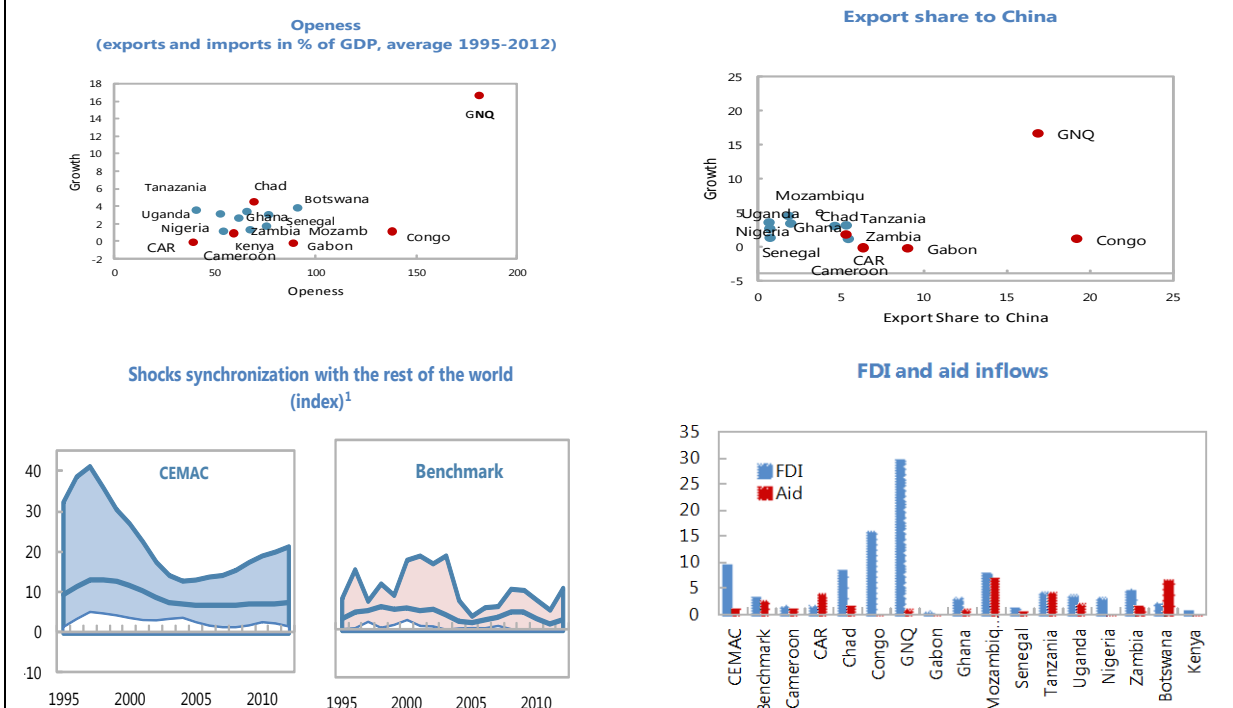


Figure 2. CEMAC Countries: External Environment



<sup>1</sup> Shaded area corresponds to maximum and minimum values for CEMAC or benchmark countries, lines to regional average.



**Table 1. CEMAC Countries: Growth Regression**

	External	Macroeconomic policy	Structural
Openness (Exports and Imports in % of GDP)	0.087** (2.41)		
Exports to China (% of total exports)	43.696 (1.54)		
FDI (% of GDP)	0.147** (2.68)		
Inflation (annual change in CPI)		-0.126 (-0.34)	
Current account (% of GDP)		-0.109*** (-7.04)	
External debt (% of GDP)		-0.039 (-1.82)	
Public investment (% of GDP)		-0.816*** (-6.29)	
Services (% of GDP)			-0.332 (-1.81)
Industry (% of GDP)			-1.026*** (-13.78)
Credit to private sector (% of GDP)			0.358 (0.47)
N	94	93	91
R <sup>2</sup>	0.58	0.64	0.62
Note: Estimations for 6 CEMAC countries over the period 1995–2012; Variables are taken in relative terms compared to the benchmark; Country and time fixed effects included but not reported; t-statistics basic on clustered standard errors reported in parenthesis. ***, **, * denote significance at 1%, 5% and 10%, respectively.			

**4. Macroeconomic policies have generated less growth in the CEMAC than in the benchmark countries.** Although public investment was relatively higher than in the benchmark countries (Figure 3), it generated about 0.9 percentage point less per capita growth in the CEMAC<sup>3</sup> Conversely, an increase in external indebtedness has not been significantly linked to higher growth whereas the current account improvement has generated 0.1 percentage point lower growth in the CEMAC than non-resource rich countries. CEMAC region has not taken advantage from a more stable macroeconomic context and lower and less volatile inflation (Figure 3) and has not generated a significantly higher growth in the region compared to the benchmark.

<sup>3</sup> The results show that the effect of public investment is significantly reduced when TFP is controlled for. TFP is estimated using a Cobb-Douglas production function with constant returns to scale and perfect competition.

## 5. **Structural factors seem to be the main reason behind CEMAC underperformance.**

Structural factors seem to explain growth underperformance in CEMAC countries. In particular, as financial development and access to finance have been limited (Figure 4), they have not significantly affected growth performance in the region. Also, total factor productivity has been considerably lower—or even negative—in the CEMAC region than in the benchmark when excluding Equatorial Guinea and, especially, accounting for oil discoveries in the late 1990s–early 2000’s. It can reflect a number of factors, such as limited structural transformation and innovation, weak governance and business environment in the CEMAC (Figure 5). It also explains why an increase in structural transformation (measured by a share of industry and service in GDP) has generated a percentage point lower per capita growth in the region than in the benchmark.

## B. **Role of Business climate, Governance, and Competitiveness**

6. **Weak Business climate indicators<sup>4</sup> for CEMAC have not improved.** CEMAC has made very few advances in the World Bank’s Doing Business Indicators (WBDBI) since 2007, the average ranking has worsened in four out of six indicators and most countries are at the bottom of overall ranking (Gabon 163<sup>th</sup>, Equatorial Guinea 166<sup>th</sup>, Cameroon 168<sup>th</sup>, Congo 185<sup>th</sup>, Central African Republic 188<sup>th</sup> and Chad 189<sup>th</sup> out of 189 countries). Moreover, CEMAC’s scores have not improved over time, but they have fallen from an already weak position (Figure 5). CEMAC’s average percentile rank was respectively 32 in 2007 and 36 in 2014, as opposed to 47 and 47 in the benchmark. Despite some marginal improvements in some areas such as registering property and trading across borders, there are serious deteriorations in others, in particular in protecting investors or registering, making CEMAC the region with the most challenging business climate in the World.

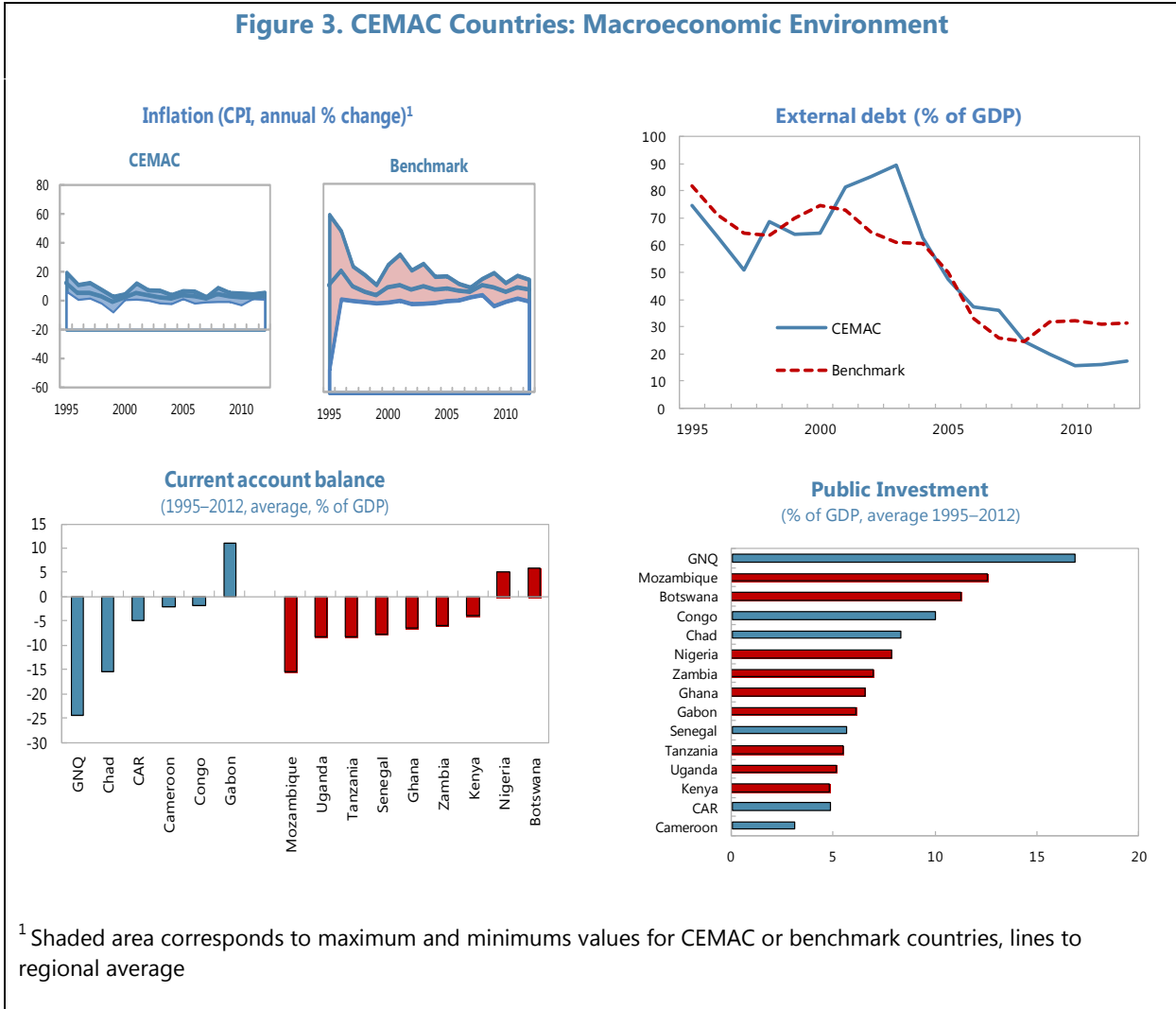
7. **Despite policy initiatives launched by regional and country authorities, progress in the improvement of governance also seems to be disappointing.** The World Bank’s Worldwide Governance (WBG) Indicators show a deterioration or lack of progress in four of the six governance indicators in the CEMAC, compared to the benchmark and different groups of SSA countries between 1996 and 2002 (Figure 5). The governance indicators are much lower in the CEMAC, especially regarding regulatory quality, control of corruption or voice and accountability. The CEMAC position (in terms of average percentiles of the WBG Indicators) improved only slightly from 28 in 1996 to 29 in 2012 while the benchmark countries progressed from 41 to 44.

8. **A limited progress in business climate and governance reforms and lower TFP productivity had also impacted CEMAC overall competitiveness.** The 2013–14 World’s Economy Forum Global Competitiveness Index only ranks three CEMAC countries: Cameroon, Chad and Gabon (Box 1). Cameroon and Gabon are ranked as relatively more advanced and/or

<sup>4</sup> These indicators should be interpreted with caution due to a limited number of respondents, a limited geographical coverage, and standardized assumptions on business constraints and information availability.

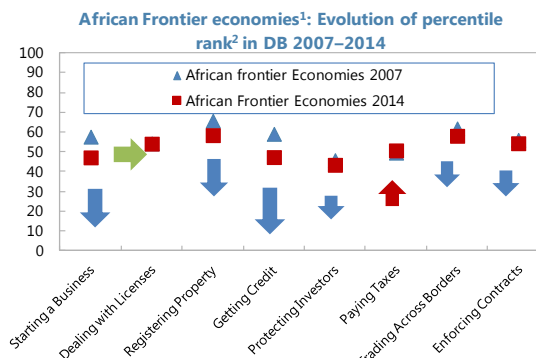
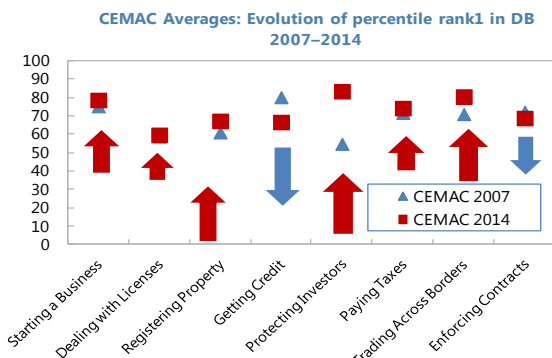
diversified economies in the region and Chad—as a less advanced economy. The ranking of the three countries points to serious competitiveness issues. In particular, Cameroon ranks 112 of 148, Gabon 115, and Chad 148 positions. Similarly, the evolution of (non-oil) exports of the CEMAC compared to the benchmark countries shows a continuous deterioration of regional competitiveness (Figure 6).<sup>5</sup>

**Figure 3. CEMAC Countries: Macroeconomic Environment**



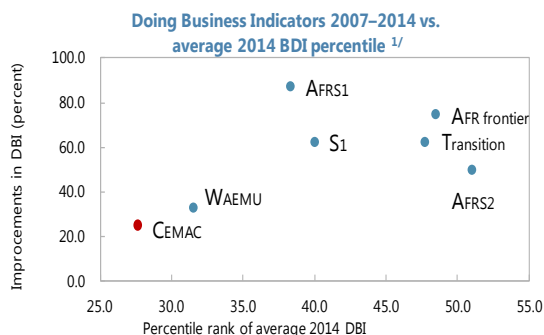
<sup>5</sup> Price competitiveness does not seem to have been an important issue. First, since the 1994 devaluation of the CFA franc, the real effective exchange rate (REER) has appreciated moderately and remained broadly in line with the region’s economic fundamentals. Second, some of the benchmark economies have actually recorded larger REER appreciations (Figure 6)

**Figure 4. CEMAC Countries: Business Institutional Environment**

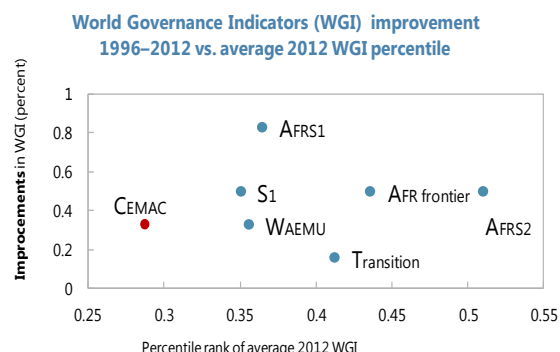


<sup>1</sup> The lower percentile rank the better the country performs.

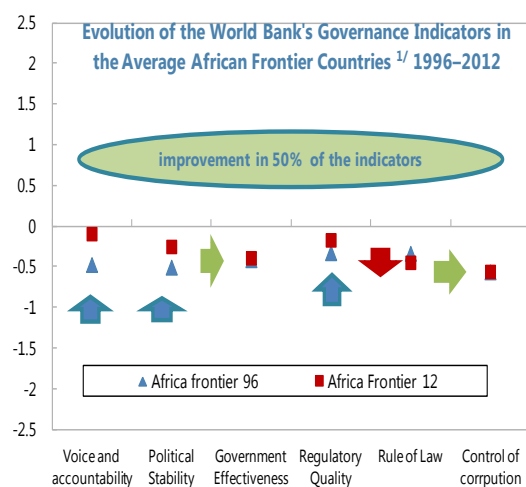
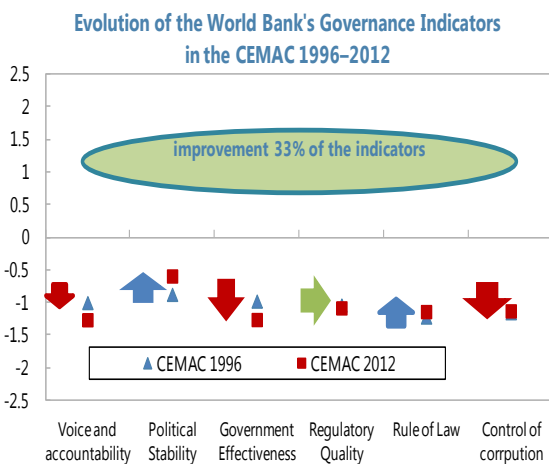
1: Kenya, Ghana, Mauritius, Mozambique, Nigeria, Senegal, Tanzania, Uganda, Zambia.  
2: The lower percentile rank the better the country performs.



<sup>1/</sup> A lower rank indicates a lower average percentile in WBDI. Sources: WBDBI database and staff estimates.



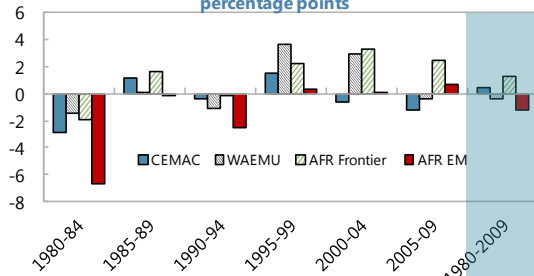
<sup>1/</sup> A lower rank indicates a lower average percentile in WGI. Sources: WBGI database and staff estimates.



Sources: World Bank Doing Business Indicators database, World Bank Global Governance Indicators database, IMF staff estimates.

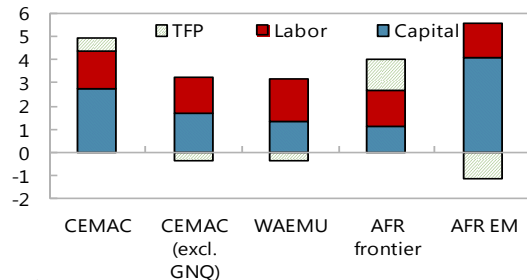
**Figure 5. CEMAC Countries: Productivity and Structural Competitiveness**

**Average Productivity in CEMAC, WAEMU <sup>1/</sup>, AFR Frontier <sup>2/</sup>, AFR Emerging Markets <sup>3/</sup>, 1980–2009 in percentage points**



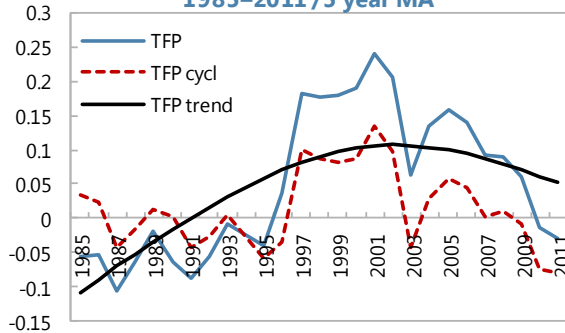
<sup>1/</sup>WAEMU: Benin Burkina Faso, Guinea Bissau, Mali, Niger, Senegal, Togo.  
<sup>2/</sup>AFR Frontier Ghana, Kenya, Mauritius, Mozambique, Nigeria, Senegal, Tanzania, Uganda, Zambia.  
<sup>3/</sup>AFR EM: Botswana, Cape Verde, Namibia, Seychelles and South Africa

**Growth decomposition for CEMAC, WAEMU1/, AFR frontier 2/, and AFR EM 3/, 1980–2009**

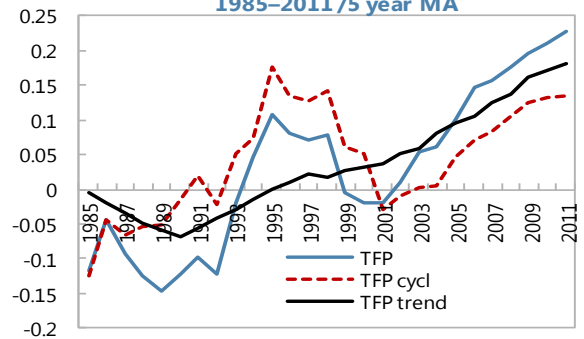


<sup>1/</sup>WAEMU: Benin Burkina Faso, Guinea Bissau, Mali, Niger, Senegal, Togo.  
<sup>2/</sup>AFR Frontier Ghana, Kenya, Mauritius, Mozambique, Nigeria, Senegal, Tanzania, Uganda, Zambia.  
<sup>3/</sup>AFR EM: Botswana, Cape Verde, Namibia, Seychelles and South Africa

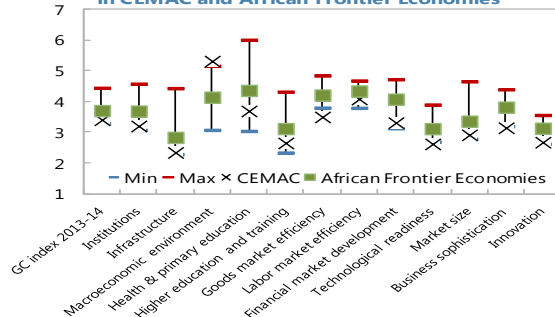
**CEMAC: TFP and TFP components, 1985–2011 / 5 year MA**



**AFR Frontier: TFP and TFP components, 1985–2011 / 5 year MA**

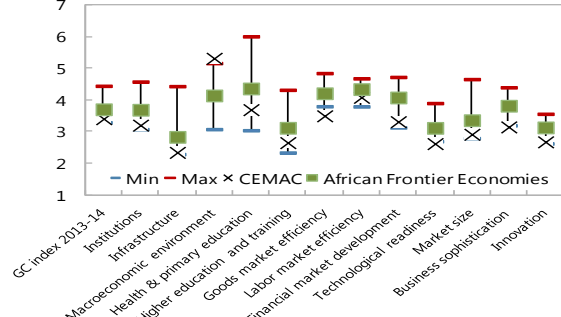


**2013–14 Scores in the WEF's GCI and pillars in CEMAC and African Frontier Economies<sup>1</sup>**



<sup>1</sup> Kenya, Ghana, Mauritius, Mozambique, Nigeria, Senegal, Tanzania, Uganda, Zambia.

**2013–14 Scores in the WEF's GCI and pillars in CEMAC and African Frontier Economies<sup>1</sup>**



<sup>1</sup> Kenya, Ghana, Mauritius, Mozambique, Nigeria, Senegal, Tanzania, Uganda, Zambia.

Sources: PWT, Barro and Lee (2012), WEF (2014), IMF Staff computation

### Box 1. The World's Economic Forum Global Competitiveness Index (GCI)

The GCI assesses competitiveness based on twelve indicators grouped in three main subindexes: (i) *basic requirements* that includes institutions, infrastructures, macroeconomic environment, and health and primary education, (ii) *efficiency enhancers* that includes higher education and training, goods market efficiency, labor market efficiency, financial market development, technological readiness, and market size, and (iii) *innovation and sophistication factors* based on business sophistication and innovation.

Countries are grouped into five categories according to their level of economic development (Table1):

**Table 1. WEF: Subindex weights and level of economic development**

	Stage 1	Transition 1 to 2	Stage 2	Transition 2 to 3	Stage 3
GDP per capita (US\$)*	<2000	2000-2999	3000-8999	9000-17000	>17000
Weight for basic requirements	60%	40-60%	40%	20-40%	20%
Weight for efficient enhancers	35%	35-50%	50%	50%	50%
Weight for innovation and sophistication	5%	5-10%	10%	10-30%	30%

\*For economies with a high dependency on mineral resources, GDP per capita is not the sole criterion for the determination of the stage of development. Source: WEF (2014)

The GCI currently considers three CEMAC countries: Cameroon, Gabon and Chad (Table 2). Other CEMAC members would be mostly likely included in stage 1 group (Central African Republic) or a transition stage 1 to 2 group as other middle income oil exporters. According to the WEF classification, it also means that *basic requirements* account at least for 50 percent of the assessment of CEMAC's overall competitiveness.

**Table 2. WEF: AFR countries level of economic development**

WEF stages of economic development	AFR countries
Stage 1 (factor driver)	Benin, Burkina Faso, Burundi, <b>Cameroon, Chad</b> , Cote d'Ivoire, Ethiopia, Gambia, <b>Ghana</b> , Guinea, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, <b>Mozambique, Nigeria, Rwanda, Senegal</b> , Sierra Leone, <b>Tanzania, Uganda Zambia</b> , Zimbabwe.
Transition from 1 to 2 and stage 2	Angola, <b>Botswana, Gabon</b> , Cape Verde, Mauritius, Namibia, South Africa, Swaziland.

Source: WEF (2014)

To reach higher level of economic development CEMAC countries should increase productivity while ensuring sufficient physical factor accumulation. To do so, *basic requirements* such as the level of infrastructure or the quality of institutions must be able to support these gains in productivity. This would require structural reforms in areas such as the efficiency of tax administration, investment, education, and fair competition in domestic markets.

## C. Policy actions and Reforms

**9. CEMAC faces significant challenges in business environment, governance and structural competitiveness.** These difficulties seriously constrain private investment growth and overall investment efficiency, limit structural transformation and economic diversification, and undermine growth performance of CEMAC economies. They also prevent the CEMAC region to take advantage from a more stable macroeconomic environment and favorable global conditions.

**10. Policy actions should focus on improving governance and institutional quality, physical infrastructure, and education, but significant efforts in other areas are necessary.**

Priority policy actions should focus on improving governance and institutional quality, physical infrastructure, and education (the areas identified by the WEF as basic requirements). Regional and national authorities should also focus on measures to improve the efficiency of domestic good markets and support of financial sector development. The WBDBI and Governance Indicators show that it is extremely challenging to open and operate a business in the CEMAC. Hence, an ambitious institutional reform targeting the simplification of administrative procedures (e.g. registering business, protecting investors or paying taxes), improving the effectiveness of public administration and fighting corruption should be envisaged. Without a significant institutional reform, the effects of the new public infrastructure in CEMAC economies will be limited.

**11. Export diversification policy with a strong institutional framework for export promotion and greater regional integration are important steps toward sustainable and strong growth.**

Countries with a strong non-oil tradable sector and successful export diversification strategies usually relied on a strong institutional framework for export promotion.<sup>6</sup> A similar framework should be developed in the CEMAC. In particular, the Chilean model that hinges on a strong collaboration with the private sector would help to create a very competitive agribusiness export sector. Finally, improvements in productivity in the tradable sector and a successful diversification strategy should be underpinned by greater trade openness through greater integration within the CEMAC and other regional integration initiatives.

---

<sup>6</sup> Gijon (2010)

## References

Berg, A., J. D. Ostry, J. Zettelmeyer, (2008) "What Makes Growth Sustained?", IMF Working papers 8/59.

Gijon, J., (2010), "Will the New Foreign Direct Investment Regime Promote Export Diversification in Algeria? A perspective from Chile's and Malaysia's Successes", the Maghreb Center Journal 1/10 ([www.themaghrebcenter.org](http://www.themaghrebcenter.org)).

IMF, (2008) IMF Regional Economic Outlook, October 2008.

IMF, (2013) "Sub-Saharan Africa. Keeping the Pace." IMF Regional Economic Outlook, October 2013.

IMF, (2014) "WAEMU: Staff Report on Common Policies for Member Countries." IMF Country Report 14/84.

IMF (2014 a) "Sustaining long-run growth and macroeconomic stability in low-income countries –the role of structural transformation and diversification"

WEF (2014), "The Global Competitiveness Report. 2013–014"( <http://http://www.weforum.org/issues/global-competitiveness>)



# FINANCIAL INCLUSION IN THE CEMAC<sup>1</sup>

## A. Introduction

**1. Financial inclusion matters for economic and social development.** In recent years, and especially since the 2009 financial crisis, financial inclusion—typically defined as the proportion of individuals and firms that use financial services—has become a subject of considerable interest among policy makers, researchers, and other stakeholders (2014 Global Financial Development report)<sup>2</sup> There has been a growing realization that only about half of the world population has access to financial services, and that access is unequally spread across regions, countries, income levels and gender. More importantly, it has been increasingly recognized that financial inclusion affects economic and social development. Access to financial services can play a critical role in reducing poverty, inequality, and supporting inclusive development. Worldwide evidence indicates that the poor benefit from having access to basic payments, savings, and insurance services. For firms, particularly for SMEs, access to finance is crucial for investing and growing.

**2. But boosting financial inclusion is neither trivial nor innocuous.** On the one hand, creating new bank accounts does not always translate into regular use and on the other hand, boosting financial inclusion should not mean lending to all indiscriminately. The promotion of credit without sufficient regard for lender protection and financial stability is likely to bring problems, especially if credit starts growing rapidly. Dozens of microcredit experiments paint a mixed picture about the developmental benefits of microfinance projects targeted at particular groups in the population. It is important not to force financial service upon groups or firms that have no need or usage for them. However, there is a large scope for improvement when markets are malfunctioning and preventing people to accessing financial services.

**3. The objective of this analytical note is to have a closer look at financial inclusion in the CEMAC region** by benchmarking financial inclusion in CEMAC countries with peer African countries and looking at interregional comparisons for the main access indicators, as well as identifying the link between financial inclusion and social indicators. The remainder of the note is organized as follows. Section B will present a benchmarking exercise and discuss financial inclusion in the CEMAC through cross country comparisons. Section C examines the microfinance sector and innovative finance and section D discusses the link between financial inclusion and human development. Section E will conclude by presenting policy recommendations.

<sup>1</sup> Prepared by Adrian Alter and Boriana Yontcheva.

<sup>2</sup> In international forums, such as the Group of Twenty (G-20), financial inclusion has moved up the reform agenda. At the country level, about two-thirds of regulatory and supervisory agencies are now charged with enhancing financial inclusion. In recent years, some 50 countries have set formal targets and goals for financial inclusion.

## B. Financial Development and Inclusion in the CEMAC: Benchmarking and Cross Country Comparisons

*Access to financial services varies across CEMAC countries but still lags behind the Sub-Saharan Africa average, peer countries and the benchmark level expected when considering the countries' structural characteristics. Furthermore, in terms of financial access for the poor, this region is one of the least inclusive. In some countries the development of mobile banking outperformed regional trends and it could create good opportunities to alleviate poverty and improve access to credit. Retail and SME banking is very limited. In some countries the microfinance and informal sectors help to meet the saving and borrowing needs.*

### Methodology

**4. The objective of benchmarking is to compare financial sectors over time and relative to other countries while controlling for the level of economic development and other structural, country-specific factors.** By taking into account the most important non-policy factors affecting financial sector development while excluding all policy-driven factors, the statistical benchmark determines the level at which a country's financial system would be expected to perform in a policy-neutral environment. Deviations with respect to the benchmark can therefore be attributed, at least in part, to the quality and possible shortcomings of the country's policies. For each country, the World Bank's Finstat tool allows to estimate a structural benchmark based on the country's economic and structural characteristics.<sup>3</sup> Therefore, given the structural characteristic of the country, regressions provide an expected median level of financial development that the country could achieve. The analysis is carried out using data from 2000 onwards, where available.

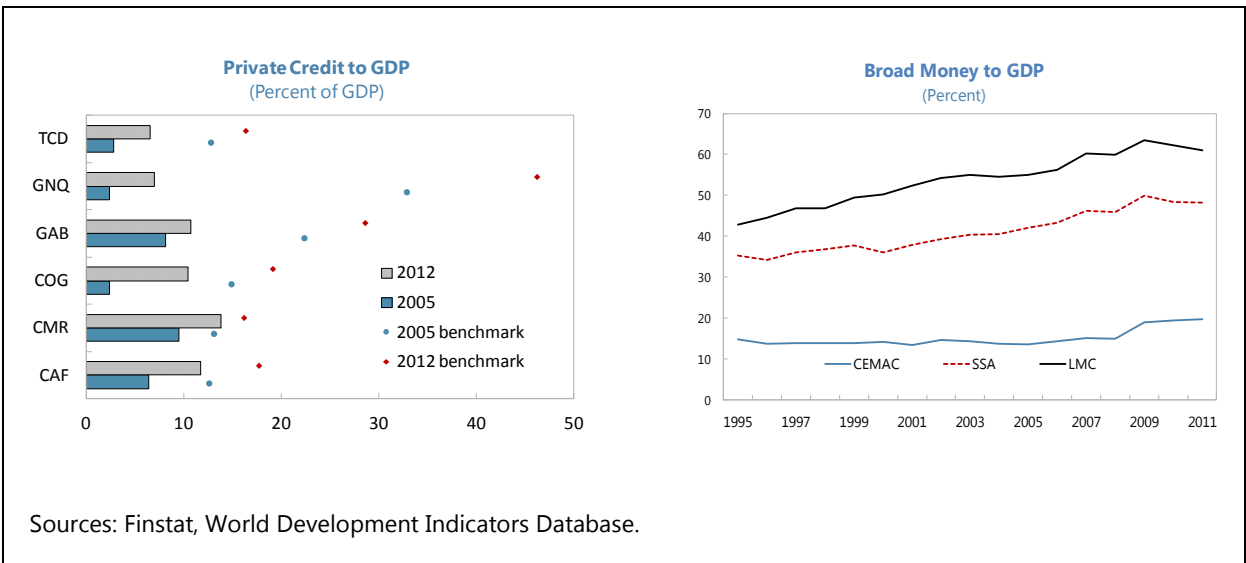
**5. Data availability permitting, financial sector indicators for the CEMAC countries are compared with those from peer countries.** Relevant peers are selected for each CEMAC country and include WAEMU countries and in particular Senegal, Benin, and Togo, but also Rwanda, Tanzania as well as with the average for sub-Saharan Africa (SSA), excluding South Africa, and the average of the lower middle income countries group (LMC) and lower income countries group (LIC). Rwanda is an interesting example of a country taking a policy decision leading to a breakthrough in access to finance (Finscope Rwanda, 2012). Kenya and Tanzania are examples of SSA economies with a rapidly developing financial sector and rapid reduction in financial exclusion. Countries from the West African Economic Monetary Union (WAEMU) provide examples from a similar institutional setting. The SSA average (excluding South Africa) reflects the development of the rest of the continent while the LMC and LIC averages provide comparisons with countries with a similar development level as the benchmarked CEMAC country.

---

<sup>3</sup> The structural benchmarks are calculated based on Beck et al. (2006) and FinStats from the World Bank. Using a large dataset of countries, the financial indicator is 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.

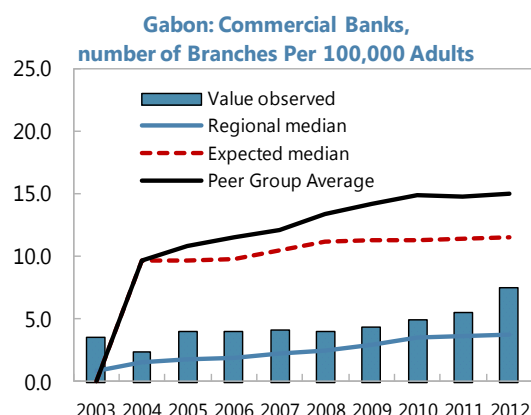
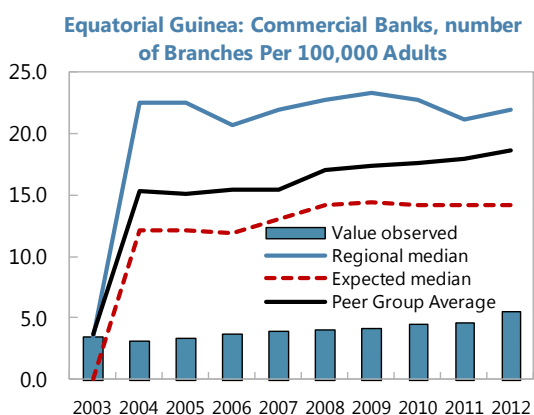
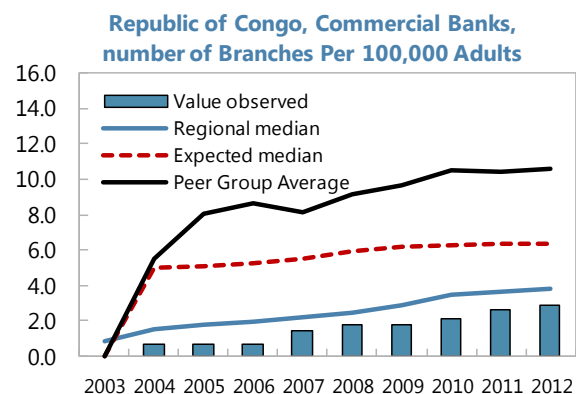
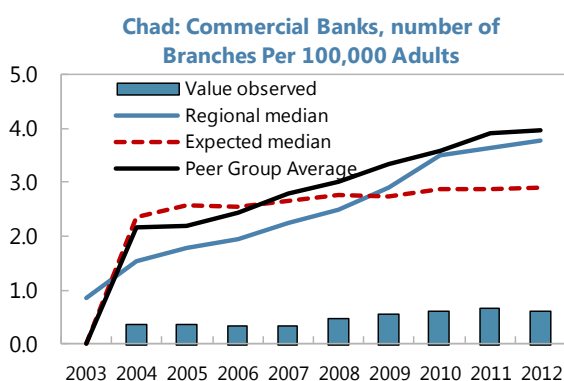
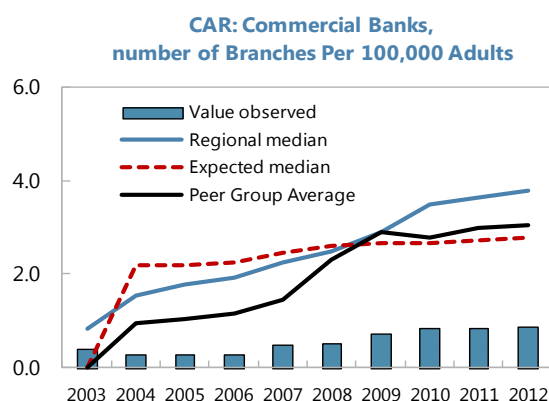
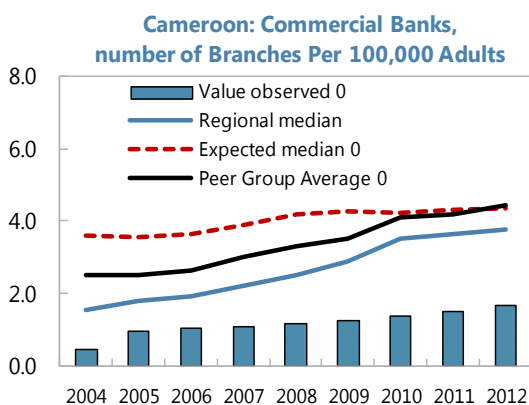
## Depth and Inclusiveness

**6. The banking system has grown in recent years but remains comparatively shallow.** In most CEMAC countries, private sector credit has grown rapidly since the mid-2000s. Nevertheless, all CEMAC countries underperform compared to their benchmarks for private sector credit and bank deposits to GDP, and the banking sector remains much shallower than in other peer countries.



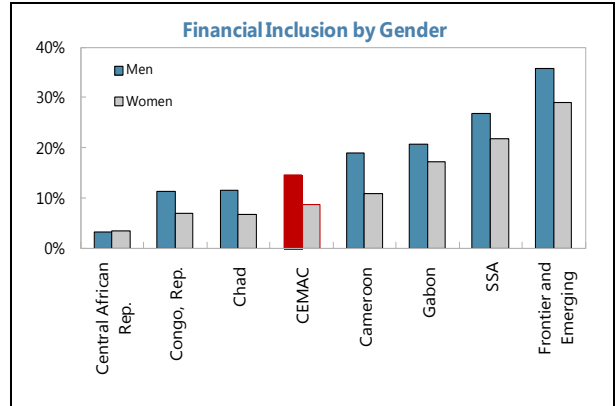
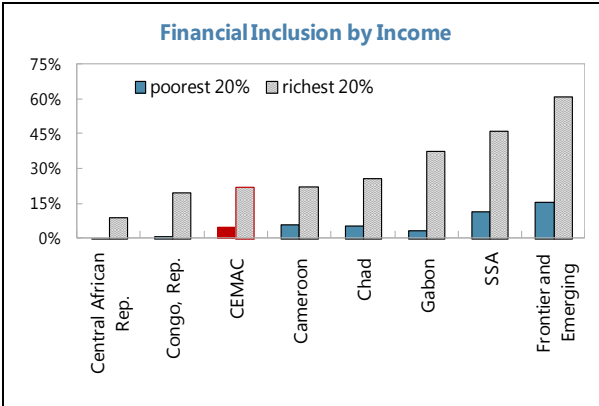
**7. Access to financial services in the CEMAC region is limited, and is falling behind other regions in Sub-Saharan Africa and other peers.** As can be seen from figure 1 below, all countries in the CEMAC region underperform their expected benchmark when it comes to financial inclusiveness as measured by the number of branches per capita. With the exception of Gabon, all countries are below the SSA median and also well below their peer group averages. In addition, the tendency in peer countries has been to catch up with the expected median while indicators in CEMAC countries have a slower evolution. There is scope for policy action to improve financial access and inclusion and the experience of some peer countries with rapid improvement in financial inclusion could help identify potential policy actions.

**Figure 1. CEMAC Countries: Benchmarking Access to Financial Services**



**8. Access to formal savings and loans is limited, especially for the poor population.**

Financial inclusion can also be approached from the perspective of the contrast between bankable “rich” and “poor”<sup>4</sup> In the CEMAC area 23 percent of the “rich” population has a formal account compared with only 4 percent among the “poor”.

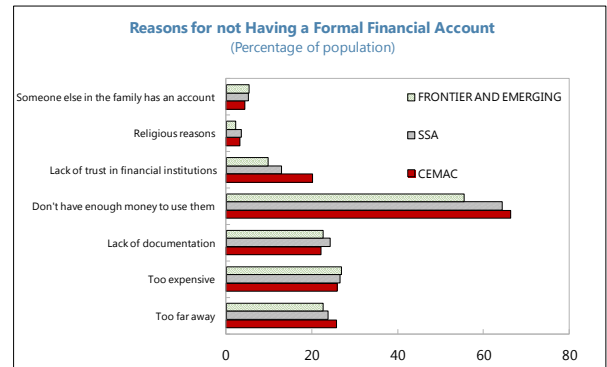


**9. Financial inclusion indicators also reveal stronger than average gender inequality compared to other SSA countries.**

Women in the CEMAC region have a lower access to financial services than men compared to their peers in SSA. Only 6.8 percent of women have a formal financial account compared to 11.3 percent of the male population. The ratio of men to women with formal accounts is therefore around 1.66 which is much higher than in Sub-Saharan Africa frontier and emerging economies where this ratio is only 1.22.<sup>5</sup>

**10. The share of adults with formal savings is on average around 7.5 percent in the CEMAC region.**

Formal savings in Central African Republic are at the lowest level while Cameroon ranks highest. The most important constraint cited by adults for not having a formal account is lack of money, possibly reflecting a lack of demand. However, costs of service and distance to the closest banking branch are also commonly cited factors. Banks services (e.g. opening and maintenance fees) in the CEMAC are costlier compared with other banks in the region.

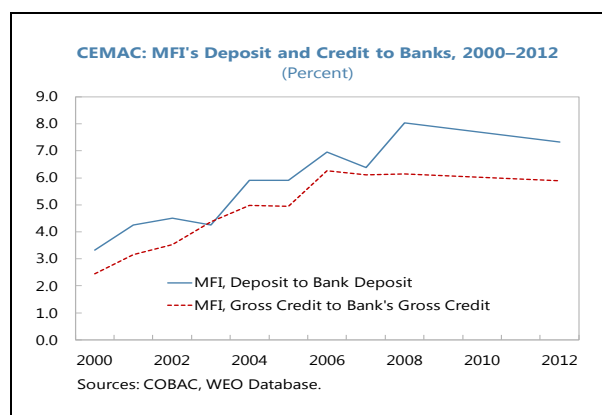
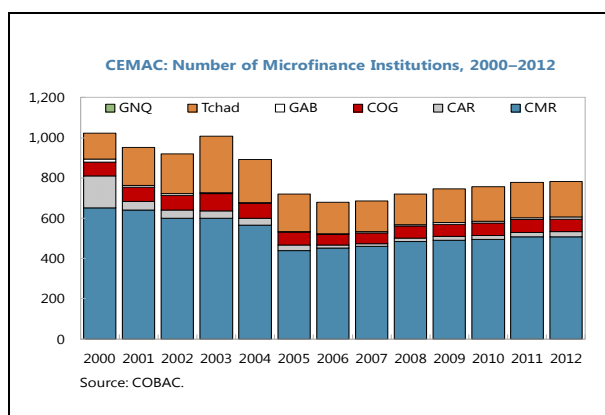


<sup>4</sup> Here we refer to the “bankable” population as the opposite of the “unbankable” population, defined in the Demircuc-Kunt and Klapper (2012a, 2012b). The former represents the share of the adult population with access to a formal financial account. The “rich” and the “poor” are the top 20% quintile and bottom 20% quintile, respectively, of the adult population ranked by income.

<sup>5</sup> The group of SSA frontier and emerging economies refers to following countries: Ghana, Kenya, Mauritius, Nigeria, Senegal, South Africa, Tanzania, Uganda, and Zambia. This group was constrained by data availability.

## C. Microfinance and Mobile Banking Services

**11. Micro Finance Institutions (MFIs) help reach the unbanked population.** Saving and lending behaviors of households and SMEs reflect the importance of informal and micro finance institutions. While less than 8 percent of the population has access to formal accounts, more than 35 percent of the adults in CEMAC have saved money with formal and informal institutions. Microfinance institutions are particularly prevalent in Cameroon and Chad where they help boost financial inclusiveness. As can be seen from the charts below, while the MFIs still represent a small share of the banking sector, the sector is rising rapidly – therefore presenting some supervision challenges. Similarly, the vast majority of loans are obtained through family and friends followed by private lenders. Less than three percent of the population has received a loan from a bank in the past 12 months underscoring the marginal dimension of retail banking.



**12. Mobile banking is growing in the CEMAC region-even though it remains much less developed than in other SSA countries - and it could help promote an alternative to traditional forms of financial services.** On average, almost 30 percent of the adult population has used mobile phone services to make financial transactions: to pay bills, to transfer or borrow money. Among the best performers, Gabon ranks second, with almost 50 percent of the population while Republic of Congo is in the fourth place in SSA according to the Global Findex database.

## D. Financial access and inequality

**13. Lack of financial access hampers poverty reduction and promotes wealth inequality.** Financial access is positively correlated with per capita GDP but also Human Development Indicators in SSA. In addition, access to loans and insurance creates heterogeneous opportunities for businesses and growth.<sup>6</sup> Moreover, diversifying income sources to interest and dividend payments can augment the return and improve wealth. Thus, when the “rich” have better access to financial services than the “poor”, they have higher chances to become richer, tilting the income distribution.

<sup>6</sup> For a discussion about the link between finance and growth see Levine (2005).

## E. Policy Recommendations

**14. International experiences show that public policies can significantly improve financial inclusion.** While financial inclusion in SSA differs widely from country to country, some countries such as Tanzania, Rwanda, and Kenya have made rapid progress in widening access to financial services. Worldwide, more than half of financial regulatory frameworks include measures for promoting financial inclusion and a set of relevant best practices can be identified.

**15. The public policy agenda should include measures to address the main supply barriers to financial access.** A national or regional strategy needs to be set up with measurable targets and a coordinating institution. Regulations should foster innovative finance such as mobile banking as they lower transaction costs and will allow offering financial services at lower costs, thereby widening their usage. At the same time, it remains paramount to protect the consumers and ensure proper supervision of innovative banking or microfinance. In particular, the efforts to create a good environment for microfinance and mobile banking should continue by fostering collaboration between commercial banks and microfinance institutions and telecommunication companies. Improving legislation, property rights and documentation should improve access to finance. Ongoing implementation of the electronic payment system for taxes and utilities has to move forward and development of the banking branches network encouraged. Further reforms should aim to improve the business environment and judicial framework, boost supervision capacities, reduce asymmetry of information, and facilitate loan recovery to boost the financing of new investments and growth.

## References

- Allen, F., Carletti, E., Cull, R., Qian, J., Senbet, L., Valenzuela, P. 2012a. "Resolving the African Financial Development Gap: Cross-Country Comparisons and a Within-Country Study of Kenya", NBER Working Paper 18013.
- Allen, F., Demirguc-Kunt, A., Klapper, L., Peria, M. S. 2012b. "The Foundations of Financial Inclusion: Understanding Ownership and Use of Formal Accounts." World Bank Policy Research Working Paper 6290.
- Beck T., E. Feyen, A. Ize, and F. Moizeszowicz, Benchmarking Financial Development, World Bank Policy Research Working Paper 4638, (Washington, DC: World Bank, 2006).
- Alter, A and B Yontcheva, Financial Inclusion in the CEMAc region" IMF Working Paper, forthcoming
- Brookings Institution. 2012. Mobile Financial Services and Financial Inclusion. Washington, DC: Brookings Institution  
[http://www.brookings.edu/~media/events/2011/5/16%20mobile%20financial/0516\\_mfs\\_event\\_summary.pdf](http://www.brookings.edu/~media/events/2011/5/16%20mobile%20financial/0516_mfs_event_summary.pdf)
- Demirguc-Kunt, A., and L. Klapper. 2012a. "Measuring Financial Inclusion: The Global Index Database." World Bank Policy Research Working Paper 6025.
- Demirgüç-Kunt, A., and L. Klapper. 2012b. "Financial Inclusion in Africa: An Overview." World Bank Policy Research Working Paper 6088.
- Finscope, 2012, Financial Inclusion in Rwanda 2008–2012,  
<http://www.finmark.org.za/blog/publication/financial-inclusion-in-rwanda-2012/>
- G20 Information Center. "G20 Leaders Statement: The Pittsburgh Summit."  
<http://www.g20.utoronto.ca/2009/2009communique0925.html>
- G20 Information Center. "Principles for Innovative Financial Inclusion."  
<http://www.g20.utoronto.ca/2010/to-principles.html>
- Levine, Ross. 2005. "Finance and Growth: Theory and Evidence" in Philippe Aghion and Steven Durlauf (eds.), Handbook of Economic Growth. Amsterdam: North-Holland Elsevier Publishers.
- Piketty, T. 2003. "Income Inequality in France, 1901–1998". Journal of Political Economy, Vol. 111, No. 5 (October 2003) , pp. 1004–1042.
- World Bank. 2012. Measuring Financial Inclusion: The Global Index Database. Washington, DC: World Bank. [http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2012/04/19/000158349\\_20120419083611/Rendered/PDF/WPS6025.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2012/04/19/000158349_20120419083611/Rendered/PDF/WPS6025.pdf)
- World Bank. 2011. Financial Inclusion Data.  
<http://datatopics.worldbank.org/financialinclusion/region/sub-saharan-africa>