

The contents of this document are preliminary and subject to change.
--

GRAY/08/1679

May 22, 2008

**Statement by Mr. He and Mr. Yung on WAEMU
(Preliminary)
Executive Board Meeting 08/45
May 23, 2008**

We thank staff for the well-presented and informative papers reflecting staff's efforts to maintain close and constructive dialogue with the WAEMU authorities. We also thank Mr. Rutayisire for his comprehensive Buff statement.

WAEMU's economic performance continues to lag behind its peer countries and per-capita growth remains insufficient to help reduce poverty in a substantial way. It is unfortunate that adverse shocks have imposed further limitations on the authorities' macroeconomic management capacity. According to staff, the authorities face two key challenges: (i) the need to maintain macroeconomic stability in the face of sociopolitical and economic pressures created by rising food and energy prices; and (ii) the need to accelerate structural and other reforms to improve the region's business environment and overall competitiveness. In this respect, we agree with staff's policy recommendations.

We support the authorities' call to review access to Fund financing for LICs facing severe threat from recent inflation. Like most developing regions, WAEMU countries face social tensions from rising food and fuel prices that call for prompt response. We agree with staff's recommendations that any such response needs to be regionally coordinated and targeted, and consistent with fiscal sustainability and available financing. It is encouraging to note from Mr. Rutayisire that WAEMU Ministers of Finance recently coordinated a three-year plan aimed at achieving food self-sufficiency in the region. In the short term, WAEMU countries have taken different short-term fiscal measures to curb rising food prices and help relieve social pressures. It is important that these measures are temporary and do not crowd out the necessary public initiatives.

We encourage the authorities to accelerate structural reforms in the WAEMU to help strengthen the resilience of the region's financial sector. We consider that successful reforms are key to foster banks' steady and healthy growth over time. At present, WAEMU banks are

particularly fragile—their capital adequacy ratios are deteriorating and around one-third of them fail to meet the minimum statutory capital requirement. We see merit in staff's recommendation to strengthen prudential regulation enforcement. Unless there is a well-established framework or arrangement enabling supervisors to carry out their prudential duties and enforce banks' compliance with the relevant laws and regulations, we do not think that imposing a one-off increase in the minimum capital requirement or capital adequacy ratio can be effective in mitigating the vulnerabilities in WAEMU's banking sector.

Nevertheless, we share the concern on the capital adequacy of WAEMU banks. In an attempt to address the issue, the authorities have raised the minimum statutory capital requirement significantly from CFAF 1 billion to CFAF 10 billion. Is the new requirement applicable to existing banks? If so, in what ways can banks source the additional funding required to meet the capital requirement? If the new requirement implies a consolidation of banks in the region, how does it affect competition in the banking sector? And will it result in a reduction of banking outlets? We would like staff's elaboration.

We note that the authorities need to implement measures to improve the WAEMU's business environment. Persistent structural constraints in human resource development, the cost of starting a business and the economic infrastructure have adversely affected FDI inflows to WAEMU countries. We note that the region profits less than others from productivity and competitiveness gains associated with FDI. An improved environment for doing business will help attract FDI and enhance growth prospects for the region.

We agree that the CFA franc's peg to the euro continues to serve the WAEMU region well. We welcome staff's assessment that the region's REER is broadly in line with its long-run equilibrium and economic fundamentals. Given the characteristics and economic conditions of the WAEMU region, the authorities' continued commitment to a credible peg is essential in ensuring the stability and sustainability of their macroeconomic management.

We join staff in welcoming the authorities' decision to remove barriers to intra-WAEMU trade. However, the progress toward regional integration—both within the WAEMU and the wider ECOWAS region—has been limited. The authorities concur with staff that there is still a long way to go on the convergence agenda. The scope and benefit of financial integration can only be maximized with substantial integration in real sectors. In this regard, we are encouraged by the political commitment to the new initiatives and actions to facilitate trade as noted by Mr. Rutayisire. Nevertheless, there is no doubt that the process of preparing for monetary union can be, in itself, highly beneficial. We encourage the authorities to continue to promote trade and financial integration so as to develop the institutional and regulatory prerequisites for common markets.

With these remarks, we wish the authorities success in their future endeavors.