EXECUTIVE BOARD MEETING

SM/17/58

March 17, 2017

To: Members of the Executive Board

From: The Acting Secretary

Subject: **West African Economic and Monetary Union—Staff Report on Common Policies of Member Countries**

Board Action:	Executive Directors' **consideration** (Formal)
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Questions:	Mr. Loko, AFR (ext. 30337) Ms. Yontcheva, AFR (ext. 39912)
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WEST AFRICAN ECONOMIC AND MONETARY UNION

STAFF REPORT ON COMMON POLICIES OF MEMBER COUNTRIES

March 15, 2017

KEY ISSUES

Context. The WAEMU region has experienced strong growth over the last five years but vulnerabilities have increased. Public debt is on the rise and external buffers have shrunk. Good progress has been made in upgrading the financial sector regulatory framework but significant pockets of vulnerability remain. The outlook remains positive, provided macroeconomic stability and strong resolve to improve the business environment and promote private investment are maintained. Downside risks stem from a sharper slowdown of economic growth, tighter international financing conditions, delays in implementing fiscal consolidation, sluggish structural reforms as well as a sustained decline in cocoa prices. In addition, security threats remain significant.

Policy recommendations. Sustaining high growth will require improved coordination and consistency between national fiscal policies and regional monetary policy to contain vulnerabilities and safeguard macroeconomic stability, and accelerated structural reforms to enhance the business environment, boost competitiveness and foster diversification.

- **Fiscal and monetary policy**. The 2017 fiscal deficits are not compatible with regional financial stability, and substantial adjustment efforts will be needed over the coming years to deliver on fiscal consolidation required to preserve debt sustainability and support the external position. The decision to tighten monetary policy in late 2016 is welcome. While fiscal policy should be the first line of defense, the BCEAO should stand ready to tighten monetary conditions further if pressures on external reserves continue. Enhancing liquidity management will help develop interbank and capital markets and improve the effectiveness of monetary policy.

- **Financial sector.** Enforcing existing prudential regulations, preparing implementation of the upgraded prudential framework and consolidated supervision, developing a financial safety net and an effective resolution regime, and fostering financial inclusion and deepening would support the development of a healthy financial sector.

- **Competitiveness and diversification.** Structural policies aimed at improving competitiveness and fostering regional integration are critical to sustain the current growth momentum and make further inroads in reducing poverty.

Approved By
Roger Nord and Peter Allum

Discussions were held in Lomé and Ouagadougou during December 12-16, and in Abidjan, and Dakar during February 7–15. The staff team comprised Mr. Loko (head), Ms. Yontcheva (both AFR), Mr. Awad (MCM), and Ms. Zdzienicka (SPR). The mission was assisted by Mr. Feler (resident representative in Cote D'Ivoire), and Ms. Diouf (resident representative in Burkina Faso).

WAEMU countries are Benin, Burkina Faso, Côte d'Ivoire, Guinea- Bissau, Mali, Niger, Senegal, and Togo. They share the same currency, the CFA franc, which is pegged to the euro.

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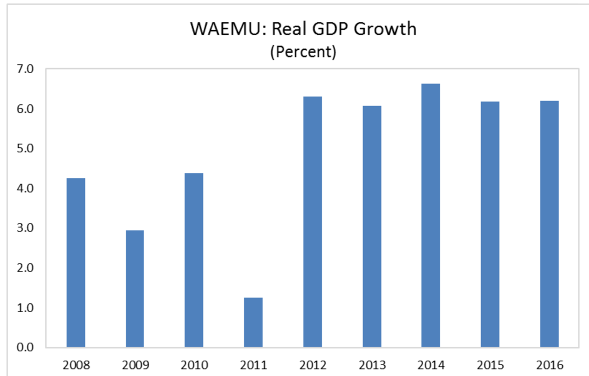
CONTEXT: ROBUST GROWTH BUT GROWING VULNERABILITIES

1. **The WAEMU region has experienced solid growth over the last five years but vulnerabilities have increased, and challenges remain significant.** The region's economy grew rapidly (on average 6.3 per annum), largely driven by high public investment. Inflation remained subdued, well below the 3 percent convergence criterion. However, public debt rose while external buffers shrank. Reserve coverage sharply declined in 2016, falling below 4 months of imports. While the macroeconomic environment has been stable for several years, slow progress in structural reforms and regional integration has held back private investment, keeping poverty and unemployment high. The business environment remains relatively unattractive, intra-regional trade is low and the region has been slow to diversify and integrate into global value chains.



2. **Policies have been broadly in line with past Fund advice, although implementation in some areas has lagged.** The BCEAO[1] took measures to activate the interbank market and enhance monetary transmission mechanisms. In particular, the Central bank increased its lending facility rate from 3.5 to 4.5 percent spread, and announced that the recourse to its lending facility will be capped at twice banks' capital starting June 2017. Important steps were also undertaken to promote financial stability. These reforms include the adoption of Basel II and III capital standards, and the introduction of consolidated supervision. Nonetheless, conditions in the banking sector remain challenging. Credit and concentration risks are important and the ratio of gross NPLs to total loans is still relatively high while the situation of several troubled banks remains unresolved. At the national level, there has been no progress on fiscal consolidation and little improvement of the business climate. Strengthening the capacity of the WAEMU Commission in helping countries improve revenue collection and public financial management is overdue.

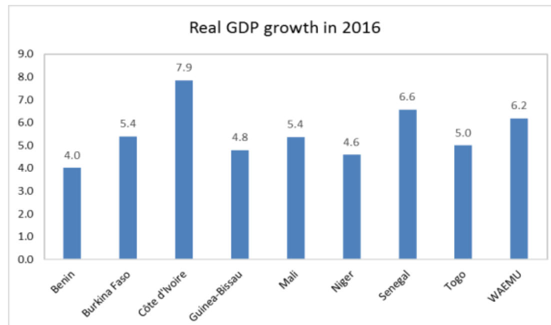
[1] The West African Economic and Monetary Union (WAEMU) and the West African Monetary Union (WAMU) cover the same 8 countries. The BCEAO (Banque Centrale des Etats de l'Afrique de l'Ouest) is the central bank of the WAMU and the WAMU Banking Commission is the financial sector supervisor. The WAEMU Commission and the BOAD (Banque Ouest Africaine de Développement) focus on economic integration and development of the WAEMU.

RECENT ECONOMIC DEVELOPMENTS, OUTLOOK AND RISKS

A. Recent Developments

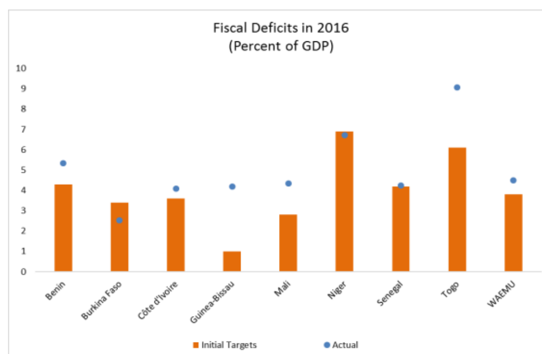
3. Economic activity has remained strong but vulnerabilities have increased. On the positive side, economic growth was robust and inflation subdued. However, as GDP growth was driven by domestic demand and notably public investment, fiscal and current account deficits remain high, and public debt is on the rise.

- ***Economic growth was robust in 2016***. Real GDP growth is expected to have reached 6.2 percent in 2016 (Table 1), underpinned by robust and resilient domestic demand. Growth was particularly strong in Cote d'Ivoire and Senegal, the two largest economies of the Union. In contrast, growth was lower than expected in Benin, reflecting, at least partially, spillovers from the difficult macroeconomic situation in Nigeria.

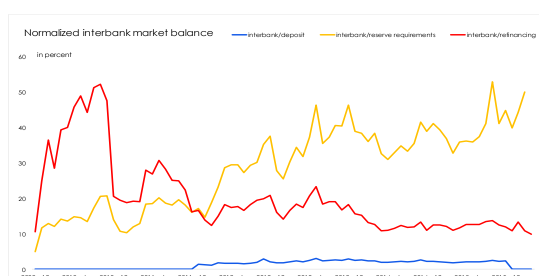


- ***Inflation has been low.*** Headline inflation remained subdued, at about 0.4 percent on average in 2016 due to continued solid agricultural production and low oil prices.

- **Fiscal consolidation was deferred again and deficits remained high.** As in recent years, planned fiscal consolidation was deferred in 2016 and most countries further scaled up public investment. Preliminary data suggest an overall fiscal deficit of 4.5 percent of GDP in 2016, higher than initially planned (4 percent). Only in Burkina Faso, Niger, and Senegal fiscal deficits are below or at initial targets in 2016.

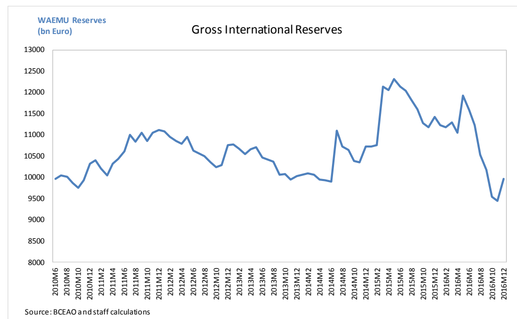


- **Monetary policy tightened.** Credit to the public sector expanded much faster (43.8 percent) than credit to the private sector (9.7 percent). However, money growth remained moderate (10.2 percent), as net foreign assets declined. The BCEAO decided on December 6, 2016 to widen the spread between the minimum bid rate for the open market refinancing operations (its de facto

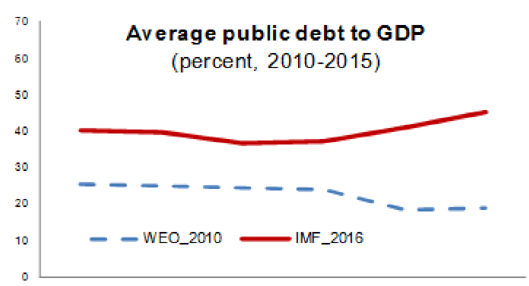


policy rate) and the credit facility rate to 200 basis points. The minimum bid rate was kept unchanged at 2.5 percent but the lending facility rate was increased from 3.5 to 4.5 percent. The BCEAO also decided to limit access to refinancing by banks to a maximum amount of twice a bank's capital.[2] The increase in the lending rate has tightened monetary conditions and led to higher interbank activity. However, on March 1, 2017, the Monetary Policy Committee (MPC) decided to reduce the reserve requirement (RR) ratio to 3 percent of deposits (from 5 percent). The reduction in the RR ratio should provide additional liquidity and reduce the need for refinancing, but will weaken somewhat the benefit expected from the December 2016 decisions.

- **External buffers have shrunk significantly.** The exchange rate appears broadly in line with fundamentals (Annex I). A deterioration in the current account deficit (by 0.3 percentage point in 2016) and a reduction in the financial account surplus (1 percentage point) contributed to lower regional reserves sharply by CFAF1000 billion (about $2 billion) to 3.7 months of imports in 2016 (from 4.5 months in 2015) or 54 percent of regional broad money, and 78 percent of short-term debt. Large fiscal deficits in 2016 were likely a key factor behind the current account deterioration. The factors contributing to the weaker financial account are not fully understood, at this stage, and warrant close monitoring.



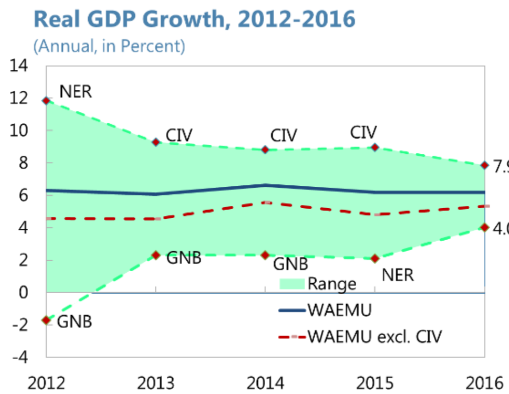
- **Public debt is on the rise.** High fiscal deficits have led to an increase in public debt from 43.9 percent in 2015 to 45.9 percent in 2016. Although staff analysis suggest that the level of debt is still sustainable (Annex II), the increasing reliance on non-concessional loans has heightened debt vulnerabilities.



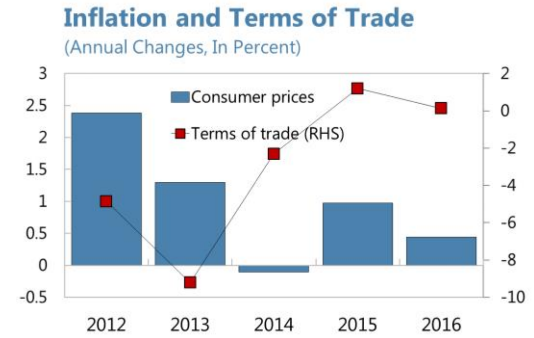
[2] The BCEAO stopped accommodating the demand for excess reserves at its operations, starting December 2015.

Figure 1. WAEMU: Recent Economic Developments

Economic activity has remained strong in 2016,

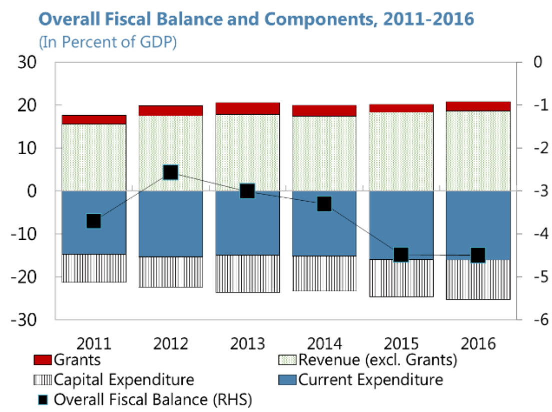


... with low inflation

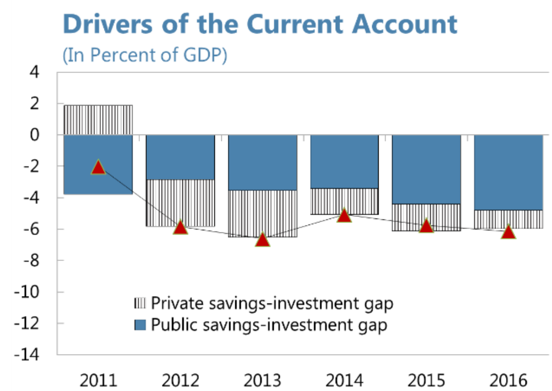


*Excl. food and energy. 2014 underlying inflation number refers to October 20
Sources: BCEAO and IMF staff projections.

Ongoing capital expenditures keep the fiscal deficit at a high level...

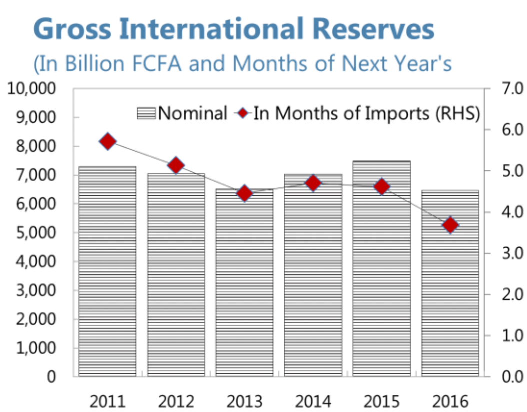


... and widen the current account deficit ...

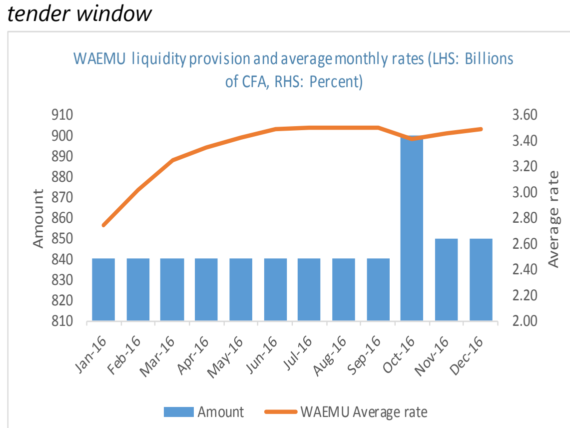


*2011: Crisis in Côte d'Ivoire.

... while deteriorating the reserve coverage.



The monetary policy stance has been tightened as the BCEAO widened the band between the permanent and the tender window



Source: BCEAO and staff calculation.

Box 1. WAEMU: Monetary Policy Framework

The BCEAO relies on:

- *Two types of open market operations*: refinancing for seven days and twenty-eight days (respectively each week and each month to banks subject to the reserve requirement) allocated at variable rates; the minimum bid rate which the BCEAO considers as its policy rate (currently 2.5 percent). The intended allotment is normally calibrated based on the BCEAO's forecast of the liquidity needs during the maturity of the operations.

- *Two types of standing lending facilities*: refinancing 1 to 7 days or for 90 to 360 days against government securities and credit claims with maturities ranging from 5 to 20 years at the demand of the banks. The facilities are priced 200 basis points above the policy rate. Starting in June 2017, recourse to the lending facility will be capped at twice the counterparty's capital.

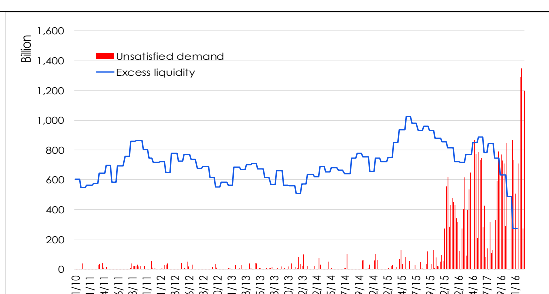
Until December 2015, the BCEAO steered short-term rates close to its minimum bid rate. The calibration of the allotment, based on the outstanding refinancing and the expected change in autonomous factors, satisfied most demand for refinancing and the auction weighted average rate hovered at around five basis points above the minimum bid rate. As refinancing fully accommodated the demand from banks (including for excess reserves[1]) and provided a high certainty with regard to the roll-over of outstanding loans, it reduced the need for interbank transactions.

At End-December 2015, the BCEAO stopped accommodating the demand for excess reserves. Since end-2015, the BCEAO levelled off its refinancing to gradually reduce the allotment toward the liquidity need arising from autonomous factors and the reserves requirement, thereby discontinuing the accommodation of the demand for excess reserves.

***At End-December 2016, the BCEAO increased* the spread between the minimum bid rate at its open market refinancing operations and the lending facility from 100 to 200 basis points**. Consequently, the refinancing weighted average rate has increased by more than 100 basis points. This result combined with the December 2015 decision are expected to boost the interbank market.

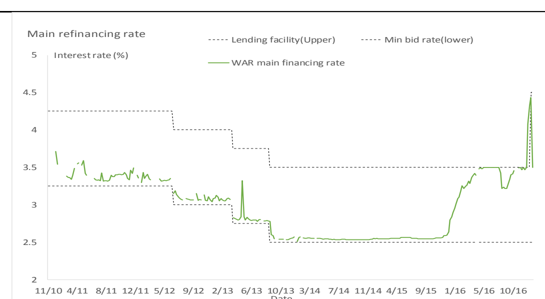
[1]The demand for excess liquidity is due to market segmentation and incompressible reserves in addition of the autonomous factors.

Oversubscription at the BCEAO 7-day Refinancing Operations



Source: BCEAO.

Weighted Average Rate of the 7-day Refinancing Operations



Source: BCEAO.

B. Outlook and Risks

4. The outlook hinges on country-level fiscal consolidation. Under the baseline**,** growth is projected to stay above 6 percent over the medium term assuming accelerated reforms to improve the business environment and promote private investment, enhanced technical capacity, and better accountability and governance in member countries. Inflation would remain low on account of continued solid agricultural production. The overall fiscal deficit of the region would increase to 4.7 percent of GDP in 2017 before declining to 3 percent in 2019, in line with the WAEMU convergence criterion, if governments implement their fiscal consolidation plans.[3] The current account deficit is expected to widen in 2017, reflecting continuous public investment efforts—related imports of intermediated goods and equipment—and less favorable terms of trade. Increasing FDI—especially for large investment projects in Niger, Burkina Faso, and Senegal—and other investment are expected to fully finance the current account deficit in 2017. Over the medium term, country goals for fiscal consolidation and assumed steps to improve external competitiveness are projected to gradually reduce the current account deficit to 5.3 percent of GDP by 2021. FDI with capital grants are expected to remain the main sources of its financing. Public debt would start declining from 2018 in relation to GDP, while international reserves are projected to increase to 4 months of next year's imports by 2019 (up from 3.5 months' cover at end-2017).

5. The reserve buffer would remain below optimal levels. The current and projected medium-term reserve cover is above the thresholds required by the zone's monetary arrangement with France.[4] However, reserve cover would remain below the optimal buffer against external shocks, estimated by staff as corresponding to a reserve cover of 5 to 12 months of imports—depending on the interest rate differential with the rest of the world (Dabla Norris et al., 2011).

Text Table 1. WAEMU: Selected Macroeconomic Indicators; 2013–21

	2013	2014	2015	2016 (est.)	2017	2018	2019 (proj.)	2020	2021
Output									
Real GDP growth (%)	6.1	6.6	6.2	6.2	6.5	6.6	6.5	6.6	6.5
Prices									
Inflation (average, %)	1.3	-0.1	1.0	0.4	1.5	1.9	1.9	2.0	2.0
Central government finances									
Overall balance incl. grants (% GDP)	-3.0	-3.3	-4.5	-4.5	-4.7	-3.7	-3.0	-2.7	-2.5
Public debt (% GDP)	37.6	38.5	44.5	45.9	46.3	44.8	43.1	41.3	40.7
Balance of payments									
Current account (% GDP)	-6.6	-5.1	-5.8	-6.1	-6.3	-6.0	-6.0	-5.7	-5.3
Reserves (months imports)	4.5	4.7	4.6	3.7	3.5	3.9	4.0	4.0	4.0

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

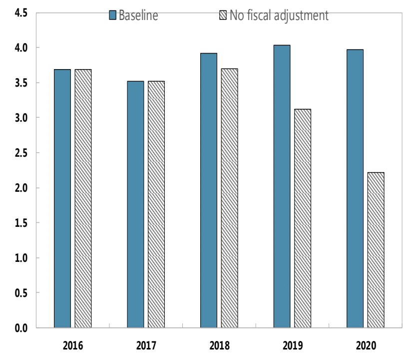
[3] The baseline does not envisage that all countries will reach the deficit of 3 percent in 2019. Burkina Faso (3.5 percent of GDP) and Niger (4.7 percent of GDP) breach the criterion.

[4] The arrangement with France provides an operation account on which the BCEAO can draw in case of reserve shortage—a mechanism akin to an overdraft possibility. However, in exchange of the French guaranteeing of the CFA Franc peg to the Euro, BCEAO countries must hold 50 percent of their exchange reserves at the French Treasury, and 20 percent of the BCEAO liabilities must be covered by foreign reserves.

6. **This outlook is subject to substantial downside risks** that could—in particular, in the current context of a limited room for maneuver—reduce regional economic growth down to 1.5 percent over the medium term (RAM).

- ***Recurrent delays in fiscal consolidation pose increasing risks to the outlook.*** The current baseline scenario contemplates a slight increase in deficits in 2017 (4.7 percent of GDP compared to 4.5 percent in 2016). This represents a clear deterioration with respect to expectations at the time of the 2016 Article IV, when the deficit was projected at 3.4 percent of GDP in 2017. Given upward revisions to the 2017 fiscal deficits, country plans for substantial fiscal consolidation in 2018 and beyond are appropriate to preserve debt sustainability and external stability. Planned fiscal consolidation has been repeatedly deferred in recent years, and there are risks of fiscal slippage in 2017 and beyond. Sustained departures from the planned fiscal paths would eventually put debt sustainability and the currency coverage at risk. Staff simulations suggest that if fiscal deficits remained at the levels observed in 2016 for another five years, the GIR coverage could fall to 2 months of imports by 2021. Given this analysis, it would be important to respond promptly to any emerging fiscal slippage with steps to reinforce budget management. This could also require parallel steps to tighten monetary policy and adjust the external/domestic financing mix.

External Sustainability in the Absence of Fiscal Consolidation: Impact on Official Reserves (in months of imports)

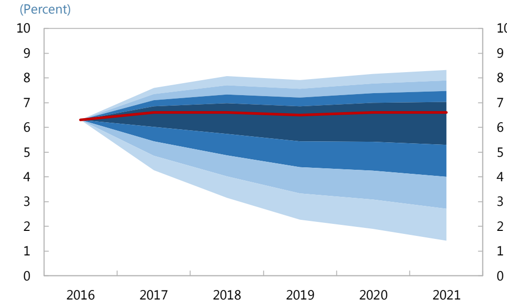


- **Lack of progress in raising public investment efficiency and advancing private-sector friendly structural reforms could slow down the growth momentum**. With many countries undertaking large infrastructure investments, a delay in PFM reforms and inefficient investment could worsen debt, fiscal and external sustainability, with negative implications for growth and poverty reduction. Over the medium term, growth cannot indefinitely continue to depend primarily on public investment. Without structural reforms to improve the business climate and access to finance —and, therefore, without a pick-up in private investment and improvement of competitiveness—the domestic and external stability of the region could significantly weaken.

- **The region is also not immune to rising uncertainty in the global economy.** Retreat from cross-border integration, a significant slowdown in emerging market growth, and structurally weak global growth could reduce foreign aid, financing, remittances, and exports, and, thus, undermine the macro-financial stability of the WAEMU. While some upside risks could result from a further strengthening of the U.S. dollar (i.e., increase revenues of certain exports), a stronger US dollar would also increase the sovereign debt burden of countries with unhedged dollar exposures and the overall cost of imports. Tighter.

financing conditions at the international level would also affect the availability and cost of external financing for the region. Staff simulations show that a slowdown in global growth (of 0.5 percent) coupled with a fall in commodity prices (20 percent), including cocoa, one of the region's major exports, could reduce regional growth to under 2 percent by 2019, that is, 4 percentage points lower than the baseline projections.[5]

Real GDP: Outlook Risks
(Percent)



Source: IMF staff projections.

- **Security-related risks remain high in the region**. Beyond the immediate human toll, security issues would put further pressure on national budgets, reduce external financing, and likely result in substantial delays in implementing major investment projects.

7. Authorities' views: The authorities broadly agreed with staff views on the outlook and risks. They were particularly concerned by the drop in cocoa prices and potential fiscal slippages in 2017. They also pointed out that informal trade is an underestimated spillover channel of regional shocks and that the impact of a slowdown in Nigeria could have significant impact on some members (Benin, Togo). The authorities agreed that, should the above-mentioned downside risks materialize, further monetary policy and fiscal tightening, along with adjustment in the external/domestic financing mix, will be required to preserve external stability. There was agreement between staff and the authorities on the need to step up efforts to rebuild policy buffers and resilience in order to avoid the need for abrupt policy responses, should downside risks materialize.

POLICY DISCUSSIONS

Against the background of the sharp drop in reserves in 2016, sustaining the current growth momentum would require a stable macroeconomic environment anchored around prudent fiscal and monetary policies and accelerated structural reforms to promote financial stability and inclusion, improve the business environment, and boost competitiveness and diversification.

[5] Simulations of global shocks: we consider two scenarios. An "Emerging Markets Slowdown scenario" where global growth slows by a cumulative 1.6 percent during 2016–19, relative to the Fall 2016 WEO baseline, recovering in later years. Commodity prices follow a similar dynamic, falling relative to the baseline by 10 percent for fuel and 6 percent for metals over 2016–19. The second scenario "Global Growth Shock" assumes a sustained slowdown in global growth of 0.5 percent relative to the first scenario, coupled with a 20 percent decline in commodity prices relative to the baseline. This scenario focuses on shocks of particular relevance to LIDCs and should be seen as a low probability event.

A. Macroeconomic Policies: Meeting Development Needs While Preserving Debt sustainability and External Stability

Risks to public debt sustainability and external stability have risen, calling for a well-articulated path toward a sustainable fiscal position, increased coordination and consistency between national fiscal policies and regional monetary policy, and improved debt management.

Background

8. Vulnerabilities have increased. Public debt is on the rise and regional reserves have dropped. The decline in reserves results from several factors. First and foremost, delays in fiscal consolidation in most member countries, the BCEAO's accommodative refinancing policy, and weak mobilization of external financing. Fiscal deficits remained high in most member countries, and in the context of reduced external financing, the regional public debt market was the major source of financing in 2016. The increased reliance on domestic financing contributed to the deterioration of the external position due to the high import content of public capital expenditure. Second, commercial banks had more recourse to the BCEAO for their foreign exchange needs, owing to simplified and faster administrative procedures. Meanwhile, the overall repatriation rate of export receipts continued its increasing trend of recent years, suggesting that capital flight did not play a role in the decline in reserves.

Staff's recommendations

9. International reserves should increase to provide higher buffers against shocks. Reserve cover would remain below optimal levels on existing policies. This warrants a reinforced effort to strengthen external competitiveness through structural reforms and/or further strengthen fiscal balances to build reserve cover towards at least 5 months of import cover.

10. Growth-friendly fiscal consolidation is needed to reduce public debt and lift pressure on monetary policy and reserves. The BCEAO and the WAEMU Commission should convey forcefully to member governments the need to stick to their planned current fiscal consolidation paths, which lead to an overall regional fiscal deficit of 3 percent of GDP in 2019, in line with the WAEMU convergence criteria. Fiscal plans for 2017 and 2018 need to be consistent with that target. Achieving this goal while filling the gap in infrastructure investments and creating more room for social protection will require steadfast implementation of reforms to enhance revenue mobilization, contain current expenditure, improve public financial management, increase public investment efficiency and strengthen debt management. Strengthened regional institutions are needed to help achieve these objectives and enforce fiscal targets. Focus should be on:

- *Expanding fiscal space*: Progress has been made in recent years to improve revenue collection, but more remains to be done to meet the WAEMU convergence criterion of 20 percent of GDP by 2019. In particular, the WAEMU Commission could help

(i) strengthening revenue administrations and ensuring taxpayer compliance; (ii) further broadening the tax base, including by attracting informal firms to the formal sector and accelerating property tax reforms; (iii) improving the exchange of information between tax and customs administrations and effectively implementing the common tariff; and (iv) reducing tax expenditure, and adopting and implementing regulations to limit base erosion and profit shifting by multinational corporations. Room exists to improve the composition and the quality of spending. Public wage bills should be kept below 35 percent of domestic revenue (WAEMU criterion) and subsidies and social assistance should be well-targeted to protect the most vulnerable. Several key WAEMU convergence criteria remain unobserved in the majority of member countries, and current projections suggest that breaches will persist in several countries over the medium term (Text Table 2). Technical assistance from the IMF and other development partners can help countries with the reform implementation.

Text Table 2. WAEMU: Number of Countries Violating Convergence Criteria, 2015—21

	2015	2016	2017	2018	2019	*2020*	2021
		Est.				*Proj.*	
First-order criteria							
Overall Balance/GDP (≥ - 3 percent)	6	7	7	7	*3*	*2*	*1*
Average consumer price inflation (≤ 3 percent)	0	0	0	0	0	*0*	*0*
Total debt/GDP (≤ 70 percent)	1	1	1	0	0	*0*	*0*
Second-order criteria							
Wages and salaries/tax revenue (≤ 35 percent)	6	6	6	4	3	*3*	*3*
Tax revenue/GDP (≥ 20 percent)	8	7	7	7	6	*6*	*6*

Sources: WAEMU; Central Bank of West African States (BCEAO); and staff estimates and projections.

- *Improving public investment*. The WAEMU Commission and the BOAD should help countries build capacity and improve the overall planning, programming, budgeting, monitoring and evaluation of projects.

- *Promoting public-private partnerships* (PPPs). The authorities should fully explore concessional financing options before considering non-concessional resources and private sector participation. In a context of limited resources, further development of alternative forms of financing, such as PPPs, is needed to support infrastructure investment. PPPs, if appropriately planned and managed, could help provide financing for much-needed infrastructure investment. However, PPPs carry some fiscal risks, particularly as regards pricing and contingent liabilities. It is crucial that country authorities put in place the appropriate legal and institutional frameworks as well as adequate accounting and reporting frameworks to promote efficiency and manage risks.

- *Enhancing debt management*: The WAEMU Commission should continue to help countries improve debt management capacity. Coordination between countries, particularly with respect to the issuance of Eurobonds, may be needed to limit debt rollover risks. The WAMU Securities Agency (UMOA-Titres) could help ensure such coordination.

11. While fiscal policy should be the first line of defense, **the BCEAO should stand ready to tighten monetary conditions if pressures on external reserves continue**. Staff welcomed the December 2016 decision of the Monetary Policy Committee of the BCEAO to increase its credit facility rate and tighten access to the refinancing window (Box 1).[6] These measures could support the reserve cover by increasing the cost of domestic resources and pushing governments to limit their fiscal deficits and recourse to financing in the regional market. Staff recommended keeping monetary policy on hold as the impact of recent measures feeds through the economy. However, should international reserves continue to decline, additional monetary policy measures would be necessary, for example by raising the BCEAO policy rate or further widen its interest rate spread.

12. The BCEAO should improve its monetary policy effectiveness. The banking system is segmented between a few large international banks, pan-African groups, and small local banks which undermines market development and monetary policy transmission. The large international banks hold most excess liquidity but do not use it to buy government securities and trade only within their groups.[7] As a result, the interbank market is shallow. The BCEAO is the leading source of refinancing. The increase in the BCEAO's credit facility rate in December 2016 and the tighter access to its refinancing window has prompted a sharp increase in transactions on the interbank market. Reforms will require:

- *Energizing the interbank market*. Efforts should be made to establish an interbank reference rate, and stimulate repurchase (repo) operations, including by better aligning the local legal framework for repo operations with international standards. The effective implementation of the new prudential framework (including capital requirements in accordance with Basel II/III) should help reduce counterparty credit risk and enhance confidence in the interbank market.

- *Further improving liquidity management*: The BCEAO should calibrate its open market operations based on market liquidity needs arising from the autonomous factors and the reserve requirement (which level should be adjusted to provide enough buffer above the banks' incompressible balance).

[6] These measures could potentially affect growth by reducing both public and private investment. The impact via the public sector could, however, be limited if member countries implement fiscal consolidation plans that protect growth-enhancing public investment. The impact on the private sector in the WAEMU should also be relatively small because banks in liquidity need and resorting to refinancing have not been providing significant credit to the private sector. They have instead engaged in a carry trade by acquiring government paper and benefiting from the interest rate differential.

[7] Most of the international banks have already reached their internal statutory ceilings on country-specific exposures imposed by their headquarters.

- *Developing healthy financial markets*. The limit imposed on banks' access to refinancing in December 2016 appears to have slowed transactions in the regional public debt market. In that context, strong resolve is needed to make government paper more attractive for other institutional investors such as pension and insurance funds and for international investors. In particular, an active debt management allowing for the development of a risk-free yield curve would support both monetary policy transmission and the development of the capital market. Other actions include (i) establishing individual ratings for all member countries; (ii) merging or linking the two existing clearing and depository systems (one for auction-based issues and another for syndication based-issues); (iii) allowing brokerage institutions (SGIs) to be full-fledged actors in the auction market;[8] and (iv) harmonizing the tax treatment of government securities throughout the region and eliminating tax distortions discriminating against non-resident investors. Over time the BCEAO should move to a full interest rate corridor system, which will promote secondary market development and improve monetary transmission channels.

Authorities' views

13. The WAEMU Commission and the BCEAO agreed that coordination and consistency between national fiscal policies and regional monetary policy is essential to contain vulnerabilities, and preserve macroeconomic stability and the growth momentum. They acknowledged, however, the important challenges involved in getting member countries to adhere to their fiscal consolidation plans. They believed that recent monetary policy decisions would encourage countries that have the capacity to rely more on external financing. Staff agreed, but underlined that while this could stem pressure on international reserves in the short run, in the medium term, fiscal deficits need to be reduced to preserve the external position. While agreeing to convey this message to member governments, the BCEAO underscored that the IMF should play an important role in improving consistency between national fiscal policies and regional monetary policy as, with Fund programs in most WAEMU countries, fiscal policy was largely determined by Fund-agreed targets. The authorities saw no need to tighten monetary policy further at the moment. Nevertheless, they were committed to take further monetary policy action should external reserves decline further. The BCEAO also indicated they would pursue their efforts to improve compliance with the regulations requiring 80 percent repatriation of export receipts.

14. The BCEAO broadly agreed with staff on the need for strengthening the effectiveness of monetary policy. They believed that recent monetary policy decisions to widen the interest rate corridor and limit access to refinancing would help improve liquidity management and boost the interbank market. The authorities pointed out that further progress

[8] The network of primary dealers includes commercial banks and brokerage institutions (SGI). However, existing regulations permit only commercial banks to hold accounts with the central bank. Therefore, an SGI, which is being invited to be a primary dealer can only transact in primary issues of sovereign bonds by opening an account with a commercial bank. This exposure is likely to deter the SGI from primary market activity.

on financial market deepening is a continued priority. The BCEAO would seek technical assistance from the Fund as needed.

B. Promoting Financial Stability and Inclusion

The recent improvements to the regulatory framework represent a commendable progress. Efforts are, however, needed to address the current pockets of vulnerability in the banking system by enforcing existing prudential regulations and adequately preparing for the effective implementation of the upgraded regulatory framework. Fostering financial inclusion and deepening will also be critical.

Background

15. A set of ambitious regulatory reforms was adopted by the regional Council of Ministers in June 2016. These new regulations included the adoption of Basel II and III capital standards, the introduction of consolidated supervision (including over WAEMU-based financial holding companies), and the tightening of the large exposure limit. The Basel II and III regulations introduced capital requirements for operational and market risks and increased the minimum requirements to 9 percent.[9] The regulations also included capital buffers and surcharges (mainly a common equity capital conservation buffer of 2.5 percent). In addition, the single large exposure limit was reduced to 25% of banks' Tier 1 capital.[10] Transitional implementation arrangements were also introduced spanning from 2018 until 2022. In addition, the council of ministers adopted a decision giving the BCEAO and the Banking Commission the power to regulate and supervise financial holding companies on a consolidated basis.[11] Other measures include (i) the adoption of a new banking chart of accounts; and (ii) the reorganization of the Banking Commission to integrate the monitoring of crisis resolution processes and supervision of large microfinance institutions and other specialized institutions such as mobile money firms.

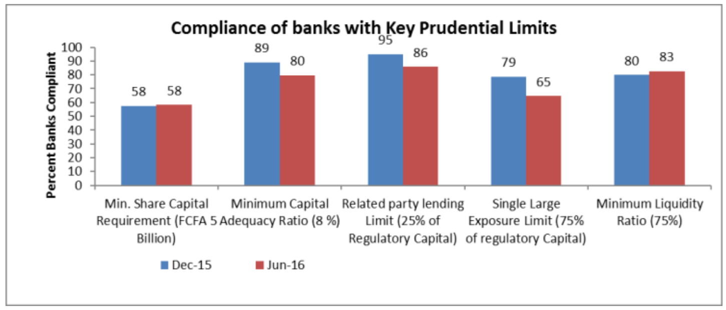
16. The BCEAO has continued to enhance the supervision of Pan-African banks. In particular, it organized in 2016 supervisory colleges for the two WAEMU-based Pan-African banks, and the BCEAO participated in supervisory colleges organized by home supervisors of Moroccan, Nigerian and Central African banking groups having subsidiaries in the region.

[9] The current capital adequacy requirements covered only credit risk and the minimum capital adequacy ratio was 8 percent. The new requirements are based on Basel II standardized approach for credit risk, basic indicator approach (or standardized approach) for operational risk, and standardized approach for market risk. The new minimum capital requirements of 9 percent, should comprise a minimum of 5 percent common equity Tier 1 capital and 6 percent total Tier 1 capital.

[10] The single large exposure limit is currently set at 75 percent of banks' total regulatory capital.

[11] This decision enters into effect in 2018.

17. Conditions in the banking sector remain challenging. The current rules—despite being less strict than the newly introduced ones—are not effectively enforced. Only 57 out of 102 banks comply with the minimum share capital of CFA 10 billion at end-June 2016.[12] In addition, the current capital adequacy of the regional banking sector remains relatively weak at 9.6 percent in June 2016, which signals that banks would need significant reinforcement in their capital levels to meet the new stricter requirements that will be phased in starting January 2018. Four banks (mainly state-owned) are under temporary administration and 14 banks remain under closer supervisory scrutiny, accounting for around 16.1 percent of the banking sector assets at end-June 2016. Credit and concentration risks are important and the ratio of gross NPLs to total loans is still relatively high at 15.6 percent at end-September 2016. In addition, around 40 percent of banks are in violation of the relatively soft single large exposure limit at the same period.



18. Dealing with weak and problem banks is also hampered by the lack of an effective resolution regime and weak financial safety nets. Resolution of troubled banks is often delayed and challenged in part due to the shared powers with national authorities. A new deposit insurance fund (FGD) was established but major milestones remain to be completed before it becomes operational.[13] Authorities hope that these actions would be completed in 2017. In addition, the Council of Ministers has approved in 2015 the establishment of a resolution framework and has mandated the BCEAO Governor to propose the practical modalities and functions of such a resolution regime. Authorities indicated that they are currently amending the Annex to the Convention establishing the Banking Commission to introduce, among others, resolution clauses that would include designating a regional resolution authority and establishing a resolution fund.

19. The strong link between banks and sovereigns remains a concern. About 27 percent of bank assets consist of government securities. As shown in Annex III, the demand for BCEAO refinancing can be at least partially explained by increased investment in sovereign securities.

[12] The minimum share capital for banks was increased from CFAF 5 billion to CFAF 10 billion in July 2015. Banks have two years, i.e. till June 2017, to comply with the new requirements.

[13] The organizational structure of the FGD and the recruitment of three of its employees were done in 2016. In addition, drafting of some procedures and circulars has started. The main remaining actions that need to be completed before the FGD becomes operational include: adoption of the circulars related to membership requirements, contribution rates, and reimbursement rules by the FGD Board of Directors, finalizing working procedures for the FGD and setting its accounting system, collection of data related to bank deposits and assessment of contributions, and finally launching the FGD website.

20. Despite the progress made in recent years to improve financial inclusion and development, WAEMU countries still lag behind benchmark countries. Access to finance and utilization of financial services remain low especially for the most vulnerable parts of the population. The Council of Ministers approved in June 2016 a framework for a regional strategy promoting financial inclusion as well as an associated action plan and budget for this strategy. This five-year strategy aims at expanding access and use of financial services and products to 75 percent of the WAEMU adult population.

Staff's recommendations

21. Enforcing existing prudential regulations, preparing for the effective implementation of the new regulations, and enhancing the financial safety nets should be a priority. In order to achieve these objectives, reforms should focus on:

- *Further strengthening bank supervision*: this calls for (i) upgrading supervisory tools in order to implement risk-based supervision (assessing the risk profile of banking institutions, enhancing the bank rating system, conducting stress tests, automating reporting tools and procedures, etc.); (ii) strengthening AML/CFT supervision, including by implementing dissuasive sanctions for breach of compliance with preventive measures related to domestic politically-exposed persons; (iii) taking the needed preparatory steps to implement consolidated supervision of banking groups (including those structured under holding companies); (iv) implementing the new reporting framework and improving the Banking Commission information system; and (v) strengthening supervisory capacity and resources.

- *Ensuring that the new prudential framework is effectively enforced within the set timeframe*: it is important to ensure that the banks take the measures and actions needed to cover their capital needs when the new prudential framework enters into force. Prompt action is also needed to finalize the draft instructions and circulars related to the new prudential framework, and authorities should continue their engagement with various stakeholders, including banks, to explain the main requirements of the new regulations and address any implementation issues.

- *Continuing efforts to strengthen cross-border supervision of banking groups*: it is important in this respect to continue organizing supervisory colleges of large cross-border banking groups and reinforce cooperation agreements and joint supervisory activities with foreign supervisory authorities.

- *Making the Deposit Guarantee Fund (FGD) fully operational and establish an effective regional bank resolution framework*: the authorities should ensure that the regional bank resolution framework that is currently being developed is in line with international standards and principles, particularly those issued by the Financial Stability Board. The annex to the Convention governing the Banking Commission should be amended without delay to incorporate provisions enabling the Commission to act as a resolution authority (as provided by the regional Council of Ministers in July 2015) with adequate resolution powers, and establishing a bank resolution fund.

- *Acting to further promote financial inclusion*: the necessary steps should be taken to fully implement the regional action plan and strategy for financial inclusion adopted by the regional Council of Ministers in June 2016. This will require, inter alia, a reduction of the cost of financial services, strengthening of the legal framework and the business environment, and improved financial education and protection for financial consumers.

Authorities' views

22. The authorities agreed with the thrust of staff views on financial stability and stressed that they will continue their reforms to upgrade financial sector regulation and supervision. They underscored that recent reforms, including the adoption of Basel II and III capital framework, will enhance the resilience of banks against potential shocks and vulnerabilities. The BCEAO also indicated that the introduction of credit bureaus and the plan to reduce large exposure limits will reduce credit and concentration risks. The BCEAO fully agreed that the resolution authority should be endowed with the necessary powers and independence.

C. Fostering Sustainable Growth

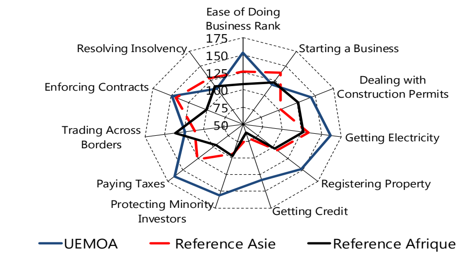
Promoting competitiveness and diversification would help contain vulnerabilities and sustain high growth.

23. Accelerating the pace of reforms and fostering regional integration are important to improve competitiveness and resilience of the region. Survey-based indicators indicate very limited progress in improving structural competitiveness compared to African and Asian peers. The region scores low in the business climate and global competitiveness indicators with significant obstacles persisting in, for instance, registering property, dealing with construction permits, getting credit and electricity, paying taxes, and the availability of infrastructure, technology, and specialized labor. Infrastructure gap remains important, and public investment efficiency is limited (IMF, 2015), resulting in high costs of communication, transport and electricity and a challenging business and investment climate. To increase competitiveness and improve resilience to the shocks—but also integrate into and move up the global value chains—the region will need to close rapidly structural reforms and investment gaps, and foster regional integration. Coordinate and decisive policy actions at both regional and national levels are essential to this end.

Reforms have continued at a slower pace …

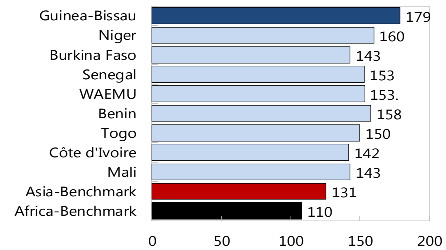
… in most of WAEMU countries…

Doing Business 2016
(place permit 189 pays)



Source: World Bank, Doing Business 2016

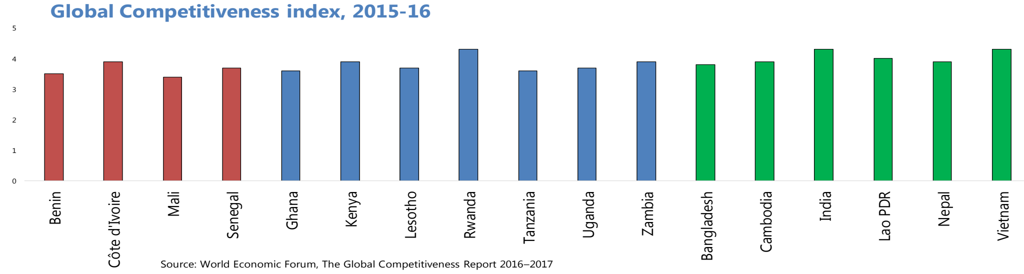
2.Ease of Doing Business 2016
(Rank among 189 Economies)



Sources: World Bank, Doing Business 2016

… but business and investment climate remain challenging and the region shows competitive disadvantages compared to the peers

Global Competitiveness index, 2015-16



Source: World Economic Forum, The Global Competitiveness Report 2016–2017

Authorities' Views

24. **The authorities agreed with the thrust of staff's recommendations**. They highlighted ongoing efforts to address infrastructure gaps, reduce the cost and alleviate the burden of doing business, promote financial inclusion and deepening, and strengthen human capital.

OTHER ISSUES

25. **The latest safeguards assessment of the BCEAO, conducted in 2013, found a continuing strong control environment**. All recommendations from the assessment have been implemented. These include strengthening the external audit arrangements by appointment of an international firm with ISA experience for the audits of FY 2015–17, reinforcing the capacity of the audit committee with external expertise to oversee the audit and financial reporting processes, and adoption of IFRS starting with the financial year 2015.

26. **It is important to further strengthen the quality, timeliness, and public availability of economic statistics.** Progress has been made in recent years, but there is still a need for better and more timely data, notably external sector statistics. Staff pointed to the need to develop a framework of macroeconomic, vulnerability and risk indicators to enhance the regular surveillance of economic developments in the Union. Staff encouraged the BCEAO to report

timely official reserves for the monetary union to avoid delays in the forthcoming subscription by Senegal to the Special Data Dissemination Standards (SDDS).[14]

STAFF APPRAISAL

27. Economic activity remains strong but vulnerabilities have increased. Real GDP growth exceeded 6 percent for the 5th year in a row, and inflation has remained subdued. However, fiscal consolidation was deferred again and deficits remain high, further pushing up public debt. The external position is broadly consistent with regional fundamentals and desirable policy settings. Reserve coverage declined sharply in 2016, reflecting larger than expected fiscal deficits, fueled by continued expansion in public infrastructure spending, and lower-than-expected external financing.

28. The outlook is positive but remains subject to significant downside risks. Growth is expected to remain around 6 percent. But risks to the outlook include global uncertainties, further slippages in fiscal consolidation plans, sluggish structural reforms, as well as a sustained decline in cocoa prices. Security-related risks remain high in the region. These risks could—in particular in the current context of a limited room for maneuver—dampen growth and require quick policy responses.

29. A well-articulated path toward a sustainable fiscal position and enhanced coordination and consistency between national fiscal policies and regional monetary policy are crucial to reduce vulnerabilities, maintain macroeconomic stability and sustain the growth momentum. The 2017 fiscal deficits are not compatible with medium-term external stability. Member countries need to stick to their current budget deficit reduction plans. The focus should be on reforms to enhance revenue mobilization and contain current expenditure to expand space for development needs. More attention will need to be paid to debt management and to the quality rather than the quantity of public investment. Further development of alternative forms of financing, such as PPPs, is also needed to support infrastructure investment. The BCEAO should stand ready to tighten monetary policy if pressures on external reserves continue.

30. The December 2016 decisions of the Monetary Policy Committee of the BCEAO to increase its credit facility rate and tighten access to the refinancing window are welcome. These measures are expected to affect primarily banks involved in government securities carry trade financed with BCEAO refinancing. They should increase the cost of government borrowing in the regional market and encourage banks to reconsider their risk policy and participate more in the interbank market. This would help reduce market segmentation, which has been a main cause of excess liquidity. However, while the March 1, 2017 decision to reduce the reserve requirement ratio should provide additional liquidity, it will weaken somewhat the benefit

[14] The SDDS prescribes the dissemination of data on official reserve assets on a monthly basis (weekly periodicity is encouraged) within one week after the end of the reference month.

expected from the December 2016 decisions. Further progress to improve liquidity management, energize the interbank market, and deepen financial markets will help enhance monetary transmission mechanisms.

31. Financial stability and deepening should remain top priorities. Staff commended the authorities for the ambitious set of regulatory reforms adopted in June 2016, to modernize the financial sector. Key reforms included adopting Basel II and Basel III capital standards and introducing consolidated supervision of cross-border banks. The authorities should continue these efforts by enforcing existing prudential regulations, preparing implementation of upgraded prudential framework and consolidated supervision; making the financial safety net (FGD) operational and developing an effective regional bank resolution regime.

32. Efforts to enhance financial inclusion should be intensified. In particular, implementation of the regional action plan and strategy for financial inclusion needs to be accelerated. Reforms should focus on lowering the cost of financial services, strengthening the legal framework and judicial processes, enhancing the business environment, and boosting the development of mobile banking, while paying due consideration to financial stability and anti-money laundering issues.

33. Addressing structural constraints to promote private investment, competiveness and diversification will help secure sustainable and inclusive growth. Structural reforms should focus on improving the business environment, reducing barriers to regional trade, including cumbersome administrative procedures, and enhancing regional infrastructures.

34. The quality, coverage and timeliness of regional data need to improve. Staff encouraged the authorities to pursue efforts to enhance economic statistics, in particular external sector statistics and financial soundness indicators.

35. The discussions with the WAEMU authorities will be on the 12-month cycle in accordance with Decision No. 13656-(06/1), as amended.

Table 1. WAEMU: Selected Economic and Financial Indicators, 2012–21

Social Indicators

GDP		**Poverty**	
Nominal GDP (2015, millions of US Dollars)	91293	Headcount ratio at $2 a day (2011 PPP, percent of population)	39.6
GDP per capita (2015, US Dollars)	827	Undernourishment (2012, percent of population)	12.3
Populations charateristics		**Inequality**	
Total (2015. millions)	110.33	Income share held by highest 10 percent of population (DATE)	32.1
Urban Population (2015, percent of total)	40	Income share held by lowest 20 percent of population (DATE)	6.3
Life expectancy at birth (2014, years)	58.8	Gini index	40.7

Economic Indicators

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
					Est.			Proj.		
	(Annual percentage change)									
National income and prices										
GDP at constant prices	6.3	6.1	6.6	6.2	6.2	6.5	6.6	6.5	6.6	6.5
GDP per capita at constant prices	3.4	3.3	3.7	3.3	3.3	3.6	3.7	3.6	3.8	3.6
Broad money to GDP	-2.5	3.2	4.7	2.4	4.0	...	...	...	...	...
Consumer prices (average)	2.4	1.3	-0.1	1.0	0.4	1.5	1.9	1.9	2.0	2.0
Terms of trade	-4.9	-9.2	-2.3	1.2	0.1	0.1	-1.2	-1.7	-0.6	1.1
Nominal effective exchange rates	-2.3	4.3	3.8	-3.8	2.0	...	...	...	...	...
Real effective exchange rates	-2.6	2.7	1.0	-5.5	-0.4	...	...	...	...	...
	(Percent of GDP)									
National accounts										
Gross national savings	15.6	15.9	17.0	15.0	16.1	17.1	17.7	17.5	18.1	18.3
Gross domestic investment	21.4	22.5	22.1	21.2	22.1	23.4	23.7	23.5	23.7	23.5
Of which: public investment	5.7	7.4	7.1	7.8	8.2	8.9	8.7	8.4	8.6	8.4
	(Annual changes in percent of beginning-of-period broad money)									
Money and credit [1]										
Net foreign assets	-2.1	-6.0	0.1	-1.7	0.0	...	...	...	...	...
Net domestic assets	11.9	16.4	12.7	0.4	14.7	...	...	...	...	...
Broad money	9.8	10.5	12.9	-1.3	14.7	...	...	...	...	...
Credit to the private sector	14.8	15.6	14.3	15.6	12.4	12.1	11.6	13.6	12.8	13.5
	(Percent of GDP, unless otherwise indicated)									
Government financial operations [2]										
Government total revenue, excl. grants	17.5	17.8	17.4	18.3	18.6	19.2	19.4	19.8	20.1	20.2
Government expenditure	22.6	23.8	23.5	24.9	25.5	26.1	25.4	25.0	25.0	24.8
Official grants	2.5	3.0	2.7	2.1	2.4	2.2	2.2	2.2	2.1	2.2
Overall fiscal balance, incl. grants (cash basis)	-2.6	-3.0	-3.3	-4.5	-4.5	-4.7	-3.7	-3.0	-2.7	-2.5
Basic fiscal balance, incl. grants & HIPC	-1.6	-1.4	-1.6	-1.5	-1.5	-0.9	-0.3	0.3	0.6	0.9
External sector										
Exports of goods and services [3]	26.7	24.3	23.7	24.3	23.9	24.1	25.8	23.0	22.7	22.3
Imports of goods and services [3]	34.5	35.7	35.2	33.2	33.5	33.6	34.8	31.9	31.1	30.1
Current account, excl. grants [4]	-7.2	-9.1	-7.5	-8.0	-8.8	-8.9	-8.4	-8.4	-7.9	-7.4
Current account, incl. grants [4]	-5.8	-6.6	-5.1	-5.8	-6.1	-6.3	-6.0	-6.0	-5.7	-5.3
External public debt	24.6	24.5	23.9	27.9	27.9	28.1	27.8	27.6	27.1	26.9
Total public debt	36.5	37.6	38.5	44.5	45.9	46.3	44.8	43.1	41.3	40.7
Broad money	27.9	28.8	30.1	30.8	32.1	...	...	...	...	...
Memorandum items:										
Nominal GDP (billions of CFA francs)	43,200	46,194	49,918	53,968	57,991	62,584	67,969	73,667	79,969	86,726
Nominal GDP per capita (US dollars)	835	897	943	827	867	899	951	1,007	1,069	1,126
CFA franc per US dollars, average	511	494	494	591	601	...	...	...	...	...
Foreign exchange cover ratio [5]	98.4	84.0	77.0	71.1	...	...	...	...	...	...
Reserves in months of imports (excl. intra-WAEMU imports)	5.1	4.5	4.7	4.6	3.7	3.5	3.9	4.0	4.0	4.0

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

[1] Year on year change, end December; for 2014 year on year change, end November.

[2] Fiscal data for 2014 reflect a strong increase in the fiscal deficit of Niger, following a new project in the hydrocarbon sector.

[3] Excluding intraregional trade.

[4] Data up to 2011 are corrected for intraregional trade discrepancies by BCEAO.

[5] Gross official reserves divided by short-term domestic liabilities (IMF definition).

Table 2. WAEMU: Selected National Accounts and Inflation Statistics, 2012–21

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
				Est.			Proj.			
				(Annual percentage change)						
Real GDP										
Benin	4.8	7.2	6.4	2.1	4.0	5.4	6.0	6.3	6.7	7.1
Burkina Faso	6.5	5.7	4.2	4.0	5.4	6.1	6.3	6.5	6.5	6.5
Côte d'Ivoire	10.1	9.3	8.8	8.9	7.9	7.9	7.8	7.3	7.2	6.9
Guinea-Bissau	-1.7	3.3	2.3	4.8	4.8	5.0	5.0	5.0	5.0	5.0
Mali	-0.8	2.3	7.0	6.0	5.4	5.3	4.8	4.7	4.7	4.7
Niger	11.8	5.3	7.0	3.5	4.6	5.2	5.5	5.4	7.4	6.2
Senegal	4.5	3.6	4.3	6.5	6.6	6.8	7.0	7.1	7.1	7.1
Togo	5.9	6.1	5.4	5.3	5.0	5.0	5.3	5.4	5.6	5.6
WAEMU	6.3	6.1	6.6	6.2	6.2	6.5	6.6	6.5	6.6	6.5
Real GDP per capita										
Benin	2.0	4.4	3.6	-0.4	1.5	2.9	3.6	3.9	4.4	4.8
Burkina Faso	3.2	3.2	1.1	1.2	2.5	3.2	3.5	3.6	3.7	3.7
Côte d'Ivoire	7.3	6.5	6.1	6.2	5.1	5.1	5.1	4.6	4.5	4.2
Guinea-Bissau	-3.8	1.0	0.1	2.5	2.5	2.7	2.7	2.7	2.7	2.7
Mali	-3.8	-0.7	3.7	2.7	2.1	2.0	1.6	1.5	1.5	1.5
Niger	8.5	2.1	3.8	0.4	1.4	2.0	2.4	2.3	4.2	3.0
Senegal	1.5	0.6	1.4	3.5	3.5	3.7	4.0	4.0	4.0	4.1
Togo	3.1	3.3	2.6	2.5	2.2	2.2	2.5	2.6	2.8	2.8
WAEMU	3.4	3.3	3.7	3.3	3.3	3.6	3.7	3.6	3.8	3.6
Inflation										
Benin	6.7	1.0	-1.1	0.3	-0.8	2.1	2.2	2.2	2.2	2.1
Burkina Faso	3.8	0.5	-0.3	0.9	0.7	1.5	2.0	2.0	2.0	2.0
Côte d'Ivoire	1.3	2.6	0.4	1.2	1.0	1.5	2.0	2.0	2.0	2.0
Guinea-Bissau	2.1	0.8	-1.0	1.5	2.4	2.6	2.8	3.0	3.0	3.0
Mali	5.3	-0.6	0.9	1.4	-1.6	0.8	1.2	1.6	1.9	2.1
Niger	0.5	2.3	-0.9	1.0	1.1	2.0	2.1	2.0	2.0	2.0
Senegal	1.4	0.7	-1.1	0.1	1.1	1.7	1.8	1.8	1.8	1.8
Togo	2.6	1.8	0.2	1.8	0.9	1.5	1.9	2.0	2.0	2.0
WAEMU	2.4	1.3	-0.1	1.0	0.4	1.5	1.9	1.9	2.0	2.0
				(Percent of GDP)						
Gross national savings										
Benin	15.1	20.4	20.0	17.6	17.4	20.8	20.4	19.8	21.4	23.1
Burkina Faso	7.9	7.0	12.7	5.3	6.0	9.0	10.2	10.3	10.8	10.6
Côte d'Ivoire	16.0	16.7	18.6	16.8	17.3	17.7	18.7	18.5	18.8	18.7
Guinea-Bissau	-4.5	0.1	7.9	11.9	9.9	9.1	8.6	9.3	9.6	9.9
Mali	15.0	14.9	12.9	10.1	11.8	13.3	14.6	14.5	14.4	14.1
Niger	24.8	25.2	23.8	24.5	24.1	24.0	24.3	24.5	24.6	24.6
Senegal	18.5	17.3	16.1	16.6	20.7	20.5	20.3	19.5	20.7	21.0
Togo	16.3	11.4	15.7	15.9	17.6	17.3	16.3	16.1	18.1	19.5
WAEMU	15.6	15.9	17.0	15.0	16.1	17.1	17.7	17.5	18.1	18.3
Gross domestic investment										
Benin	22.6	27.8	28.6	26.0	24.5	29.3	27.3	26.3	27.2	27.9
Burkina Faso	14.9	18.2	20.8	13.3	13.6	15.8	16.7	17.2	17.8	17.7
Côte d'Ivoire	17.2	18.1	17.1	17.8	19.3	20.2	21.2	21.2	21.4	21.1
Guinea-Bissau	7.4	7.3	11.4	12.5	12.8	13.2	13.4	13.4	13.5	13.8
Mali	17.2	17.8	17.6	17.4	19.5	20.3	20.1	20.0	20.1	20.0
Niger	39.5	40.2	39.3	42.6	39.5	42.0	42.8	43.0	40.1	37.9
Senegal	29.3	27.8	25.1	24.0	27.2	27.4	27.3	26.6	27.6	27.8
Togo	23.8	24.5	25.7	27.0	27.4	26.4	24.6	23.5	24.6	24.9
WAEMU	21.4	22.5	22.1	21.2	22.1	23.4	23.7	23.5	23.7	23.5

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

Table 3. WAEMU: Selected Fiscal Indicators, 2012–21

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
				Est.			Proj.			
				(Percent of GDP)						
Primary fiscal balance										
Benin	0.1	-2.1	-1.5	-7.3	-4.3	-6.0	-2.5	-0.1	0.8	1.2
Burkina Faso	-2.4	-3.0	-1.1	-1.5	-1.8	-2.7	-2.8	-2.8	-2.8	-2.9
Côte d'Ivoire	-1.5	-0.8	-0.9	-1.3	-2.3	-1.8	-1.5	-1.1	-1.0	-1.1
Guinea-Bissau	-2.2	-1.7	-1.0	-1.1	-2.7	-1.0	-1.5	-1.2	-1.2	-0.2
Mali	-0.4	-1.9	-2.3	-1.2	-3.6	-3.5	-3.0	-2.4	-2.3	-2.3
Niger [1]	-0.8	-2.3	-7.6	-8.5	-5.7	-6.3	-4.9	-3.4	-1.7	0.2
Senegal	-3.7	-4.0	-3.3	-2.8	-2.4	-1.6	-0.8	-0.8	-0.8	-1.0
Togo	-5.5	-4.1	-5.3	-6.5	-7.2	-6.1	0.4	2.6	2.2	2.2
WAEMU	-1.8	-2.2	-2.3	-2.9	-3.1	-3.0	-2.0	-1.4	-1.1	-1.0
Overall fiscal balance (including grants), cash basis										
Benin	-0.6	-2.4	-2.5	-8.0	-5.3	-7.6	-4.3	-1.9	-0.8	-0.2
Burkina Faso	-2.8	-2.7	0.4	-3.6	-2.5	-3.6	-3.5	-3.5	-3.5	-3.5
Côte d'Ivoire	-2.2	-2.0	-3.1	-2.8	-4.1	-3.8	-3.5	-3.1	-2.9	-3.0
Guinea-Bissau	-2.3	-1.8	-2.3	-2.6	-4.2	-1.7	-2.1	-1.6	-1.7	-0.8
Mali	-1.0	-2.4	-2.4	-3.2	-4.3	-4.5	-3.7	-3.2	-3.1	-2.9
Niger	-0.9	-3.2	-6.6	-9.4	-6.7	-8.3	-6.2	-4.7	-2.9	-0.9
Senegal	-5.2	-5.5	-5.0	-4.8	-4.2	-3.7	-3.0	-3.0	-3.0	-3.0
Togo	-7.0	-5.8	-7.9	-7.8	-9.4	-9.7	-3.2	-0.3	0.0	0.1
WAEMU	-2.6	-3.0	-3.3	-4.5	-4.5	-4.7	-3.7	-3.0	-2.7	-2.5
Government revenue (excluding grants)										
Benin	17.4	17.6	16.3	16.7	14.7	15.3	15.9	16.7	17.3	17.8
Burkina Faso	17.5	19.0	17.5	15.9	18.3	18.9	19.3	20.0	20.1	20.2
Côte d'Ivoire	18.6	18.4	17.1	18.8	19.1	19.6	19.8	19.8	20.1	20.2
Guinea-Bissau	9.1	7.9	12.6	14.1	13.2	12.8	13.1	13.4	13.7	14.0
Mali	14.4	14.5	14.9	16.4	16.9	17.9	18.2	18.6	19.1	19.1
Niger	15.3	16.6	17.5	18.1	15.3	16.1	16.8	17.5	19.1	20.3
Senegal	20.2	20.1	21.4	22.2	23.7	23.5	23.1	23.1	23.2	22.1
Togo	17.6	18.1	18.2	19.6	18.9	20.2	21.0	21.8	22.2	21.9
WAEMU	17.5	17.8	17.4	18.3	18.6	19.2	19.4	19.8	20.1	20.2
Government expenditure										
Benin	19.6	21.0	19.1	25.3	21.2	24.6	21.9	20.2	19.5	18.9
Burkina Faso	25.5	28.0	23.6	21.5	24.5	26.5	26.8	27.5	27.3	27.5
Côte d'Ivoire	22.3	21.9	21.0	23.1	24.7	24.8	24.8	24.5	24.5	24.5
Guinea-Bissau	13.8	13.1	23.6	22.6	21.3	19.5	20.8	20.8	21.3	20.7
Mali	15.5	19.7	20.0	20.9	23.2	24.3	23.8	23.7	23.9	24.0
Niger	22.5	27.2	31.0	32.7	26.5	28.1	27.3	26.4	26.0	24.4
Senegal	28.5	28.1	29.8	29.9	30.7	28.7	27.7	27.6	27.5	27.6
Togo	26.4	26.6	27.3	30.8	31.4	33.8	27.8	25.6	26.2	25.7
WAEMU	22.6	23.8	23.5	24.9	25.5	26.1	25.4	25.0	25.0	24.8
Government current expenditure										
Benin	14.2	14.0	14.2	17.2	15.3	14.5	14.3	14.0	13.6	13.4
Burkina Faso	14.5	13.9	14.6	14.1	15.2	14.7	14.6	14.6	14.5	14.6
Côte d'Ivoire	17.8	15.9	15.3	16.6	17.3	16.9	16.5	16.3	16.1	16.3
Guinea-Bissau	12.3	9.6	16.8	15.6	15.3	12.6	12.2	12.1	12.0	11.9
Mali	11.3	12.2	11.9	11.9	12.7	13.1	12.9	12.9	13.0	13.1
Niger	11.4	13.5	14.6	15.6	14.4	14.6	14.2	13.9	13.4	13.2
Senegal	17.3	17.2	18.5	18.6	17.8	16.0	15.7	15.7	15.4	15.4
Togo	17.6	17.4	16.0	17.8	17.4	17.8	18.0	17.2	17.0	16.9
WAEMU	15.4	14.9	15.1	16.0	16.0	15.6	15.3	15.1	15.0	15.0
Government capital expenditure [2]										
Benin	5.2	6.4	5.2	7.7	5.8	10.0	7.6	6.2	5.9	5.5
Burkina Faso	11.0	14.6	9.1	7.6	9.4	11.8	12.2	12.9	12.8	12.9
Côte d'Ivoire	4.5	6.0	5.7	6.4	7.5	7.8	8.3	8.2	8.4	8.2
Guinea-Bissau	1.4	3.5	7.6	8.2	7.1	7.2	8.5	8.7	9.3	9.0
Mali	2.7	6.0	6.5	7.3	9.4	9.9	9.7	9.6	9.6	9.6
Niger	11.1	13.7	16.4	17.1	12.1	13.5	13.1	12.5	12.5	11.3
Senegal	11.2	10.9	11.3	11.3	12.9	12.7	12.1	11.9	12.1	12.2
Togo	8.8	9.3	11.3	13.0	14.0	12.0	9.8	8.4	9.2	8.9
WAEMU	7.0	8.7	8.2	8.7	9.3	10.1	9.9	9.7	9.8	9.6

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

[1] 2014 data for Niger reflect the impact of a new project in the hydrocarbon sector which is reflected in net lending (included in the government total expenditure in this table).

[2] Excludes net lending.

Table 4. WAEMU: Balance of Payment, 2011–21

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
					Est.			Proj.			
				(Percent of GDP)							
Balance on current account	-2.0	-5.8	-6.6	-5.1	-5.8	-6.1	-6.3	-6.0	-6.0	-5.7	-5.3
excluding official transfers:	-3.4	-7.2	-9.1	-7.5	-8.0	-8.8	-8.9	-8.4	-8.4	-7.9	-7.4
Balance on goods and services	-4.4	-7.8	-9.8	-8.4	-8.9	-9.6	-9.5	-9.0	-8.9	-8.3	-7.8
Exports of goods	28.4	27.8	26.3	25.2	25.0	24.6	25.6	25.9	26.2	26.5	26.9
Exports of services	5.0	4.8	4.7	4.4	4.2	4.1	4.0	3.9	3.8	3.8	3.6
Imports of goods	-27.7	-30.3	-29.8	-27.7	-27.7	-27.3	-28.3	-28.4	-28.7	-28.7	-28.8
Imports of services	-10.0	-10.0	-11.1	-10.4	-10.3	-11.0	-10.9	-10.4	-10.2	-9.9	-9.6
Income, net	-1.9	-2.3	-2.1	-2.1	-2.1	-2.1	-2.2	-2.1	-2.1	-2.1	-2.0
Income credits	1.5	1.3	1.3	1.4	1.5	1.5	1.5	1.4	1.4	1.4	1.4
Income debits	-3.4	-3.7	-3.5	-3.5	-3.6	-3.6	-3.6	-3.6	-3.5	-3.4	-3.4
Of which											
Investment income, debit: interest	-0.6	-0.7	-0.6	-0.6	-0.6	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Current transfers, net	4.3	4.2	5.3	5.4	5.2	5.6	5.3	5.1	5.0	4.8	4.6
Private current transfers, net	3.0	2.9	2.9	2.9	3.0	2.9	2.8	2.7	2.6	2.1	2.0
Official current transfers, net	1.3	1.3	2.5	2.5	2.3	2.7	2.6	2.4	2.4	2.2	2.1
Balance on capital and financial account	1.7	4.7	6.0	5.1	7.3	4.1	6.7	6.6	6.5	5.8	5.6
Balance on capital account	1.6	11.3	2.4	2.1	2.0	2.0	1.9	1.8	1.7	1.6	1.6
Balance on financial account	0.1	-6.6	3.6	3.0	5.2	2.1	4.8	4.9	4.8	4.2	4.1
Direct investment, net	2.2	2.3	2.8	2.0	2.0	2.7	3.0	3.3	3.5	3.5	3.5
Portfolio investment, net	1.2	0.7	0.1	2.0	1.1	0.6	0.6	0.4	0.5	0.3	0.4
Other investment, net	-3.3	-9.6	0.7	-1.0	2.2	-1.2	1.2	1.1	0.8	0.4	0.1
Errors and omissions, net	0.3	0.2	0.3	0.8	0.2	-0.2	0.0	0.0	0.0	0.0	0.0
Overall balance[1]	0.0	-1.0	-0.3	0.8	1.7	-2.2	0.4	0.7	0.5	0.2	0.3
Change in official NFA ("-" increase)	-0.7	0.9	1.3	-0.5	-1.7	2.2	...	...	...	...	...

Source: IMF, African Department database.

[1]Excludes revaluation differences for 2015.

Table 5. WAEMU: Government Debt, 2012–21

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
					Est.			Proj.		
					(Percent of GDP)					
External Debt										
Benin	15.3	16.7	19.8	21.3	23.2	25.8	27.0	28.3	27.5	26.6
Burkina Faso	22.6	21.9	22.0	23.8	23.9	23.2	23.1	23.0	23.4	23.7
Côte d'Ivoire	28.2	25.9	26.7	29.8	28.9	28.2	27.4	26.6	25.7	25.4
Guinea-Bissau	26.7	24.8	24.4	24.3	22.4	22.2	22.6	22.5	22.6	22.7
Mali	21.8	21.5	21.0	23.4	22.9	23.8	24.4	25.4	26.6	27.8
Niger	16.7	17.6	22.1	27.9	31.6	33.5	34.7	35.8	35.8	36.1
Senegal	30.6	32.6	40.3	41.1	39.9	38.7	37.5	36.5	35.8	35.1
Togo	13.3	14.3	17.1	21.1	19.7	17.2	15.2	13.3	11.5	10.0
WAEMU	24.6	24.5	23.9	27.9	27.9	28.1	27.8	27.6	27.1	26.9
Domestic Debt										
Benin	11.4	8.6	10.6	21.1	25.0	26.6	25.7	22.2	19.0	16.2
Burkina Faso	5.7	7.4	8.6	8.7	8.6	10.2	10.6	11.0	11.2	11.5
Côte d'Ivoire	16.7	17.2	18.0	18.0	19.4	19.7	19.0	18.3	17.8	17.2
Guinea-Bissau	25.7	27.5	28.6	24.9	25.5	23.5	21.3	19.8	18.3	16.8
Mali	3.6	4.9	6.3	7.5	6.8	7.2	7.2	7.2	7.2	7.2
Niger	5.1	4.5	8.7	11.5	12.9	15.3	15.9	15.8	13.9	11.4
Senegal	12.2	14.4	14.1	15.8	18.4	17.0	12.4	8.4	5.2	7.3
Togo	31.5	42.1	48.1	54.5	59.4	53.7	47.6	39.4	34.4	30.0
WAEMU	11.9	13.1	14.6	16.6	18.0	18.2	17.0	15.5	14.2	13.7
Total Debt										
Benin	26.7	25.3	30.5	42.4	48.3	52.4	52.7	50.5	46.6	42.8
Burkina Faso	28.3	29.3	30.6	32.5	32.5	33.3	33.7	34.0	34.5	35.2
Côte d'Ivoire	44.9	43.1	44.7	47.8	48.3	47.9	46.4	44.9	43.4	42.5
Guinea-Bissau	52.5	52.3	53.1	49.2	47.9	45.7	43.9	42.4	40.8	39.5
Mali	25.4	26.4	27.3	30.9	29.7	31.0	31.6	32.6	33.8	35.0
Niger	21.8	22.1	30.8	39.4	44.6	48.7	50.6	51.5	49.7	47.5
Senegal	42.8	46.9	54.4	56.9	58.4	55.7	49.9	44.8	41.0	42.4
Togo	44.7	56.4	65.2	75.6	79.1	70.9	62.8	52.8	46.0	40.0
WAEMU	36.5	37.6	38.5	44.5	45.9	46.3	44.8	43.1	41.3	40.7

Source: IMF, African Department database.

Table 6. WAEMU: Monetary Survey, Dec. 2011–Dec. 2016

	2011 Dec.	2012 Dec.	2013 Dec.	2014 Dec.	2015 Dec.	2016 Dec.
	(Billions of CFA francs)					
Net foreign assets	**5,764**	**5,572**	**4,730**	**4,747**	**4,751**	**3,649**
Of which:						
BCEAO	5,963	5,562	4,997	5,238	5,482	4,529
Commercial Banks	-199	10	-267	-491	-731	-880
Net domestic assets	**7,094**	**8,496**	**10,910**	**12,903**	**15,491**	**18,668**
Domestic credit	10,345	11,900	14,248	16,753	19,616	22,989
Net credit to government	1,910	2,217	3,051	3,776	4,306	6,193
Net credit to the economy	8,435	9,683	11,197	12,977	15,310	16,796
Other items, net	-3,251	-3,405	-3,338	-3,850	-4,124	-4,321
Broad Money	**12,858**	**14,067**	**15,640**	**17,650**	**20,243**	**22,317**
Money	8,524	9,198	10,223	11,482	13,303	14,678
Of which: Currency in circulation	3,722	3,911	4,232	4,666	5,227	5,516
Quasi-money	4,335	4,869	5,417	6,168	6,939	7,639
	(Factors affecting liquidity, in percent of previous period's broad money)					
Net foreign assets	**3.2**	**-1.5**	**-6.0**	**0.1**	**0.0**	**-5.4**
Net domestic assets	**4.2**	**10.9**	**17.2**	**12.7**	**14.7**	**15.7**
Domestic credit	14.2	12.1	16.7	16.0	16.2	16.7
Net credit to government	0.6	2.4	5.9	4.6	3.0	9.3
Net credit to the economy	13.7	9.7	10.8	11.4	13.2	7.3
Other items, net	-10.0	-1.2	0.5	-3.3	10.3	16.2
Broad Money	**7.4**	**9.4**	**11.2**	**12.9**	**14.7**	**10.2**
	(Year on year percent change)					
Net foreign assets	**7.0**	**-3.3**	**-15.1**	**0.3**	**0.1**	**-23.2**
Net domestic assets	**7.7**	**19.8**	**28.4**	**18.3**	**20.1**	**20.5**
Domestic credit	19.7	15.0	19.7	17.6	17.1	17.2
Net credit to government	3.7	16.1	37.6	23.8	14.0	43.8
Net credit to the economy	24.0	14.8	15.6	15.9	18.0	9.7
Other items, net	58.2	4.7	-2.0	15.3	7.1	4.8
Broad Money	**7.4**	**9.4**	**11.2**	**12.9**	**14.7**	**10.2**

Source: BCEAO and Staff calculations.

Table 7. WAEMU: Monetary Projections, 2013–21

	2008-2013 average	2013	2014	2015	2016	2017	2018	2019	2020	2021
	CFAF billion									
Broad money	12,463	15,640	17,650	20,243	22,317	25,032	28,051	31,297	34,984	38,627
Net foreign assets	...	4,730	4,747	4,751	3,649	3,899	4,352	4,713	4,856	5,123
Net domestic assets	...	10,910	12,903	15,491	18,668	21,133	23,699	26,585	30,128	33,504
Net credit to govt.	...	3,051	3,776	4,306	6,193	7,628	8,760	9,096	9,556	9,784
Net credit to the economy	...	11,197	12,977	15,310	16,796	17,276	18,710	21,260	24,343	27,491
Other items, net	...	-3,338	-3,850	-4,124	-4,321	-3,771	-3,771	-3,771	-3,771	-3,771
Memorandum items										
Broad money growth	11.7	10.4	12.9	14.7	10.2	12.2	12.1	11.6	11.8	10.4
Nominal GDP growth	8.6	9.1	8.1	8.1	7.5	7.9	8.6	8.4	8.6	8.4
Velocity (% change)	-2.7	-1.2	-4.2	-5.7	-2.5	-3.8	-3.1	-2.9	-2.9	-1.8
Growth in credit to economy	14.9	26.9	15.9	18.0	9.7	12.1	11.6	13.6	12.8	13.5
Growth in credit to govt.	44.8	9.9	23.8	14.0	43.8	23.2	14.8	3.8	5.1	2.4
New credit to govt (CFAF bn)		274	725	530	1,888	1,434	1,132	336	460	228
New credit to govt (% of GDP)	1.2	0.6	1.5	1.0	3.3	2.3	1.7	0.5	0.6	0.3
Nominal GDP (CFAF bn)		46,194	49,918	53,968	57,991	62,584	67,969	73,667	79,969	86,726

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

Table 8. WAEMU: Financial Soundness Indicators 2010–16

	2010 Dec.	2011 Dec.	2012 Dec.	2013 Dec.	2014 Dec.	2015 Dec.	2016 Jun.
	(in percent, unless otherwise indicated)						
Solvency ratios[1]							
Regulatory capital to risk weighted assets	11.3	12.5	12.8	12.9	12.7	12.6	11.4
Tier I capital to risk-weighted assets	10.7	11.7	12.0	11.8	11.2	10.5	10.3
Provisions to risk-weighted assets	11.4	10.7	10.8	10.3	10.7	11.7	10.6
Capital to total assets	6.9	7.3	7.3	7.2	6.7	5.7	6.1
Composition and quality of assets							
Total loans to total assets	55.3	55.2	55.0	55.9	54.6	53.1	52.5
Concentration: loans to 5 largest borrowers	105.9	92.9	92.3	75.1	88.6	113.1	100.9
Sectoral distribution of loans							
Agriculture	2.0	2.9	2.6	2.8	3.1	3.2	2.6
Extractive industries	2.0	2.2	1.6	1.8	2.0	2.0	1.8
Manufacturing	18.9	18.8	18.2	17.0	17.9	17.2	16.7
Electricity, water and gas	3.4	3.2	3.2	3.7	3.9	4.2	4.1
Construction	6.1	6.7	6.7	7.8	8.6	9.4	10.0
Retail and wholesale trade, restaurants an	31.9	32.3	34.7	33.5	31.1	31.5	30.6
Transportation and communication	13.6	11.2	10.1	11.2	9.8	9.5	10.9
Insurance, real estate and services	5.2	5.5	6.1	5.9	6.5	6.6	7.1
Other services	17.0	17.1	16.8	16.2	17.0	16.4	16.2
Gross NPLs to total loans	17.6	15.9	16.0	15.3	14.9	14.4	15.2
Provisioning rate	63.7	64.2	63.4	61.0	62.8	62.8	63.9
Net NPLs to total loans	7.2	6.3	6.5	6.6	6.1	5.9	6.1
Net NPLs to capital	57.3	47.8	48.8	51.1	50.1	54.9	52.7
Earnings and profitability							
Average cost of borrowed funds	2.9	2.4	2.5	2.8	2.4	2.4	...
Average interest rate on loans	10.9	9.7	9.8	10.7	9.1	8.8	...
Average interest margin[2]	8.0	7.3	7.3	7.9	6.7	6.4	...
After-tax return on average assets (ROA)	1.1	1.2	0.9	0.9	1.1	1.2	...
After-tax return on average equity (ROE)	12.6	13.7	10.1	11.5	15.5	16.4	...
Noninterest expenses/net banking income	64.8	61.6	61.0	60.6	58.6	58.6	...
Salaries and wages/net banking income	27.1	26.4	25.7	26.5	25.4	25.4	...
Liquidity							
Liquid assets to total assets	33.3	33.6	32.5	32.2	30.9	29.4	27.6
Liquid assets to total deposits	45.1	46.1	45.8	47.1	45.9	43.8	41.0
Total loans to total deposits	84.0	84.3	86.2	90.0	89.5	87.0	86.4
Total deposits to total liabilities	74.1	72.9	71.1	68.5	67.3	67.1	67.3
Sight deposits to total liabilities[3]	36.7	37.8	36.5	35.5	34.5	35.4	35.2
Term deposits to total liabilities	37.5	35.1	34.6	32.9	32.8	31.7	32.1

Source: BCEAO.

[1] The indicators do not take into consideration the additional provisions required by the WAMU Banking Commission.

[2] Excluding tax on bank operations.

[3] Including saving accounts.

Table 9. WAEMU: Risk Assessment Matrix[1]

	Source of Risk	Relative Likelihood	Potential Impact
	Spillover Risks		
Short-ST to MT Term (ST)	**Significant further strengthening of the US dollar and/or higher rates.**	High	**Low to medium.** The region's exposure to global financial markets remains limited, but increased financing costs could adversely affect the region through higher regional risk premium and WAEMU countries which plan to tap international financial markets. Stronger US dollar could increase sovereign debt burden of countries with un-hedged dollar exposures and increase costs of certain imports. On the upside, stronger USD could increase export receipts of certain exports (e.g., cocoa, oil)
	Retreat from cross-border integration.	High	Medium **to high.** The realization of this risk, particularly in Europe, could lower foreign aid, trade, and foreign investment in the region.
ST to MT Short Term	**Weaker-than-expected global growth:**		**Medium to high**. Sharper-than-expected downturn in China could significantly lower trade, investment, aid, and tourism flows and affect WAEMU region trough cross-border spillover effects from the Euro area and SSA emerging markets.
ST	**Significant slowdown in other large EMs/frontier economies.**	Medium	
	Significant China slowdown and its spillover.	Low /Medium	**Medium.** Slower growth in advanced markets, in particular Europe, could lower trade, remittances, foreign aid and FDI. Slower growth in and subsequently lower demand for commodities by emerging markets could dampen commodity prices and thus exports in some countries (e.g. gold, cocoa); a positive impact is expected for the region's current account deficit if mainly oil prices are affected.
MT	**Structurally weak growth in key advanced and emerging economies.**	High/ Medium	
ST	**Heightened risk of fragmentation/security dislocation in part of the Middle East, Africa, and Europe**, leading to a sharp rise in migrant flows, with negative global spillovers.	High	**Medium to high.** With the exception of Niger, all WAEMU countries are net oil importers. An increase in oil prices would deteriorate the current account balance and negatively impact growth through an increase in production costs.
	Regional Risks		
ST	Political and security risks, including regional spillovers.	Medium	**High.** Security risks in the Sahel remain. Stability could be tested within the context of elections in several WAEMU countries. Risks include a destruction of (human) capital, negative effects on growth and inclusiveness, delays in reforms, and increased fiscal cost and liquidity risks for the affected sovereign.
MT	Delay in reforms at country and regional level related to (i) fiscal consolidation (ii) infrastructure investment, (iii) the energy sector, (iii) PFM, (iv) the financial sector and (iv) regional integration.	Medium	**Medium to high.** Fiscal consolidation and key reforms will require strong political will. Weak implementation capacity and bureaucratic hurdles pose risks to efficient reform implementation. With many countries targeting large infrastructure investments, a delay in PFM reforms and inefficient investment could give rise to debt, fiscal and external sustainability issues, with negative implications for growth and poverty reduction. Delays in supervisory reforms may pose financial stability risks.
ST	Adverse weather conditions.	Medium	**High.** Lower agricultural production could imply heightened food security risks, a decline in growth rates, and additional fiscal costs.
MT	Exchange rate pressure in the CEMAC.	Low/ Medium	**High. High.** Given similarities between the two zones (e.g., CFAF peg agreement, economic and policy challenges) pressure on the XAF could have spillover effects on the XOF

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Table 10. WAEMU: Authorities' Responses to 2016 Policy Recommendations
(Scale: fully consistent, broadly consistent, partially consistent, and inconsistent)

	2016 Article IV Recommendations	Authorities' Response
Policy Mix	- Macroeconomic conditions do not warrant a tightening of monetary policy at this juncture. -	**Broadly consistent** - Bank refinancing has somewhat slowed down. Risks remain.
Fiscal Policy Coordination	- Governments need to adhere to their budget deficit reduction plans while maintaining public investment efforts, which will require increasing tax revenue and improving quality of spending.	**Partially consistent** - Planned fiscal consolidation has been deferred in many countries
Monetary/ Financial sector Development	- Enhance monetary policy effectiveness Continue financial sector reforms - Accelerate the development of the interbank and government debt markets.	**Partially consistent** - The regional debt agency is coordinating bond issuance but the regional market remains underdeveloped - Reforms to debt and interbank market still ongoing.
Financial Regulation and Supervision	- Speed up financial sector reform and implementation of Base II/III - Strengthen risk based supervision, avoid regulatory forbearance	**Partially consistent** - Significant progress has been achieved in the implementation of Basel II/III - Compliance to key prudential ratios remains weak. - Many prudential limits remain lax. - Reforms on enhancing resolution frameworks are slow. -
Growth/ Regional Integration	- Further improve the quality of public infrastructure and ease constraints on the business environment.	**Partially consistent** Some WAEMU countries (Niger, Guinea-Bissau, and Mali) have kept the pace of reforms and made progress in areas such as starting a business, investment protection, contract enforcement, and insolvency resolutions but overall progress is slow. The 2017 World Bank's Report indicates that the regional Doing Business climate has improved less than last year and much less than in other African and Asian regions.

Table 11. WAEMU: Selected Policy Recommendations for Member States

	Fiscal and Debt Policies	Financial Sector and Structural Reforms
BEN	- Boost domestic revenue, mainly through better tax administration. - Pursue prudent borrowing policy and strengthen public debt management to preserve debt sustainability.	- Improve PFM and government capacity to support efficient spending. - Improve the business environment, foster financial deepening, and strengthen bank supervision and resolution.
BFA	- Improve coherence of budget planning and execution. Improve debt and cash management. - Attend to pace and quality of public investment spending.	- Boost energy supply; reform income support schemes in the cotton sector. - Implement a more systematic approach to transfer schemes to protect the vulnerable.
CIV	- Build fiscal buffers, particularly through improving tax policy administration and new tax policy measures. - Strengthen surveillance of fiscal risks stemming from public enterprises. - Strengthen public financial and debt management, and pursue prudent borrowing policy to avoid an excessive bunching of maturities in the mid-2020s.	Implement the financial sector reform, including recapitalization and restructuring of public banks. Undertake further reforms to improve the business climate and encourage private investment, and strengthen national statistics.
GNB	- Advance PFM reforms, particularly in budget execution and better Treasury management. - Enhance revenue by expanding the tax base and strengthening tax administration, implementing the measures agreed under the ECF program.	- Commence audit of state-owned enterprises and autonomous funds according to the plan and schedule prepared under the ECF program, - Design a strategy to promote cashew production and transformation based on results of the FUNPI audit.
MLI	- Mobilize more tax revenue by broadening the tax base and reducing tax exemptions; improve quality of spending. - Implement fiscal decentralization plans (gradually). -Keep the basic fiscal balance close to zero and the overall fiscal balance in line with overall public debt sustainability.	- Reduce NPLs by accelerating clean-up of commercial banks' balance sheets; strengthening the balance sheet of the new bank resulting from the merger of the BHM with BMS; clean up the microfinance sector. -Improve the business environment; improve public infrastructure and education; lighten the labor tax load; tackle corruption.
NER	- Maintain fiscal sustainability by broadening the tax base, prioritizing public spending, and improving expenditure control, while anchoring investments in a multiyear plan - Implement a prudent debt policy, using concessional resources and focusing on high return projects.	- Strengthen long-term resilience to weather-related shocks by enhancing food security and Trade. - Promote economic diversification and create jobs for Niger's fast growing population by improving the business climate and financial access, while scaling-up investment on key infrastructure.
SEN	- Anchor fiscal policy on an agreed debt path, with corrective action mandated in case of deviations. - Control public consumption and implement revenue reforms to create space for PSE projects and achieve WAEMU deficit target.	- Implement reforms to improve the business environment and increase incentives to extend credit to the private sector, including to SMEs. - Develop and implement an action plan to strengthen Treasury operations.
TGO	- Reduce the overall fiscal deficit to ensure long-term debt and external sustainability; - - Strengthen debt management and undertake investment projects that are fully integrated in all phases of the budget process.	- Enforce the regulatory framework in the financial sector, solve problem banks, and strengthen supervision in the microfinance sector. -Further modernize revenue administration, improve public financial management, public investment management, open key economic sectors to private sector competition, and further improve the business environment.

Annex I. WAEMU: External Stability Assessment and Competitiveness

- The WAEMU current account deficit is estimated to have widened in 2016 by about 0.3 percentage point of GDP compared to 2015, reflecting mainly continuous public investment scaling-up in most countries and less favorable terms-of-trade. FDI and capital transfers—the main source of external financing—have partially offset lower portfolio and other investment inflows. Reserves coverage has deteriorated to 3.7 months of imports. Even though, official reserves appear adequate according to the zone's monetary arrangement with France, in light of the significant downside risks to the outlook, there will be benefits to building additional reserves. EBA-based analyses suggest that WAEMU external position is broadly consistent with regional medium-term fundamentals and desirable policy settings. Survey-based indicators of structural competitiveness show improvement, but there is significant room for progress.

- **Current account development.** The regional current account deficit (including grants) is estimated at 6.1 percent of GDP in 2016, about 0.3 percentage point of GDP more than last year, reflecting continued public investment efforts and less favorable terms-of-trade. The trade and service deficit increased by 0.7 percentage point to 9.6 percent of GDP, reflecting a decline in exports of goods—especially cocoa and uranium—and an increase in imports of specialized services. Current official transfers are estimated to have increased by 0.4 percentage point to 2.7 percent of GDP in 2016 compensating for slightly lower private transfers (e.g., dividend payments). The current account deficit is expected to gradually decline to 5.3 percent of GDP by 2021, assuming fiscal consolidation and improved external competitiveness.

- **External financing.** Capital transfers remained stable at about 2 percent of GDP. FDI is estimated to have increased from 2 to 2.7 percent of GDP. At the same time, portfolio and other investments (mainly official loans) are expected to decline by 0.5 and 3.4 percentage point of GDP, respectively. In the medium term, FDI would increase to 3.5 percent of GDP term while capital transfers would stabilize at their 2016 level. WAEMU external debt is expected to decline progressively to about 35 percent of GDP in 2021.

- **Reserves adequacy**. Regional gross international reserves have declined from CFAF 7487 billion (US$12.4 billion) at end-2015 to CFAF 6498 billion (US$10.8 billion) at end-2016, equivalent to 3.7 months of extra-regional imports, 55 percent of narrow money, and 74 percent of short-term debt. The current and projected medium-term reserve cover is above the thresholds required by the zone's monetary arrangement with France.[1] However, reserve cover would remain below the optimal buffer against external shocks, Following

[1] The arrangement with France provides an operation account on which the BCEAO can draw in case of reserve shortage – a mechanism akin to an overdraft possibility. However, in exchange of the French guaranteeing of the CFA Franc peg to the Euro, BCEAO countries must hold 50 percent of their exchange reserves at the French Treasury, and 20 percent of the BCEAO liabilities must be covered by foreign reserves.

Dabla-Norris et al. (2011), the "optimal" level of reserves is determined by maximizing their net benefits which depend on (i) the expected cost of a crisis given the stock of reserves, (ii) a vector of fundamentals (exchange rate regime, fiscal balance, institutions), (iii) the exposure to shocks (terms of trade, external demand, FDI, aid), and (iv) the cost of holding reserves (interest rate differential with the rest of the world). The approach suggests an optimal range of reserves between 5-12 months of imports for the WAEMU depending on the interest rate differential with the rest of the world. This result implies that international reserves in the WAEMU should increase to provide higher buffers against typical shocks. With a prolonged slowdown in global growth and regional terms of trade, regional reserves could decline up to 1.5 months of imports.

- **Assessment of external position.** The REER is estimated to have depreciated marginally by 0.4 percent while the NEER appreciated by about 2 percent compared to last year. "EBA-lite" does not indicate significant misalignments of the current account or the real effective exchange rate compared to regional fundamentals adjusted by a policy gap (the region's policies relative to an optimal level and to the rest of the world). The results suggest the current account gap varies between -0.4 to -0.7 percent and the real effective exchange rate overvaluation ranges between 0.9 percent and 1.7 percent (which is within margins of error) and slightly less than last year. The largest contributor to the CA norm is lagged productivity and demographics while fiscal policy and change in reserves are the largest contributor to the policy gap.

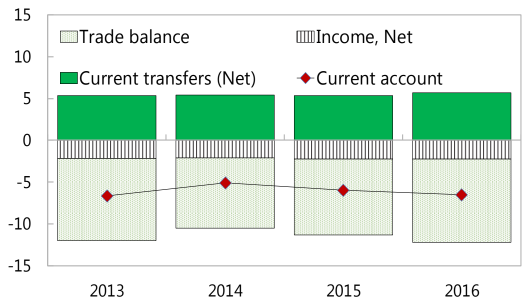
- **Competitiveness.** Competitiveness remains weak, and progress is slow. The 2017 World Bank's Report indicates that the regional Doing Business climate has improved less than last year and much less than in other African and Asian regions. However, some WAEMU countries (Niger, Guinea-Bissau, and Mali) have kept the pace of reforms and made progress in areas such as starting a business, investment protection, contract enforcement, and insolvency resolutions. Fostering regional integration and adopting a regional approach to bridging the infrastructure gap would also help improve competitiveness.

Annex I, Figure 1. WAEMU: Recent Developments

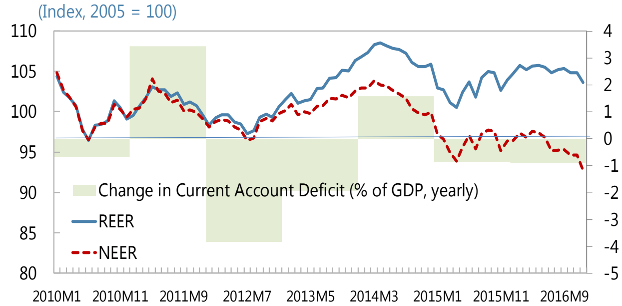
The current account and trade deficits have deteriorated in 2016…

…with less favorable terms of trade…

1.Current Account Balance
(in Percent of GDP)



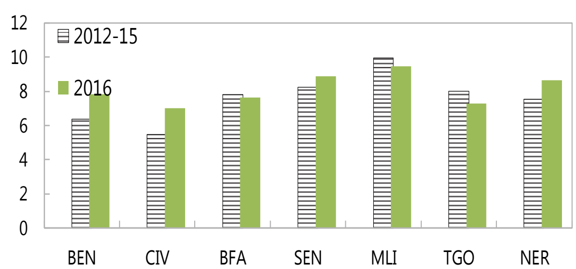
2. Real and Nominal Effective Exchange Rates
(Index, 2005 = 100)



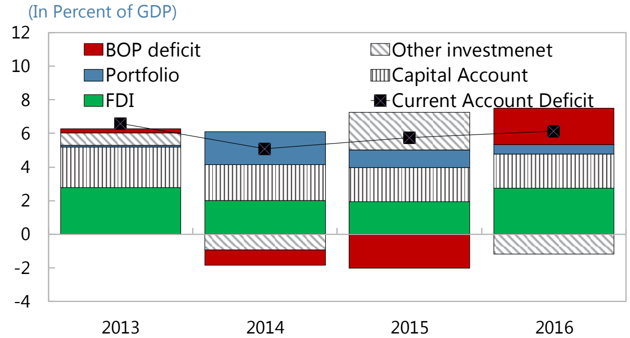
…reflecting steadfast capital goods imports in most countries….

Higher FDI has partially compensated for lower portfolio and other investment.

3. Capital Imports
(In Percent of GDP)



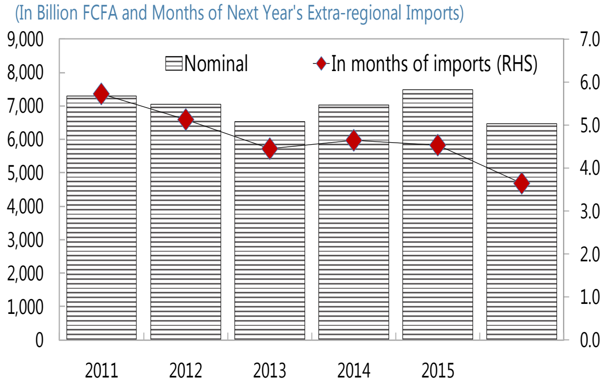
4.Financing Sources
(In Percent of GDP)



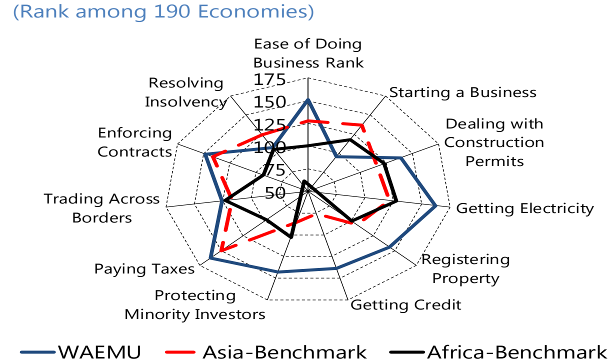
Consequently, official reserve coverage has decreased below 4 months of imports.

Structural reforms continue but at a slower pace.

5.Gross International Reserves
(In Billion FCFA and Months of Next Year's Extra-regional Imports)



6. Ease of Doing Business 2017
(Rank among 190 Economies)



Source: World Bank, Doing Business 2017

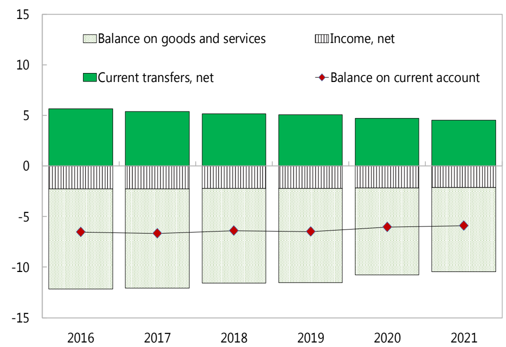
Sources: BCEAO; and IMF staff calculation.

Annex I, Figure 2. WAEMU: Outlook

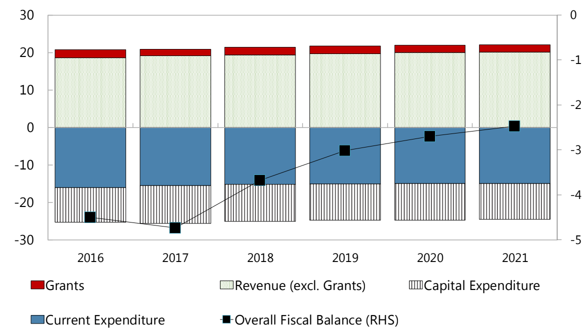
The current account deficit is expected to stabilize over the medium term…

if fiscal consolidation efforts materialize…

1. Current Account Balance
(in percent of GDP)



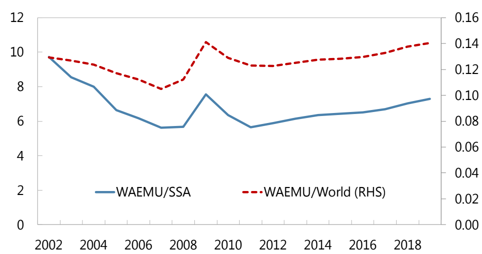
2. Overall Fiscal Balance (Cash Basis) and Components
(in percent of GDP)



…while reform efforts would improve competitiveness and…

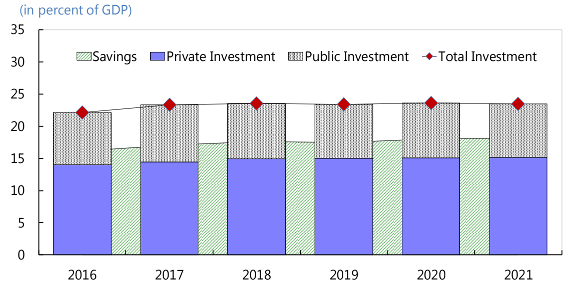
…and domestic savings would finance investment.

3. Exports of Goods and Services
(in percent of SSA and World Exports)



Sources: World Economic Outlook

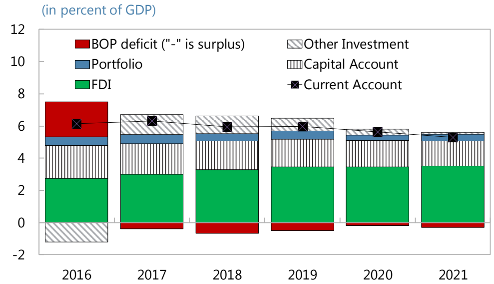
4. National Savings and Investment
(in percent of GDP)



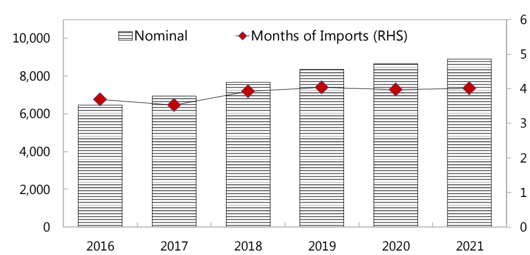
Financial inflows are expected to balance the BOP by the end of the projection period…

…while reserve coverage would increase to about 4 months of imports.

5. Financing Sources
(in percent of GDP)



6.Gross International Reserves
(In Billion FCFA and Months of Next Year's Imports))



Sources: BCEAO; and IMF staff calculation.

Annex II. Anchoring Debt Accumulation in the WAEMU[1]

This note applies elements of the Fund-Bank debt sustainability framework to analyze the risks of debt distress in the WAEMU. The results suggest substantial vulnerabilities to shocks that point to moderate risks of debt distress for the region.[2] *Member countries need to increase fiscal and external buffers and improve their debt management policy and framework to ensure debt sustainability and macroeconomic stability.*

1. Public debt has risen. The average public debt ratio has increased from 36.5 percent of GDP in 2012 to 45.5 percent of GDP in 2016, reflecting predominantly public investment scaling up. External debt still accounts for the vast majority of public debt but its composition has changed with a significant substitution between concessional and commercial borrowing. Commercial debt increased from 8 percent of total external public debt in 2011 to 16 percent in 2016. At the same time, the share of Non-Paris club creditors in total external debt grew from 2 percent in 2011 to about 22 percent in 2016. These changes coupled with the drop in the share of traditional multinationals creditors resulted in a decline in grant element for the region.

A. External and Public Debt Vulnerabilities in the WAEMU

2. Elements of the Fund-Bank debt sustainability framework (DSF) can be used to monitor the external and domestic debt development and risks of debt distress for the region. The DSF takes into account the regional indebtedness, repayment capacities, policy and institutional capacity, macroeconomic shocks, and heterogeneity of WAEMU countries to determine the risk of debt distress in the region and individual countries (Box 1). The analysis, using end-2015 data, indicates a moderate risk of debt distress for the region.

3. WAEMU regional external debt remains sensitive to external and domestic shocks (Figure 2). All five debt indicators (in present value—PV) remain below the policy-dependent thresholds under the baseline scenario. The stress test scenarios show, however, that external debt remains vulnerable to shocks.[3] In particular, in the extreme stress scenario with export growth falling temporarily by one standard deviation below its historical average, all indicators of debt distress increase significantly with two breaching the thresholds. Also, all debt indicators increase significantly following a combined GDP growth and external financing shock with two of

[1] Prepared by Edna Mensah, Boriana Yontcheva, and Aleksandra Zdzienicka with input from Jose Gijon, Jean van Houtte, and WAEMU teams.

[2] This aggregation exercise of WAEMU countries' DSA is an analytical exercise, not a formal World Bank/IMF sanctioned DSA.

[3] In the baseline scenario, real GDP growth is projected to average around 5.5 percent over long term, annual inflation measured by GDP deflator is expected to remain at around 2 percent, real primary spending will increase at above 5 percent and domestic and FX effective interest rates is projected at above 3 and 2 percent, respectively. The grant element of new FX borrowing will remain at 20 percent.

them breaching the threshold.[4] Other shock simulations—including, for instance, tighten financial conditions—lead to similar results confirming the conclusions of the most recent individual WAEMU countries DSAs on the moderate risk of debt distress facing by the Union.[5]

4. Public domestic debt breaches the policy-dependent threshold under all stress test scenarios (Figure 3). The PV of domestic debt-to-GDP ratio remains stable under the baseline scenario. However, the stress test scenarios show high vulnerability to growth shocks (i.e., when GDP growth is temporary lower by one standard deviation compared to the historical average). The simulations also suggest that under an unchanged fiscal policy stance (with the primary fiscal balance remaining at the 2015 level), the PV of domestic debt steadily increases over the medium term reaching the debt thresholds. The results of this *historical* scenario are similar to a combined large shock when both GDP growth and the primary fiscal balance decline temporarily by a half standard deviation compared to the baseline. Domestic debt indicates similar sensitivity using a WAEMU-specific threshold (Box 1).

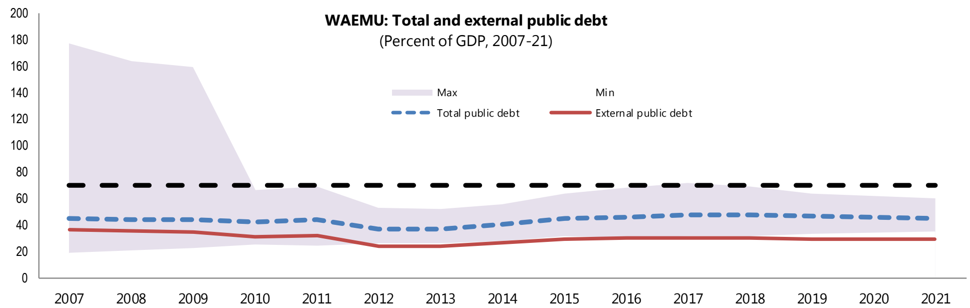
5. Some differences can be noticed with public domestic debt dynamics at an individual country level (Figure 4). The PV of domestic debt-to-GDP ratio breaches the debt thresholds in Togo, Cote d'Ivoire, and, temporarily, in Guinea-Bissau, but remains below the threshold for other countries. The risk of debt distress is significantly higher for Togo, Côte d'Ivoire, Niger, and Benin as the PV of debt-to-GDP ratio breaches substantially the debt threshold in at least two stress test scenarios.

[4] This shock simulates the impact of a permanently lower by 0.5 standard deviation growth and non-debt creating inflows.

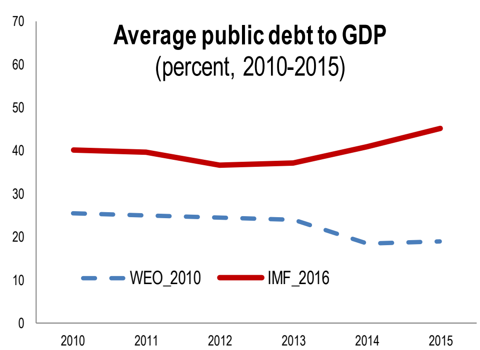
[5] The recent individual DSA indicate a moderate risk of debt distress for all WAEMU countries.

Annex II. Figure 1. WAEMU: Regional Debt Profile

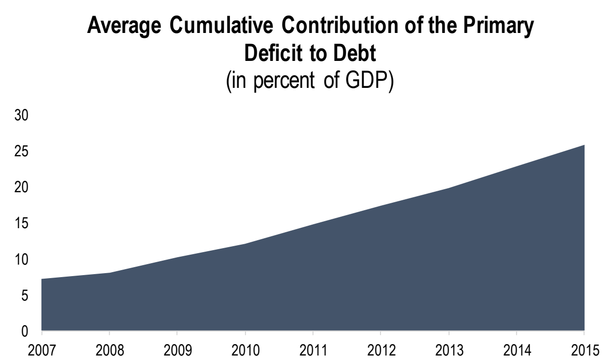
The average regional debt remains stable below 70-percent threshold but debt ratios have been increasing in individual countries…



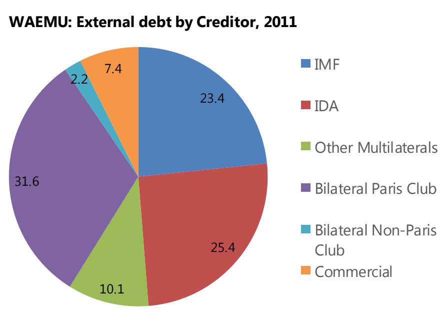
beyond expectations…



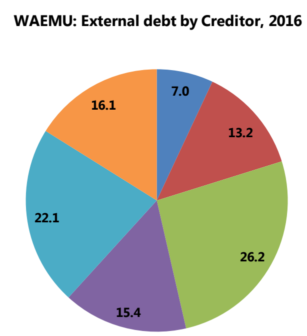
reflecting new borrowing largely to finance public investment …



The composition of the external debt has changed as …



commercial debt and debt to non-Paris Club creditors has increased



Sources: BECAO; WEO, IMF Staff estimations.

Annex II, Box 1. Elements of Debt Sustainability Framework (DSF)

The 2012 DSF methodology estimated a probit model of debt distress following the approach developed by Kraay and Nehru (2004) and IMF (2004). In particular, the following model is estimated:

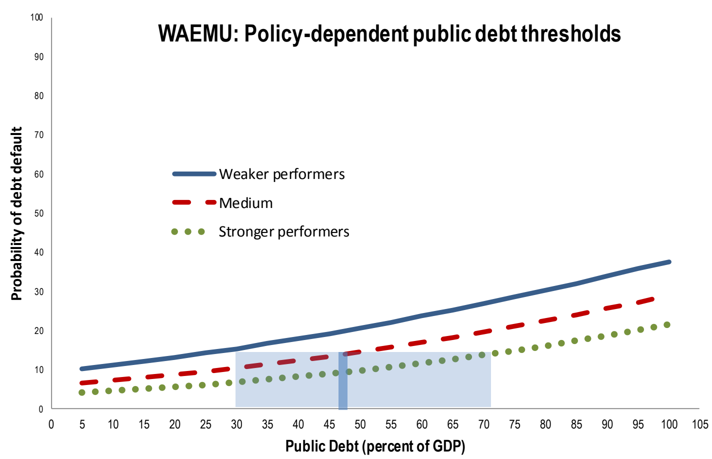
$$P(debt\ distress_t) = \Phi\,(\beta_1 debt\ burden_{t-1} + \beta_2 governance_{t-1} + \beta_3 shock_{t-1} + \beta_4 other_{t-1}) \quad (1),$$

where *debt distress* takes value of 1 if the country experiences a debt crisis and 0 otherwise. *Debt burden* measures a country's indebtedness before the crisis, governance captures the quality of policy and institutions, *shock* denotes real GDP growth, and *others* is a set of controls including several country features such as the level of income per capita.

The following events are used to characterize debt crises: (i) public and public guaranteed (PPG) external arrears are higher than 5 percent of external debt, (ii) debt is rescheduled, (iii) IMF GRA financing exceeds 50 percent of the quota or (iv) the sovereign failed to meet principal or interest pavement on the due date.

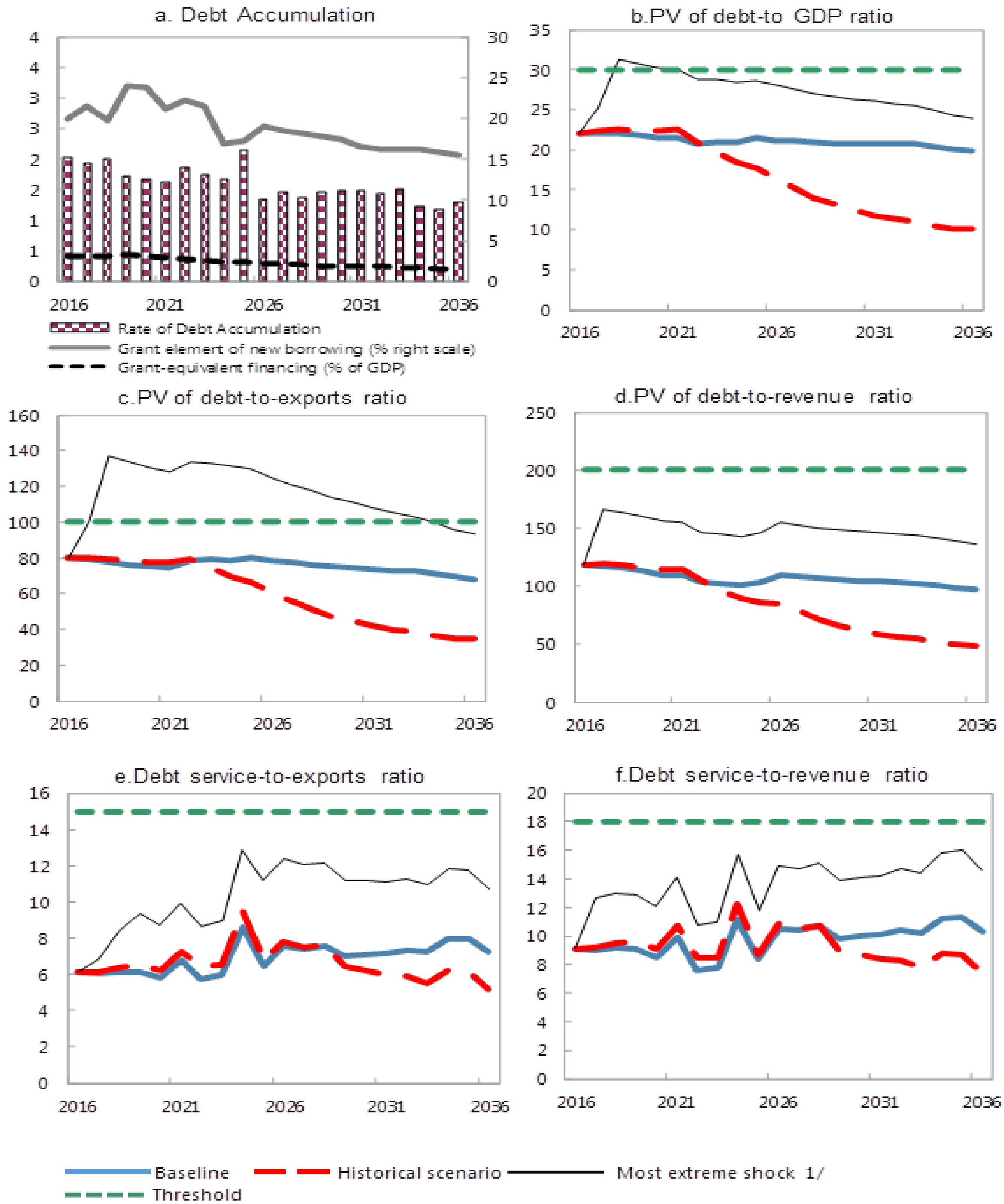
An indicative debt burden threshold is then calibrated by fixing the values for the probability of debt distress, governance, and macroeconomic shocks. Three methods are used to determine the default probability: (i) the medium debt burden indicator, (ii) unconditional probability, and (iii) the noise-to-signal ratio. The DSF probability of the debt distress varies from 12 to 15 percent.

As an illustration how the DSF could be applied, debt burden thresholds are computed for the WAEMU as the average unconditional probability of debt distress for low and lower-middle income countries a year before the debt crisis occurrence and are a function of policy and institutional capacities of the country. The resulting debt burden threshold for WAEMU region—assuming average 5 percent economic growth—varies between about 30 and 70 percent. For the average macro-financial intuitional capacities of WAEMU countries, the regional debt burden threshold is around 45 percent. [1]



[1] To identity the debt crises, the note relies on several databases: (i) Laeven and Valencia (2008) that includes sovereign default to private sector and debt rescheduling; (ii) Reinhart et al. (2003) that includes data on default and restructuring and Standard and Poor's Credit Week information. Additionally, episodes of debt default are also identified when the areas on principals on external obligations exceeds 15 percent of the total debt.

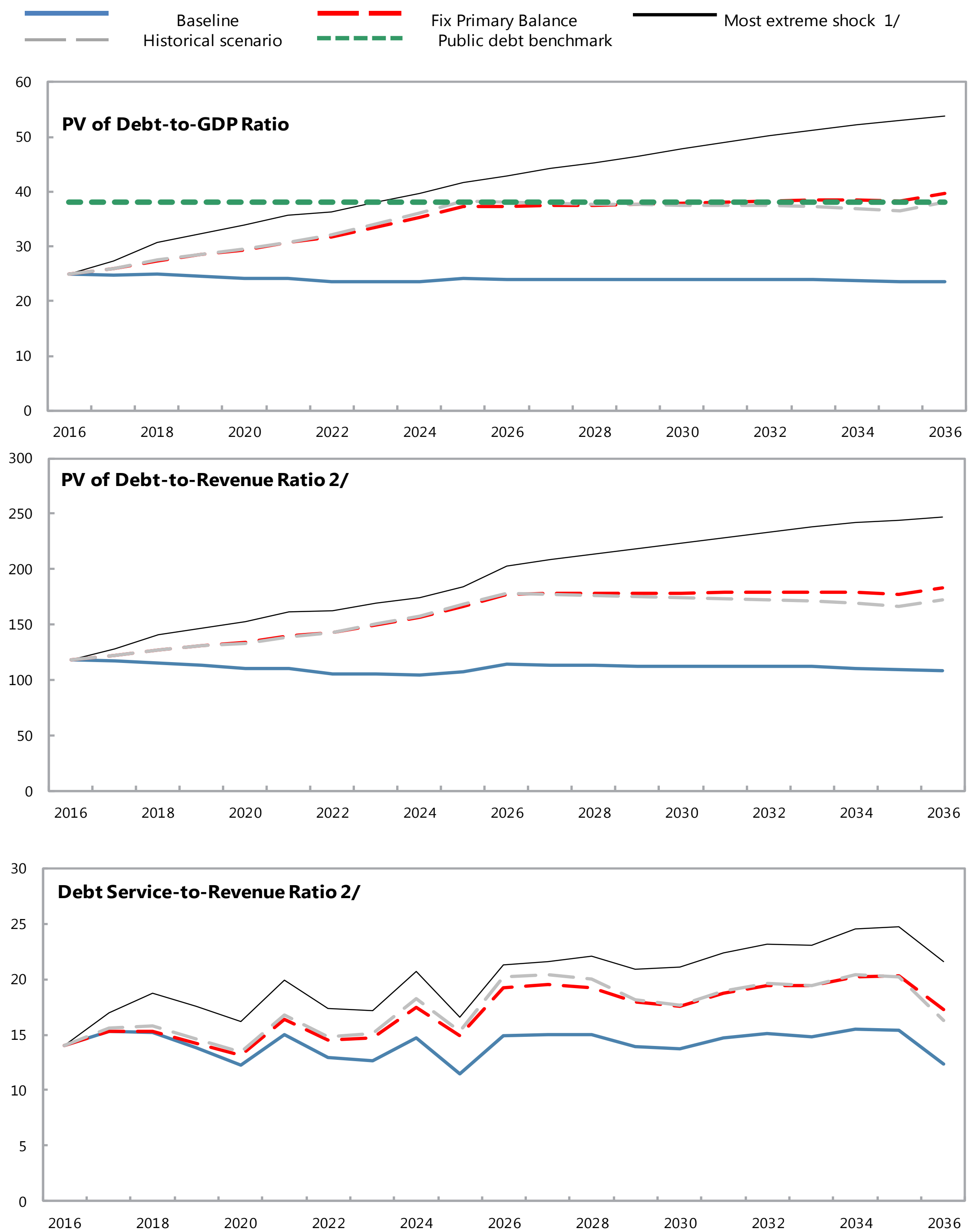
Annex II, Figure 2. WAEMU: Indicators of Public- and Publicly-Guaranteed External Debt Under Alternative Scenarios, 2016-36[1]



Sources: Country authorities; and staff estimates and projections.

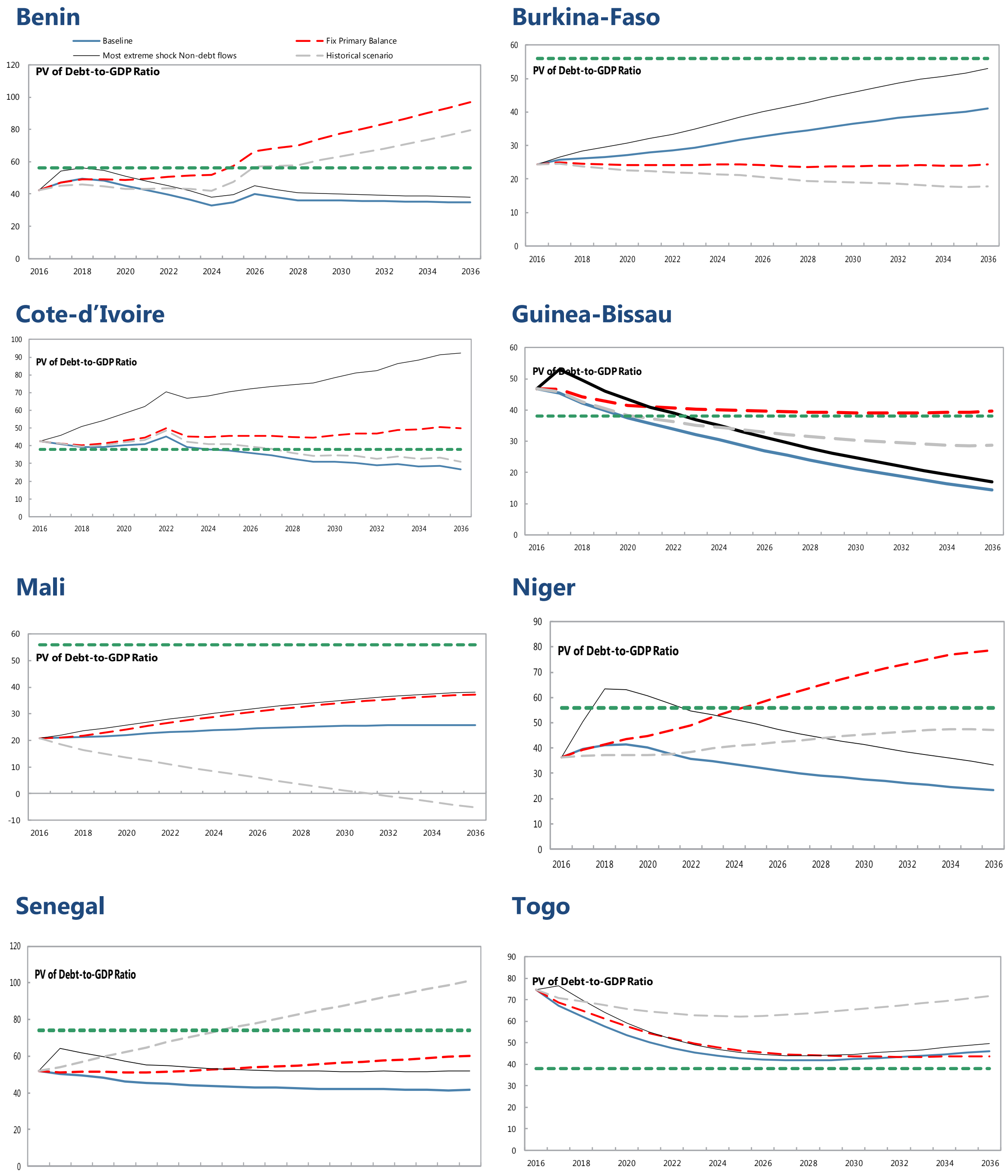
[1]/ The most extreme stress test is the test that yields the highest ratio on or before 2026. In figure b. it corresponds to a Combination shock; in c. to a Exports shock; in d. to a One-time depreciation shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

Annex II, Figure 3. WAEMU: Indicators of Public Debt Under Alternative Scenarios, 2016-36[1]



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2026.
2/ Revenues are defined inclusive of grants.

Annex II, Figure 4. WAEMU Countries: PV of Public Debt -to-GDP Under Different Scenarios (2016-36)



Annex III. Monetary Policy, Market Segmentation and Refinancing in the WAEMU[1,2]

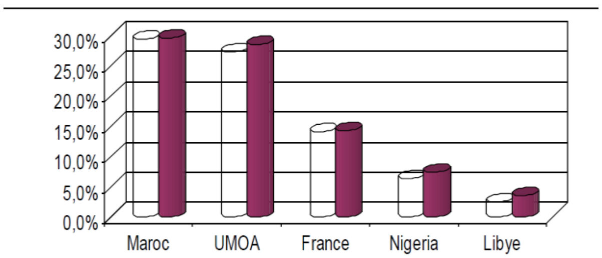
This note examines the functioning of the interbank market and assesses the determinants of the demand for BCEAO refinancing. The banking system mainly comprises a few large international banks, pan-African groups, and small local banks. The interbank market is shallow and highly segmented. A degree of skepticism is commonplace concerning the credit quality of peer institutions, proving a hindrance to the unsecured market while the illiquid nature of debt markets obstructs the development of a secured repo market. The large international banks hold most excess liquidity but do not participate in the interbank market. The small, and mostly regional banks, are liquidity-constrained and rely predominantly on BCEAO's refinancing, including to build up their portfolios of government securities.

A. Characteristics of the banking sector

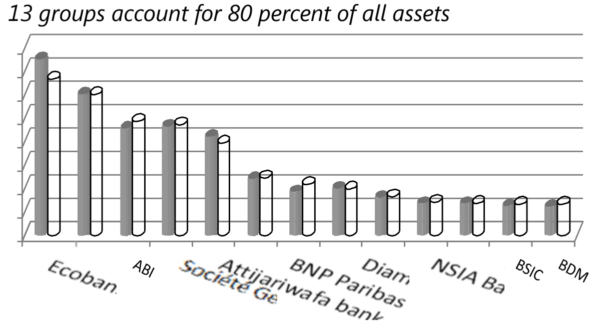
1. The WAEMU banking system is heterogeneous and segmented. The banking system comprises 102 banks, including 28 banking groups. The 13 larger banking groups accounted together for 80 percent of the total bank assets in June 2016[3]. WAEMU-based banking institutions make up 28 percent of total assets[4] while Moroccan banks dominate among foreign-based institutions with about 30 % of total bank assets followed by French banks (13 percent). Banks are very heterogeneous with regard to business models, size, geographical coverage, and

Banking Groups' Share of Total Assets (percentage)

Foreign commercial banks dominate the sector …



13 groups account for 80 percent of all assets



Source: BCEAO.

[1] Prepared by Romain Veyrune, Rachid Awad, Shaoyu Guo, (all MCM), Boileau Loko and Boriana Yontcheva (all AFR).

[2] This note draws upon an MCM technical assistance mission report on improving the liquidity management framework (mission led by Romain Veyrune January 13-20, 2017).

[3] Ecobank, Bank Of Africa (BOA/BMCE), Atlantic Business International (ABI/BCP), Société Générale, Attijariwafa bank, BNP Paribas, Diamond Bank, Oragroup, Coris Bank International (CBI), NSIA Banque Côte d'Ivoire, United Bank for Africa (UBA), BSIC and BDM.

[4] Ecobank alone makes up for about 15 percent of total assets.

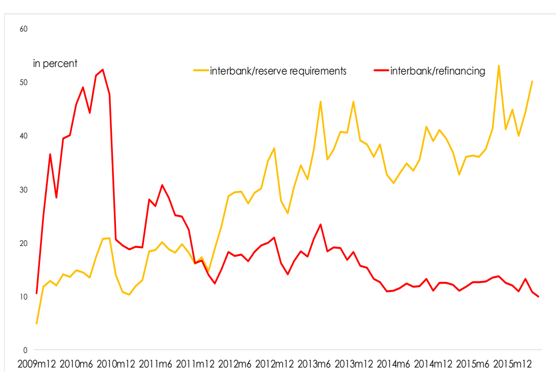
profitability. Banks are predominantly geared towards large enterprises and banking is conducted within national borders. Cross-border flows to corporations within the region are largely in the form of syndicated loans involving a sister bank located in the country of the client.

2. **Conditions in the banking sector remain challenging**. Credit and concentration risks are important and the ratio of gross NPLs to total loans is still relatively high at 15.6 percent at end September 2016. In addition, around 40 percent of banks are in violation of the relatively soft single large exposure limit at the same period. Four banks (mainly state-owned) are under temporary administration and 14 banks remain under closer supervisory scrutiny, accounting for around 16.1 percent of the banking sector assets at end-June 2016. Resolution of troubled banks is often delayed and challenged in part due to the shared powers with national authorities. A new deposit insurance fund (FGD) was established but major milestones remain to be completed before it becomes operational. Authorities are working on establishing a regional resolution framework comprising a resolution authority and a regional resolution fund.

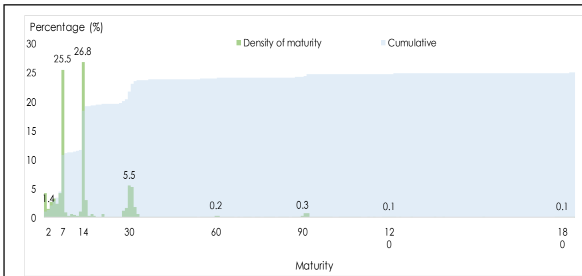
B. Small and segmented interbank market

3. **The WAEMU interbank market is small and mainly unsecured.** Interbank loans represented about 2.5 percent of bank deposits between 2009 and 2015 (figure below) and banks' funding mainly relies on client deposits. Interbank outstanding debt has increased and reached about 50 percent of the banks' reserve requirements at-end 2015. The most frequently traded maturities are 7 days and 14 days which seem to confirm that interbank loans are related to the reserve requirements. The WAEMU interbank market is mainly unsecured. From 2010 to 2016, about 93 percent of the lending in the interbank market was done without any form of collateral.

WAEMU: Interbank Market Size



Distribution of Interbank Market Lending Maturities



Source: BCEAO

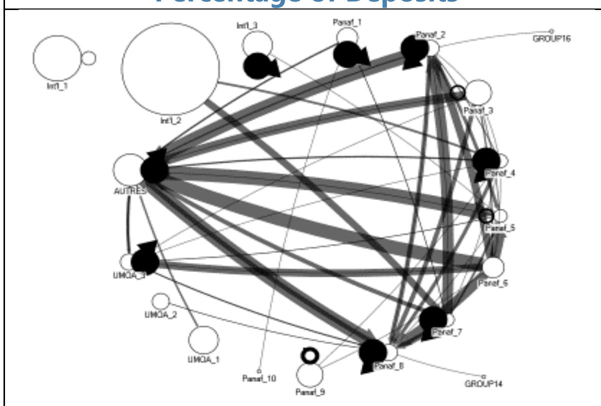
Source: BCEAO.

4. **The market is very segmented.** Most interbank transactions occur intragroup and banks with the largest excess reserves limit their participation. Intra-group transactions represent about 80 percent of interbank market transactions. Banks with large excess reserves are in general,

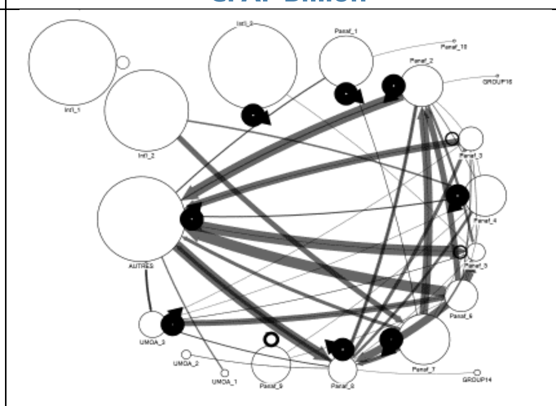
though not exclusively, the subsidiaries of large international banks and are reluctant to lend to other banks. As a result, international banks do not recycle their excess liquidity in the market or recycle only within the group. The figure below illustrates interbank flows. We split WAEMU banks into groups according to their ownership: Nine Pan-African groups, three international (mostly European) groups, three WAEMU groups, and a residual category, which includes local banks. 5 groups generate 75% of all interbank transactions and most of those transactions happen within the group. In half of the 16 groups intra-group transactions exceeded significantly intergroup transactions.

5. Pan African and local banks are more active in the interbank market. The number of credit lines, which are reflected in two-way transactions, is higher between different Pan-African groups and between Pan-African groups and local banks. The higher level of inter-group transactions indicates a better distribution of reserves in this segment of the market. Only the most active groups in the unsecured market and local banks also participate in the secured market. Groups with high excess liquidity, with limited participation in the unsecured market, do not participate more in the secured segment of the market.

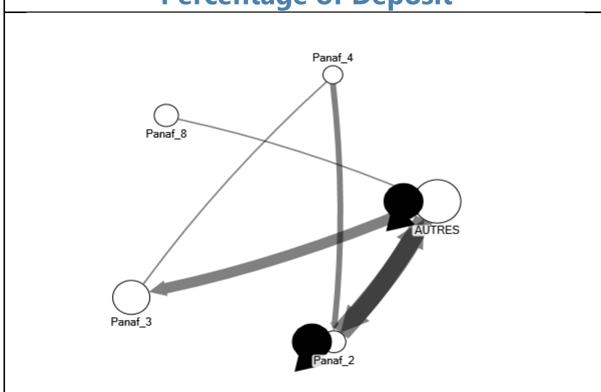
Unsecured Interbank Group Network as a Percentage of Deposits



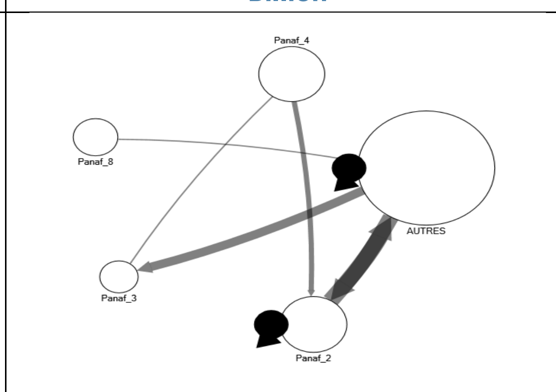
Unsecured Interbank Group Network in CFAF Billion



Secured Interbank Group Network as a Percentage of Deposit



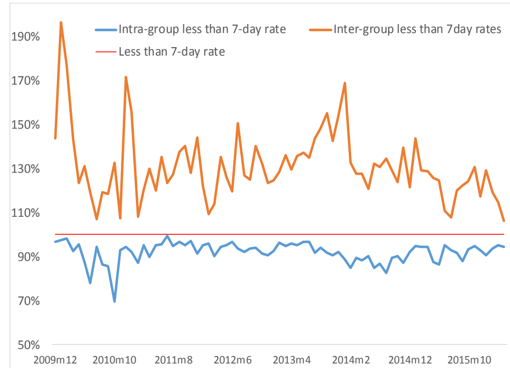
Secured Interbank Group Network in CFAF Billion



Source: BCEAO.
Note: the size of nodes represent excess liquidty in each segment. The arrows represent interbank transactions. INT represents international banking groups, Panaf represent pan-African banks, UEMAO represents WAEMU based banks, "autres" represents a residual category with mostly small local banks.

6. The inter versus intra-group segmentation results in noticeable pricing differences. Unsecured inter-group transactions are consistently priced noticeably above the same type of intra-group transactions.

Inter and Intra Group Short-Term Interest Rates



Source: BCEAO.

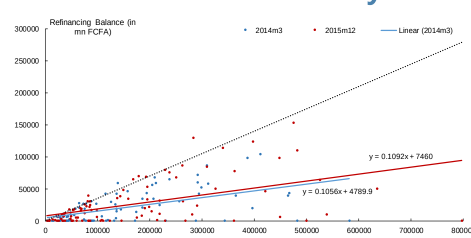
7. Most interbank transactions in the WAEMU occur cross-border. Cross-border transactions between the eight WAEMU member countries represent 85 percent of interbank transactions. This finding mirrors the fact that interbank transactions happen mainly intra-group, who normally have one subsidiary per country. Excess reserves are evenly distributed among member countries, generally as a percentage of banks' deposits. Unsecured intra-country transactions are consistently priced above the same type of cross-border transactions as the latter mainly consist of inter-group transactions.

C. Monetary Policy Operations and Demand for refinancing

Monetary Policy Operations

8. The BCEAO has two types of open market operations. The BCEAO provides refinancing for seven days and 28 days respectively each week and each month to financial institutions subject to the reserve requirement (mainly banks). The refinancing is allocated at variable rates and the minimum bid rate of the 7-day operation is the BCEAO's policy rate. This minimum bid rate also applies to the 28-day refinancing tender. There is a maximum bid amount set such as banks cannot receive refinancing for more than 35 percent of their credit to the private sector and government securities, which is binding for 110 counterparties (Figure 3).

Refinancing, Loan, and Government Security

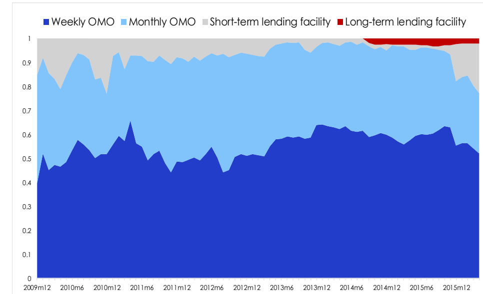


Source: BCEAO.

9. The BCEAO also operates two types of standing lending facilities. The first type provides refinancing at the demand of the banks from one to seven days. The second facility provides refinancing for 90 to 360 days against government securities and credit claims with maturities ranging from 5 to 20 years at the demand of the banks. The facilities currently are priced 200 basis points above the policy rate. Starting in June 2017, recourse to the lending facility will be capped at twice the counterparty's capital.

10. The recourse to the lending facility represent the portion of demand not satisfied at the open market operations. The recourse to the lending facility increased since December 2015 as the unmet refinancing needs at the BCEAO operations were satisfied by the short-term lending facility rather than in the interbank market. According to discussions with market participants, the spread of 100 basis points between the minimum bid rate at the refinancing operations and the lending facility was too narrow to promote interbank transactions.

Composition of the BCEAO Refinancing by Maintenance Period

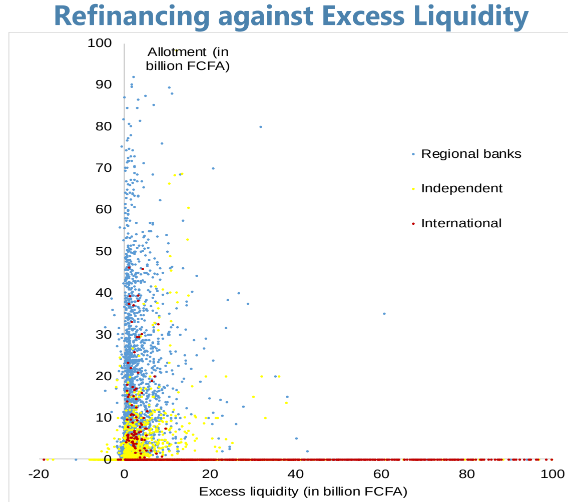


11. In 2016, the lending facility became akin to a refinancing operation, rather than an exceptional liquidity backstop. Since limits were imposed on the open market operations in December 2015, banks had relied extensively on the lending facility in 2016. In December 2016, the Central bank increased the lending facility rate by 100 basis points and announced that the recourse to its lending facility will be capped at twice banks' capital starting June 2017.

Segmentation of BCEAO counterparties

12. Access to BCEAO refinancing operation reflects the banking sector segmentation. International banks with a large low-cost retail deposit base[5] and more stringent risk limits including for holding government securities, often determined by headquarters located outside of the Union, have large excess reserves and do not need BCEAO refinancing. On the other hand, a second category of banks**,** have no excess reserves and large refinancing needs. This category includes Pan-African and WAEMU groups, striving to increase their balance sheets. Finally, some banks have excess reserves financed at the refinancing operations. This category largely consists of small local banks, which are often newcomers to the market. They do not benefit from a large deposit base and the support of a banking group. As a result, they tend to bid for precautionary excess reserves at the refinancing operations.

Refinancing against Excess Liquidity



Source: BCEAO

[5] As such, the non-remuneration of excess reserves does not represent a strong penalty for them because their cost of deposit funding is close to zero.

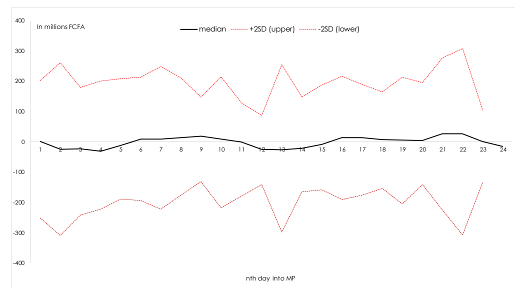
D. Determinants of the Demand for Excess reserves

The demand for precautionary money balances has two fundamental determinants: the uncertainty that affects the economic agents and against which they represent a buffer and, the opportunity cost of holding these balances.

Incompressible Reserves

13. Incompressible reserves are an important component of banks' need for refinancing. Banks try to keep a minimum balance on their account at the BCEAO, beyond the reserve requirement to buffer against unexpected cash outflows (i.e. for precautionary purposes). Concerns about access to refinancing in the market or at the central bank could also play a role. Incompressible reserves are usually estimated as the sum of the minimum balance kept by the banks during a maintenance period. The minimum account balance reflects how low each bank would comfortably allow its account to fall on a given day during the maintenance period. The aggregation gives an indication of how low the whole system is ready to go. Incompressible reserves, which are kept voluntarily, can (should) be lower than the realized excess reserves at the end of the period, which reflect the capacity of the banks to dispose of their involuntary reserves in the market.

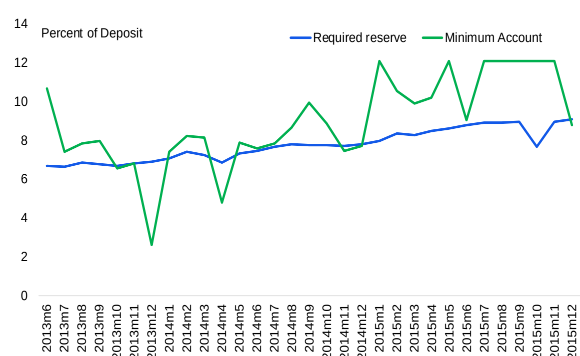
Intra-Maintenance Period Changes in Refinancing Needs



Source: BCEAO.

14. The high level of incompressible excess reserves hampers the shock absorbing function of the reserve requirement. The median of incompressible reserves stands at 6.6 percent of banks' total deposits from 2013 to 2016 for a reserve requirement of 5 percent of deposits (the reserve requirement also include some banks' assets in addition to deposits). While they dropped to 2.5 percent during one maintenance period, they often exceed the reserve requirement, which leaves only limited room for the reserve requirement to absorb autonomous factor shocks during the maintenance period. Altogether, the demand for voluntary reserves could reach more than eight percent of banks' deposits. Banks have two motives to hold balances at the BCEAO (i) to absorb autonomous factor shocks, which

Banks' Aggregated Minimum Balances at the BCEAO

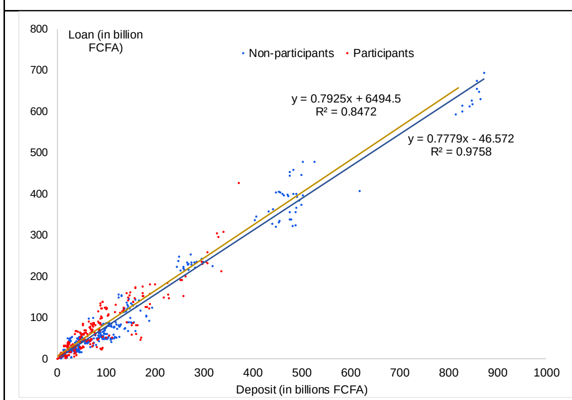


can reach CFAF 600 billion (or about 6 percent of deposits) on a given day, and (ii) keep a minimum balance permanently on account, which was estimated as at least CFAF 250 billion (or about 2.5 percent of deposits).

Banks' Funding Strategy

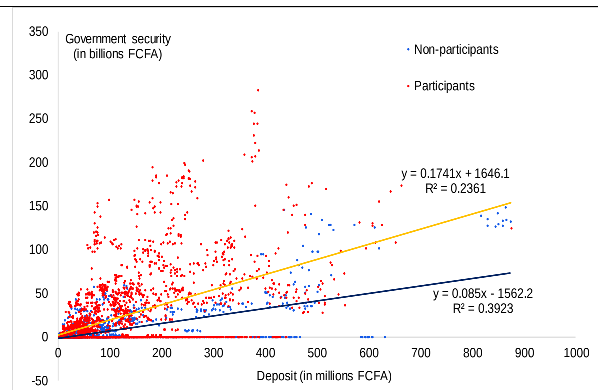
15. The demand for excess reserves also reflects financing strategies. Some banks are using BCEAO's refinancing as a cheaper source of funding compared to the market, including new customer deposits, to finance growing balance sheets. In addition, the portfolio of government securities is on average twice as large for banks with refinancing requirements (see chart). Central bank refinancing is hence going in large part to counterparties with a small deposit base, which invest in government securities rather than lending to the economy. Some banks are taking advantage of cheap short-term funding from the BCEAO in order to purchase longer-term and higher-yielding government securities. This strategy appears rational given (i) the spread between refinancing and government securities yields, (ii) the difference in capital cost between government securities and credit to the private sector, and (iii) the difference in terms of liquidity between government securities and credit to the private sector.

Deposit and loans for counterparties that participate and do not participate in refinancing operation



Source: BCEAO.

Deposit and Government securities for counterparties that participate and do not participate in refinancing operation



Source: BCEAO.

Results

16. We estimate the determinants of the demand for refinancing. Table 1 below presents the results of panel estimates of the probability that the BCEAO's counterparties participate in its 7 and 28-day refinancing operations. The results are estimated based on a logit model for the period 2010 to 2016. During this period, about half of all counterparties participated in operations on average. Dummy variables were added for the membership to a banking group and country location. Estimates were done based on nominal data and variables normalized by each bank's deposit to account for their respective size.

17. The liquidity need variables have the largest impact on the participation probability. The marginal effect of investment strategy variables on the participation probability is lower than the one of liquidity need variables, indicating that participation remains first motivated by liquidity needs. An increase in the reserve requirement amount increases the probability of counterparties' participation in a refinancing operation. On the other hand, increase in excess liquidity rapidly reduces a counterparty's probability of participating in an operation.

18. The results suggest that:

- A larger portfolio of government securities increases the probability of participation in refinancing operations. The marginal effect of an increase in the portfolio of government securities on the participation probability is positive and significant. It is also notably larger than in the case of other classes of eligible assets, such as credit claims. The participation is also correlated with the counterparty's leverage, which is approximated by the ratio of credit to deposits.

- Membership in a banking group changes the probability of participating in the operations. Membership in Pan-African groups and being an independent bank increase the most the probability of attending an operation. Membership in an international or a WAEMU group does not influence the probability of participating in an operation.

Annex III, Box 1. Model Description

The long-term relationship between the BCEAO refinancing and it determinants could be represented as a vector error correction model. The model is estimated based on maintenance period average as the averaging provision of the reserve requirement could absorb some liquidity shocks without creating a demand for more or less refinancing at the BCEAO.

$$equation\ 1{:}\ \Delta\begin{bmatrix} RF \\ AF \\ RR \end{bmatrix}_t = \Delta \boldsymbol{y}_t = \boldsymbol{\alpha\beta}'\boldsymbol{y}_{t-1} + \Sigma_{i=1}^{2}\boldsymbol{\Gamma}_i\Delta\boldsymbol{y}_{t-i} + \boldsymbol{\nu} + \boldsymbol{\varepsilon_t}$$

Following the vector error-correction model (VECM) of cointegrating variables, the change of the total refinancing balance, the sum of the autonomous factors and the reserve requirements at time $\boldsymbol{t}$ can be written as a 3×1 vector, with both $\boldsymbol{\alpha}$ and $\boldsymbol{\beta}$ being 1×3 vectors of coefficients on the lag term of the cointegrating vector. $\boldsymbol{\Gamma}_i$ are 2×2 coefficient matrices. $\boldsymbol{\nu}$ is a vector of constants and $\boldsymbol{\varepsilon_t}$ a matrix of i.i.d. shocks. The residual of equation 1 $\boldsymbol{\varepsilon_t}$ represents involuntary excess reserves**.**

Methodology:

To estimate the probability of the banks receiving refinancing from the BCEAO, we adopted a panel logit model, which can be formally written as:

$$\Pr(y_{it} = 1 | x_{it}, v_i) = F(\mathrm{x}_{it}\beta + v_i)$$

Where

$$F(z) = \frac{1}{1 + \exp(-z)}$$

In this setup, the probability of bank i receiving refinancing at time t is conditional on a vector of covariates x_{it} and a bank-specific effect v_i that is not captured by the covariates. This function $F(z)$ takes the form of logistic transformation.

We tested different specifications of the model based on changing assumptions about the bank-specific effects, namely random effect, fixed effect and population-averaged effect.

WAEMU: Determinants of the Demand for Refinancing

	1	2	3	4	5	6	7	8	9	10	11	12	13
Marginal effect	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing	Receive 1-week and 28-day refinancing
Reserve requirement	1.20***	1.19***	1.17***	0.77***	0.63***	1.24***	0.51***	0.50***	0.59***	2.58***	-0.67***	-0.90***	-0.71***
Excess liquidity	-2.61***	-2.60***	-2.50***	-3.31***	-3.28***	-3.68***	-18.19***	-1.82***	-1.86***	-1.91***	-1.20***	-1.21***	-1.43***
Credit claims	0.24***	0.24***	0.23***	0.17***	0.17***	0.15***	0.29***	0.29***	0.29***	0.14**	0.27***	0.30***	0.29***
Government securities	0.84***	0.83***	0.79***	0.99***	0.95***	0.99***	0.59***	0.59***	0.59***	0.51***	0.83***	0.82***	0.85***
Net lending	-0.13**	-0.13**	-0.12**	-0.34***	-0.34***	-0.24***	-0.14***	-0.14***	-0.13***	-0.10**	-0.10***	-0.12***	-0.07***
Rate spread	2.82***	2.80***	2.82***	6.61***	5.37***	8.7***	3.41**	3.39**	3.57**	2.71**	6.86***	5.89***	9.03***
Autres	31.56	42.91*	-20.32**	24.36***	25.77***	-21.40***	48.01*	47.35	-60.33***		12.25***	14.99***	-26.81***
Pan-African	74.48***	80.92***		55.51***	55.12***		93.95***	94.50***			53.11***	51.54***	
UMOA	40.40.	60.64**		11.52**	19.98***		-25.60	-5.58			-3.13	7.80*	
International	-20.42*	-16.43											
Nonbanks				34.71***	21.26***								
Benin	-1.77		7.79	-21.74***		-10.69***	-10.00		-1.30		4.56		1.30
Burnika	0.86		-6.4	-30.54***		-25.81***	31.73		16.43		2.48		-7.99**
Cote d'Ivoire	-16.66		-17.45	-38.55***		-29.06***	-50.69***		-53.25		-16.78**		-16.30***
Guinee Bissau	40.47		45.05				48.29**		-0.42		35.66***		3.49
Mali	31.29		35.45	-5.75		4.08	32.66		23.18		22.43***		15.51***
Niger	-5.89		3.12	-22.00***		-8.8***	-41.08**		-37.25				
Senegal	5.97		12.08	-15.74***		-3.1	-10.48		-7.81		8.91**		5.26
Togo				-21.56***		-11.12***					8.00**		4.98
Normalized by deposit	No	No	No	No	No	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Random Effect	Yes	Yes	Yes	No	No	No	Yes	Yes	Yes	No	No	No	No
Fixed Effect	No	No	No	No	No	No	No	No	No	Yes	No	No	No
Population Average	No	No	No	Yes	Yes	Yes	No	No	No	No	Yes	Yes	Yes
Hit/miss ratio	77.23	76.92	76.22	80.76	76.92	76.35	56.92	55.31	53.21	41.91	58.30	57.48	55.89
Observations	8769	8769	8769	8769	8769	8769	5102	5102	5102	2679	5102	5102	5102
Number of banks	140	140	140	140	140	140	122	122	122	60	122	122	122

Marginal effects in table

*** p<0.01, ** p<0.05, * p<0.1

INTERNATIONAL MONETARY FUND

COMMUNICATIONS DEPARTMENT

Appendix I. Draft Press Release

Press Release No. 17/xx
FOR IMMEDIATE RELEASE
March 31, 2017

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes Regional Consultation with West African Economic and Monetary Union

On March 31, 2017, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with WAEMU.

Background

Economic activity has remained strong but vulnerabilities have increased. Real GDP growth is estimated to have reached 6.2 percent in 2016, underpinned by robust and resilient domestic demand. Inflation remained subdued, at about 0.4 percent on average in 2016 due to continued solid agricultural production and low oil prices. Preliminary data suggest an overall fiscal deficit of 4.5 percent of GDP in 2016, higher than initially planned (4 percent). Credit to the public sector expanded at a significantly faster rate (43.6 percent) than credit to the private sector (9.7 percent). However, money growth remained moderate (10.2 percent), as net foreign assets declined. Public debt is on the rise and reserve coverage declined to 3.7 months of imports at End-December 2016, reflecting a continued expansion in public infrastructure and lower-than-expected external financing.

The BCEAO took measures to activate the interbank market and enhance monetary transmission mechanisms. In particular, the Central Bank widened the corridor between the minimum bid rate for the open market refinancing operations and the credit facility rate to 200 basis points, and announced that the recourse to its lending facility will be capped at twice banks' capital starting June 2017. The Central Bank also reduced the reserve requirement ratio from5perecnt to 3 percent of deposits. Important steps were also undertaken to promote financial stability. These reforms include the adoption of Basel II and III capital standards, and the introduction of consolidated supervision. Nonetheless, conditions in the banking sector remain challenging. Credit and concentration risks are important and the ratio of gross NPLs to total loans is still relatively high while the situation of several troubled banks remains unresolved.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

The outlook remains positive provided continued macroeconomic stability and strong resolve to improve the business environment and promote private investment. Growth is projected to stay above 6 percent over the medium term and inflation would remain low on account of continued solid agricultural production. Risks are titled to the downside. Planned fiscal consolidation has been repeatedly deferred in recent years and most countries are still scaling up public investment. Continued delays in implementing fiscal consolidation would further increase public debt, raising debt distress risks and put the currency coverage at risk. At the same time, a slow progress in raising public investment efficiency and advancing private-sector friendly structural reforms could slow down the growth momentum. Other risks stem from a sharper slowdown of economic growth, tighter international financing conditions, as well as a sustained decline in cocoa prices. In addition, security risks remain important.

Executive Board Assessment[2]

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Table 1. WAEMU: Selected Economic and Financial Indicators, 2012–21

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
				Est.			Proj.			
	(Annual percentage change)									
National income and prices										
GDP at constant prices	6.3	6.1	6.6	6.2	6.2	6.5	6.6	6.5	6.6	6.5
GDP per capita at constant prices	3.4	3.3	3.7	3.3	3.3	3.6	3.7	3.6	3.8	3.6
Broad money to GDP	-2.5	3.2	4.7	2.4	...	...	...	...	...	...
Consumer prices (average)	2.4	1.3	-0.1	1.0	0.4	1.5	1.9	1.9	2.0	2.0
Terms of trade	-4.9	-9.2	-2.3	1.2	0.1	0.1	-1.2	-1.7	-0.6	1.1
Nominal effective exchange rates	-2.3	4.3	3.8	-3.8	...	...	...	...	...	...
Real effective exchange rates	-2.6	2.7	1.0	-5.5	...	...	...	...	...	...
	(Percent of GDP)									
National accounts										
Gross national savings	15.6	15.9	17.0	15.0	16.1	17.1	17.7	17.5	18.1	18.3
Gross domestic investment	21.4	22.5	22.1	21.2	22.1	23.4	23.7	23.5	23.7	23.5
Of which: public investment	5.7	7.4	7.1	7.8	8.2	8.9	8.7	8.4	8.6	8.4
	(Annual changes in percent of beginning-of-period broad money)									
Money and credit [1]										
Net foreign assets	-2.1	-6.0	0.1	-1.7	...	...	...	...	...	...
Net domestic assets	11.9	16.4	12.7	0.4	...	...	...	...	...	...
Broad money	9.8	10.5	12.9	-1.3	...	...	...	...	...	...
Credit to the private sector	14.8	15.6	14.3	15.6	12.4	12.1	11.6	13.6	12.8	13.5
	(Percent of GDP, unless otherwise indicated)									
Government financial operations [2]										
Government total revenue, excl. grants	17.5	17.8	17.4	18.3	18.6	19.2	19.4	19.8	20.1	20.2
Government expenditure	22.6	23.8	23.5	24.9	25.5	26.1	25.4	25.0	25.0	24.8
Official grants	2.5	3.0	2.7	2.1	2.4	2.2	2.2	2.2	2.1	2.2
Overall fiscal balance, incl. grants (cash basis)	-2.6	-3.0	-3.3	-4.5	-4.5	-4.7	-3.7	-3.0	-2.7	-2.5
Basic fiscal balance, incl. grants & HIPC	-1.6	-1.4	-1.6	-1.5	-1.5	-0.9	-0.3	0.3	0.6	0.9
External sector										
Exports of goods and services [3]	26.7	24.3	23.7	24.3	23.9	24.1	25.8	23.0	22.7	22.3
Imports of goods and services [3]	34.5	35.7	35.2	33.2	33.5	33.6	34.8	31.9	31.1	30.1
Current account, excl. grants [4]	-7.2	-9.1	-7.5	-8.0	-8.8	-8.9	-8.4	-8.4	-7.9	-7.4
Current account, incl. grants [4]	-5.8	-6.6	-5.1	-5.8	-6.1	-6.3	-6.0	-6.0	-5.7	-5.3
External public debt	24.6	24.5	23.9	27.9	27.9	28.1	27.8	27.6	27.1	26.9
Total public debt	36.5	37.6	38.5	44.5	45.9	46.3	44.8	43.1	41.3	40.7
Broad money	27.9	28.8	30.1	30.8	...	...	...	...	...	...
Memorandum items:										
Nominal GDP (billions of CFA francs)	43,200	46,194	49,918	53,968	57,991	62,584	67,969	73,667	79,969	86,726
Nominal GDP per capita (US dollars)	835	897	943	827	867	899	951	1,007	1,069	1,126
CFA franc per US dollars, average	511	494	494	591	...	...	...	...	...	...
Foreign exchange cover ratio [5]	98.4	84.0	77.0	79.2	...	...	...	...	...	...
Reserves in months of imports (Excl. intra-WAEMU imports)	5.1	4.5	4.7	4.6	3.7	3.5	3.9	4.0	4.0	4.0

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

[1] Year on year change, end December; for 2014 year on year change, end November.

[2] Fiscal data for 2014 reflect a strong increase in the fiscal deficit of Niger, following a new project in the hydrocarbon sector.

[3] Excluding intraregional trade.

[4] Data up to 2011 are corrected for intraregional trade discrepancies by BCEAO.

[5] Gross official reserves divided by short-term domestic liabilities (IMF definition).