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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 17/24-1

2:30 p.m., March 31, 2017

1. West African Economic and Monetary Union—2017 Regional Discussions on Common Policies of Member Countries

Documents: SM/17/58 and Correction 1

Staff: Loko, AFR; Traa, SPR

Length: 30 minutes

Executive Board Attendance

M. Furusawa, Acting Chair

Executive Directors	Alternate Executive Directors
	D. Mahlinza (AE)
D. Sembene (AF)	
	V. De la Barra (AG), Temporary
	G. Johnston (AP)
	P. Fachada (BR)
	P. Sun (CC)
	W. Garcia Corzo (CE), Temporary
N. Horsman (CO)	
	T.Temiz (EC)
	S. Badirou-Gafari (FF)
	K. Merk (GR)
	R. Gunaratne (IN)
	M. Psalidopoulos (IT)
M. Kaizuka (JA)	
	M. Daïri (MD)
	F. Al-Kohlany (MI), Temporary
	J. Clicq (NE), Temporary
	T. Sand (NO), Temporary
	L. Palei (RU)
	S. Keshava (SA), Temporary
	T. Marcelo (ST)
	P. Inderbinen (SZ)
	M. Chen (UK), Temporary
	S. Sabharwal (US)

G. Bauche, Acting Secretary
J. Morco, Summing Up Officer
D. Daly, Board Operations Officer
P. Martin, Verbatim Reporting Officer

Also Present
African Department: D. Desruelle, A. Gulde, B. Loko, D. Robinson, P. Sharma, J. Toujas- Bernate, B. Yontcheva. Finance Department: H. Mooney. Legal Department: H. Pham. Middle East and Central Asia Department: S. Choi. Monetary and Capital Markets

Department: R. Awad. Strategy, Policy, and Review Department: C. Ahokpossi, X. Maret, B. Traa, A. Zdzienicka. World Bank Group: I. Konjhodzic, L. Moller.
Alternate Executive Director: M. Raghani (AF), H. Razafindramanana (AF). Senior Advisors to Executive Directors: M. Hillebrand (GR), A. Machmud (ST), R. N'Sonde (AF), P. Pollard (US), E. Sishi (AE), B. Varga (EC). Advisors to Executive Directors: P. Abradu-Otoo (MD), M. Atamanchuk (RU), S. Fan (CC), D. Hart (CO), T. Hemingway (UK), B. Jappah (AE), S. Sagdullayev (AP).

1. WEST AFRICAN ECONOMIC AND MONETARY UNION—2017 REGIONAL DISCUSSIONS ON COMMON POLICIES OF MEMBER COUNTRIES

Mr. Sembene and Mr. N'Sonde submitted the following statement:

Our authorities are thankful to staff for the quality and candor of the policy discussions that took place recently in Lomé, Ouagadougou, Abidjan and Dakar in the context of regional consultations with WAEMU. The staff report reflects faithfully the thrust of these discussions and our authorities broadly agree with staff's analysis and policy recommendations.

Recent Economic Developments

Economic activity in the WAEMU region continued to be buoyant in 2016, driven by large public investment programs and strong domestic consumption. At the same time, inflation was subdued, partly thanks to robust agricultural production. WAEMU countries pursued their growth-friendly fiscal consolidation plans, albeit unsuccessfully in many cases. Indeed, in a number of countries pressures on the budget resulted from the authorities' efforts to address infrastructure gaps and promote economic transformation. As a result, staff estimate that total debt in the region rose slightly from 44.5 percent in 2015 to 45.9 percent in 2016 due to reliance on domestic markets to finance deficits, while external debt remained unchanged during the same period. However, the external position deteriorated further, as the current account deficit widened slightly owing notably to larger imports related to investment programs and lower cocoa and gold export revenues. This contributed inter alia to the decline of reserves in months of imports.

Rapid growth of credit notably to the public sector led BCEAO to tighten the monetary policy stance last December through an increase in its lending facility rate. The central bank also decided to limit access to refinancing by banks, with a view to helping deepen the interbank market. These decisions contributed to decreasing banks' refinancing with the central bank and stimulating the volume of transactions in the interbank market. More recently, the Monetary Policy Committee reduced the reserve requirement rate, a move expected to enhance liquidity conditions and further reduce refinancing needs. While bank portfolios deteriorated slightly, the sector remains profitable as the profitability ratio increased by an annual average of 12 percent since 2010. Bank solvency ratios stand at more than 8 percent in all but one WAEMU country. While the ratio of non-performing loans (NPLs) to total loans remain high, it is worth noting that it declined significantly from 15.6 percent to 13.9 percent from September to December 2016.

Economic Outlook and Risks

Prospects for 2017 and over the medium-term remain generally positive for the region, with growth projected to be in the neighborhood of 6.5 percent. Inflation is expected to remain low, while fiscal programs will be anchored by the WAEMU convergence criterion of 3 percent fiscal balance to GDP ratio by 2019. The WAEMU authorities acknowledge that the emerging vulnerabilities described in the staff report call for continued vigilance. They concur that the main risks include delayed implementation of members' fiscal consolidation plans and structural reform agenda, regional security challenges, decline in the price of commodities such as cocoa, and the worsening of the economic situation in the CEMAC region. While slowdown in global growth is also considered as a risk, it is the authorities' view that its adverse impact on regional growth appears to have been overestimated in the staff report, as staff simulations fail to capture the positive implications of lower oil prices for net importers like WAEMU countries as well as other developments that typically tend to accompany global slowdown, including higher prices of commodities such as gold a safe haven in times of uncertainty.

Policy and Reform Agenda

The regional authorities agree with staff on the importance of sustaining fiscal consolidation efforts as a prerequisite for maintaining strong growth prospects over the medium term and securing a sound external position.

Integration and Policy Coordination

The WAEMU authorities will continue to promote regional integration with a view to reaping the benefits of the currency union which provides a strong framework for macroeconomic stability. To this vein, they will strive to preserve long term fiscal and debt sustainability, while implementing their respective national development plans. The WAEMU authorities stress the need to pursue national public policies in a coherent and coordinated manner in order to meet domestic and regional policy objectives. In this respect, they are mindful of the need for domestic fiscal policies to be calibrated taking into account external stability considerations at the regional level. In addition, there is broad agreement with Fund staff on the need for the WAEMU Commission to play a key role in ensuring adequate policy coordination. In this regard, Fund's continued technical assistance will be critical in strengthening countries' policy framework. They also welcome staff's recommendation to strengthen the capacities of the WAEMU Commission in terms of monitoring and harmonizing national policies, as well as managing public-private partnerships (PPPs) along with the West African Development Bank (BOAD). Regional institutions will also benefit from Fund's advice in the area of fiscal and monetary policy coordination.

Fiscal Policies

With the aim at sustaining strong growth and making it more inclusive, plans for economic development and emergence in WAEMU members are being implemented with the assistance of technical and financial partners, including the IMF, the World Bank and African Development Bank. At the same time, care will be taken by country authorities to tackle peace and security threats facing the region.

Going forward, the regional authorities acknowledge the need to pursue fiscal consolidation efforts. In line with the regional convergence criteria related to the wages-to-tax revenue and tax revenue-to-GDP ratios, country authorities will thus be encouraged to take necessary steps to strengthen revenue mobilization and further improve the quality and efficiency of public spending. In this connection, WAEMU authorities place a high premium on the need to improve the quality and efficiency of expenditures, notably by focusing capital spending on productive investments with positive impact on government revenues. It is also the authorities' conviction that achievement of fiscal targets will be facilitated by the growth dividend and fiscal gains associated with infrastructure investment. However, they acknowledge the need for adopting adequate financing mechanisms for infrastructure investment, including through concessional resources and public-private partnerships.

Monetary Policy and External Stability Issues

As noted above, BCEAO's recent shift in monetary policy stance has led to decrease in banks' refinancing with the central bank and increase in the volume of transactions in the interbank market. Issuance of government bills has continued. Meanwhile, bank liquidity had been stable in the first few months of 2016 before dropping in August on. BCEAO continues to monitor closely developments in bank liquidity and compliance to prudential requirements.

Prospects for 2017 indicate further increase in both credit to governments and to the private sector. BCEAO stands ready to take further action to prevent excess liquidity and financing. It calls for efforts to ensure that the private sector takes over the public sector as driver of growth.

Risks to the external position are significant and include: a further decrease in export commodity prices, a contraction in official development assistance (ODA), a diminution of remittances, and an increase in global oil prices. At the same time, total external financing needs for the region are on the rise. Against this backdrop, the WAEMU authorities will pursue prudent reserve management, with a view to enhancing external buffers. This will include notably diversifying reserve assets in line with the new SDR basket and asset investments in currencies offering yields with brighter prospects. In parallel, BCEAO will continue to ensure that banks' use of its window to operate foreign currency transactions is backed with actual demand for transfers. It also monitors closely the flows of export revenue repatriation. In addition, the central bank will continue to emphasize the need for country authorities to comply with existing legal guidance on external financial relations, related to the repatriation of foreign currency export revenue.

Financial Sector Policies

The WAEMU authorities reiterated their commitment to ensure a sound and well-functioning financial sector, and agreed with staff's recommendations on the need to enforce existing prudential regulations, prepare new macro-prudential regulations, and strengthen the financial safety nets, including the payment system guarantee fund (Fonds de Garantie des Systèmes de Paiement), the Deposit Guarantee Fund (Fonds de Garantie des Dépôts) and the financial stability fund (Fonds de Stabilité Financière). In particular, the operationalization of the Deposit Guarantee Fund is proceeding as planned. Its organizational and administrative framework has already been developed, with the recruitment of staff and statutory auditors. Work is underway with the aim of facilitating the adoption of the contribution rate by the WAEMU Ministerial Council, submitting relevant documentation to the executive board, finalizing enrollment procedures, and calls for contributions. It is expected that the Fund's reserves will be built gradually.

The BCEAO authorities will safeguard financial stability notably through close monitoring of, and—if required—restrictions in banks' refinancing with the central bank. They will also pursue the transposition of Basel II and III principles on capital requirements for operational and market risks to enhance the resilience of banks. With regard to the framework for banking crisis resolution, significant progress has been achieved in 2016 on proposals for the amendment of the Annex to the Convention governing the WAMU Banking Commission. These proposals which include rules of supervision on a consolidated basis, a regional resolution authority and a resolution fund, will be completed by integrating supplementary elements before submission to the Union's authorities by June 2017. The WAEMU authorities share the view that the resolution authorities should be endowed with the necessary authority and independence. The Banking Commission continues to closely monitor 28 cross-border banking groups which carry a systemic weight, and collaborate with banking supervisors from other regions, notably by participating in relevant supervisory colleges.

Progress in financial inclusion is encouraging. For instance, mobile financial inclusion varies from 40 percent to 60 percent across countries in WAEMU. BCEAO continues to aim at greater financial inclusion by promoting a conducive environment and establishing a regional framework consistent with national frameworks. It monitors risks associated with weaknesses or failure of electronic money institutions (EMIs). The regional authorities attach a particular importance to the microfinance sector given its strategic role in promoting financial inclusion. Reforms are ongoing to improve the institutional structure of microfinance supervision and an action plan is being designed to enhance the sector's profitability.

Improving Competitiveness and Resilience

The regional authorities are mindful of the importance of accelerating reforms designed to improve structural competitiveness and bolster resilience. Going forward, they will encourage national authorities to coordinate reform efforts aimed at addressing infrastructure gaps, enhancing human capital, reducing the cost and burden of doing business, and promoting financial deepening. It is also their intention to promote diversification, by prioritizing reforms that carry the highest economic impact.

In concluding, the WAEMU authorities look forward to the Fund's continuous support for their policy endeavors, at both regional and country levels.

Mr. Daïri and Mr. Abradu-Otoo submitted the following statement:

We thank staff for a detailed report and Mr. Sembene and Mr. N'Sonde for an insightful buff statement.

WAEMU’s macroeconomic performance in recent years has been strong and the outlook is favorable, even though vulnerabilities have increased. Large public investments and resilient domestic demand have helped sustain robust growth, and inflation remains subdued, but public debt has risen, external buffers have been reduced, and the pace of structural reforms, including those designed to improve the business climate, has been slow. We welcome Mr. Sembene and Mr. N’Sonde’s indication that the authorities are cognizant of the vulnerabilities faced by the region and the need for continued vigilance. To put the region back on a path of fiscal consolidation and relieve pressure on the external position, the authorities would need to gradually reduce fiscal deficits while preserving critical infrastructure investments and rebuilding fiscal buffers. Deeper regional integration and improvement in the business climate will be important to support investment and growth going forward. We agree with the thrust of staff appraisal.

The persistence of the region’s fiscal deficits at current levels would further erode reserve coverage levels in the medium-term. Country fiscal consolidation plans and reinforcement of budget management will need to be implemented to preserve debt sustainability, protect reserves, and rebuild fiscal buffers. Like staff, we encourage the authorities to continue enhancing revenue and improving spending quality while strengthening debt management. In this regard, we welcome Mr. Sembene and Mr. N’Sonde’s indication of the WAEMU authorities’ broad agreement with staff recommendations, including the need to give priority to PPPs and concessional resources for financing member countries’ ambitious infrastructure development programs.

Monetary policy in the last quarter of 2016 was appropriately tightened by raising the lending facility rate and limiting banks’ access to refinancing to help deepen the interbank market. The March 2017 decision to lower the reserve requirement will reduce liquidity pressures and the need for central bank refinancing. It is important for the region to remove impediments to effective transmission mechanism. Like staff, we encourage the authorities to continue working toward reducing market segmentation, improving liquidity management, and deepening financial markets.

The WAEMU authorities have taken steps to strengthen the financial sector regulatory framework, including by adopting Basel II and III capital requirements, introducing consolidated supervision, and tightening large exposure limits. However, the sector is still faced with high, although declining NPLs, low compliance with prudential norms on capital adequacy, and the absence of an effective resolution regime. Strengthening and streamlining banking sector policies, crisis management and resolution frameworks, as well as forging ahead with the agenda for financial inclusion, which still lags behind peers in the region, should remain a priority. We welcome Mr. Sembene and Mr. N'Sonde's indication of the WAEMU authorities' plans in these areas and their intention to continue close monitoring of cross-border banking groups, in close cooperation with home country supervisors.

Finally, stronger structural reform momentum is needed to boost competitiveness and diversification. The low ranking of the region in Doing Business and Global Competitiveness indicators underscores the need for more concerted efforts to improve the business climate, develop regional infrastructure, and ensure more reliable and affordable electricity supply. These efforts will require coordination and decisive policy actions at the regional and national levels, and we welcome the authorities' determination to move ahead in this direction.

With these remarks, we wish the authorities in the region further success.

Mr. Rojas Ramirez and Ms. Garcia Corzo submitted the following statement:

We welcome the staff report on the West African Economic and Monetary Union and thank Mr. Sembene and Mr. N'Sonde for their buff statement. WAEMU economies have been on a growth trajectory based on public investment, expanded demand and low inflation supported by public sector resources. In this context, the Union has to work further on compliance of the convergence actions needed to complete its objectives, namely, promote competitiveness and exports, improve business environment, attract FDI participation in private sector project financing, enhance the banking system and deepen the financial capital markets intra-union.

On fiscal policy, the persistent overall fiscal deficit may compromise the Union's economic stability creating pressures on international reserves that have been declining, and a rise in levels of public debt impacting growth sustainability. Undertaking a process of fiscal consolidation and working on public investment efficiency is crucial. In this context, we encourage WAEMU authorities to further advance in the convergence criteria.

On Monetary stance, we see merits in tightening monetary policy and enhancing liquidity management pushing the interbank market and monetary transmission mechanisms. We observe a predominance of credit expansion to the public sector. We encourage authorities to further advance in deeper financial markets, to promote business environment to attract FDI and private sources of financing. We commend authorities for the adoption of Basel I and II capital standards. We agree with staff on further strengthening banking supervision, enforcement of prudential regulations and implementing an effective resolution regime.

Finally, we fully support the IMF's assistance to WAEMU.

Mr. Merk and Mr. Hillebrand submitted the following statement:

We thank staff for the report and Mr. Sembene and Mr. N'Sonde for their candid and insightful buff statement. We take positive note that the member countries of the West African Economic and Monetary Union have continued their growth performance. Strong domestic demand as well as low and stable inflation rates contributed to the positive performance of economic activity. However, significant downside risks persist due to high fiscal and current account deficits, rising public indebtedness and an increasing reliance on non-concessional borrowing to finance public investment, sluggish implementation of structural reforms, and persisting vulnerabilities in the financial sector. Concerted actions at the national and regional level will be needed to overcome these impediments and achieve a sustainable growth performance over the longer term.

We agree that consistent prudent fiscal and monetary policies are essential to contain vulnerabilities and preserve the growth momentum. Regarding the consistency between national fiscal policies and regional monetary policy the Fund can contribute by monitoring the consistency of macroeconomic policy formulation and implementation in the course of its surveillance activities and by giving recommendations. However, we see the primary responsibility in this respect at the respective regional and national bodies.

While we generally acknowledge the need to close the infrastructure investment gap, we would strongly encourage the member countries to pursue a growth-friendly fiscal consolidation and thus preserve their fiscal sustainability. It is unfortunate that the planned fiscal consolidation has been repeatedly deferred in recent years. Against this backdrop, staff's assessment that projected 2017 deficits are not compatible with regional stability is a cause for concern. Given the risk for additional fiscal slippages in 2017, we strongly encourage the authorities to commit to sustained adjustment efforts and implement fiscal consolidation measures to reduce the substantial downside risk to the economic outlook. We agree with staff that further departures from the planned fiscal consolidation path would put debt sustainability at risk. We thus welcome the authorities' recognition of the importance to step up efforts to rebuild policy buffers and resilience. Particular emphasis should lie on enhancing revenue mobilization, broadening the tax base, containing current expenditure, improving the efficiency of public investment as well as public financial management and strengthening debt management.

Regarding the financial sector, it appears crucial to increase the efforts to close the remaining pockets of vulnerability in order to strengthen the resilience of the financial sector. At the same time, we deem it important to further improve the development of the sector to enhance the effectiveness of monetary policy and to increase private investment. While we appreciate the improvements being made in modernizing the regulatory framework, we encourage the authorities to take additional actions to ensure the compliance with the existing prudential regulations. Given the strong link between banks and sovereigns, we further encourage the authorities to implement measures to deepen the interbank and public debt markets and to tackle the problem of banks with capital shortfalls. Establishing an effective resolution regime and strengthen financial safety nets might prove beneficial in this regard.

In order to increase productivity, raise potential growth and thus contribute to achieve sustainable and inclusive growth, a strong commitment to accelerate the implementation of structural policies appears warranted. Limited progress in improving structural competitiveness compared to African and Asian peers is worrisome. We agree with staff that the member countries should accelerate their efforts to rapidly close the structural reforms gap, which is crucial to promote competitiveness and diversification. In this regard, we encourage the authorities to implement measures to address high costs of communication, transport and electricity, which significantly weaken the business environment and impede private-sector led growth.

We join staff in encouraging the authorities to improve the quality, coverage, and timeliness of regional data provision.

Mr. Johnston and Mr. Sagdullayev submitted the following statement:

We thank staff for an informative report and Mr. Sembene and Mr. N'Sonde for their helpful buff statement. Fiscal consolidation should remain a priority for WAEMU authorities and we see merit in staff's call to enhance revenue mobilization, contain current expenditure, improve public financial management, raise public investment efficiency, and strengthen debt management. Creating fiscal space would also help fill the gap in infrastructure investment.

Monetary policy effectiveness and the regulatory framework need improving. The recent tightening of monetary policy seems appropriate, especially in view of the growing pressure on external reserves. The BCEAO should continue to hold a prudent level of reserves to preserve the stability of the peg and maintain adequate buffers against external shocks. Enhancing the transmission mechanism should be underpinned by further deepening financial markets and implementing financial market reforms. We welcome the WAEMU authorities' commitment to ensure a sound financial sector by enforcing existing prudential regulations, developing new macroprudential regulations, and strengthening the financial safety net.

Structural reforms are critical to maintaining strong and inclusive growth. We encourage the regional authorities to continue their efforts to improve competitiveness, bolster resilience and promote diversification, and to coordinate their policy actions.

Mr. Marcelo and Mr. Machmud submitted the following statement:

We thank staff for a set of well-written reports and Messrs. Sembene and N'Sonde for their informative buff statement.

While the West African Economic and Monetary Union (WAEMU) region has experienced solid growth over the last five years, driven by public investment, vulnerabilities have increased as reflected by shrinking external buffers, high fiscal deficits and rising public debt levels. In this regard, we agree that sustaining current growth will require decisive policy actions focusing on enhancing coordination and consistency between national fiscal policies and regional monetary policy to contain vulnerabilities and safeguard macroeconomic stability, as well as accelerating structural reforms to boost competitiveness and economic diversification. We broadly agree with staff's appraisal and limit our comments to the following points for emphasis.

Credible fiscal consolidation among WAEMU member countries is critical in maintaining debt sustainability and external stability. While we note positively the progress made by several member countries in achieving their fiscal deficit targets in 2016, we encourage all member countries to reinforce their efforts to implement their growth-friendly fiscal consolidation plans to preserve their external position in medium term. This 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. Given member countries' past experience in undertaking fiscal consolidation, could staff comment on the prospects of member countries planned fiscal consolidation?

In addition to fiscal policy, appropriate monetary policy adjustment is essential in preserving external stability. We welcome BCEAO's decision to tighten monetary policy in December 2016 by increasing its credit facility rate and rationalizing access to the BCEAO's refinancing window in order to preserve foreign exchange reserve cover. As highlighted in the buff statement, the authorities are also committed to implementing additional monetary policy actions should conditions warrant. Regarding the authorities' recent decision to reduce reserve requirements, could staff elaborate on the intention of these measures in light of the December 2016 tightening measures?

Accelerated structural reforms will be important to foster sustainable and inclusive growth. We commend member country authorities' efforts to advance structural reforms. Nevertheless, accelerating the pace of reforms and fostering regional integration are important to improve competitiveness and resilience of the region. Further structural reforms should focus on improving the business environment, reducing barriers to regional trade, including cumbersome administrative procedures, and enhancing regional infrastructures.

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

Mr. Gokarn and Mr. Joshi submitted the following statement:

We thank staff for the comprehensive informative paper and Mr. Sembene and Mr. N'Sonde for the buff statement.

Driven by high levels of public investment, the WAEMU region has experienced strong growth in recent years although the current outlook remains punctuated with growing vulnerabilities associated with rising public debt and declining external buffers. Moreover, down side risks stemming from regional security challenges, delays in fiscal consolidation, appreciation of U.S. dollar, tighter financial conditions and slowdown in EMEs could impact growth adversely. In this milieu, structural reforms, reducing trade barriers to facilitate inter-regional integration, promoting economic diversification, enhancing human capital and improving business climate are key to supporting investment and growth for alleviating high incidence of poverty and unemployment existing in the region. Could staff indicate the extent of public support for social protection programs devoted to poverty alleviation?

Although, there is moderate risk to debt, large fiscal deficits and rising recourse to non-concessional borrowings could elevate debt vulnerabilities going forward unless national governments revert to current fiscal consolidation paths by increasing coordination and consistency between national regional fiscal policies by way of reinforcing budget management processes, improving debt management practices and adjusting the composition of domestic and external financing requirements. We appreciate the authorities' commitment to long term debt and fiscal sustainability and strengthening of the WAEMU Commission for harmonizing national policies. Could staff indicate the impact on growth if the WAEMU countries were to return to their planned fiscal consolidation path?

Elevated fiscal gaps with increasing reliance on domestic financing of deficits have had an adverse spillover effect on the current account deficit. This has resulted in depletion of reserves, which have fallen below four months of import cover. Continued high public investment efforts may lead to further widening of CA in 2017 on higher demand for imports, although FDI and grants for large investment projects would be able to finance the CA. Increasing risks to external stability imply that the authorities should urgently build external buffers, consolidate fiscal positions by enhancing revenue mobilization through tax reforms and improving efficiency of public investments by reinforcing accountability and governance while encouraging private investment to support growth.

On the positive side, the tightening of monetary stance by BCEAO would help limit fiscal deficits and support stability. Meanwhile, the efforts to develop inter-bank and public debt markets would expand the investor base, and enhance the transmission of monetary policy. We appreciate the commitment by authorities to control fiscal deficits for ensuring external stability.

The authorities have taken significant measures to strengthen financial stability, in particular, with the adoption of Basel capital standards and consolidated supervision of holding companies. Further efforts are needed to strengthen macro-prudential policies, risk-based supervision and the AML/CFT framework. The banking system, however, is saddled with weak capital positions, large exposure to sovereigns, credit and concentration risks and high NPLs.

Four state run banks are currently under administration and remain under close supervisory scrutiny. For this reason, the deposit guarantee fund, and the regional bank resolution framework approved by the council of ministers needs to be operationalized expeditiously. We welcome the significant progress made in developing a banking crisis resolution framework under the convention governing the WAEMU Banking Commission. The reorganization of the Banking Commission for supervision and resolution of large microfinance firms is a welcome step. Authorities should promote financial inclusion for improving access to financial services and credit to the vulnerable sections of the society. We appreciate that the authorities have broadly agreed with staff views on financial system stability.

We wish the authorities the best in future endeavors.

Mr. Psalidopoulos and Ms. Lopes submitted the following statement:

We thank staff for their insightful report and Mr. Sembene and Mr. N'Sonde for their helpful buff. WAEMU's economic activity remains robust but, in order to sustain a stable macroeconomic environment, national fiscal policies and regional monetary policies will need to be consistent, financial sector regulations duly enforced and structural reforms accelerated. As we broadly share staff's assessment we would just like offer a few specific comments.

We note that staff considers that the 2017 fiscal deficits do not ensure regional financial stability. This is very worrisome, and we encourage the authorities—both at national as at regional level— to step up their efforts in this regard. As most of the countries are breaching at least one of the first-order convergence criteria, we were wondering whether the regional authorities have sufficient instruments to ensure the countries' compliance with the criteria. We would appreciate if staff could give us further information on the instruments available and whether they are judged as sufficient.

Still on the 2017 fiscal stance, it is our understanding that most of the WAEMU member countries have (or are requesting) some sort of program with the Fund. In this context, we are somewhat puzzled with the inadequacy of the fiscal position. Were these targets agreed with staff? Is the stance adequate for each individual country but not the stance for the WAEMU as a whole? Are the programs off-track? The staff's comments would be appreciated.

On the financial sector, we welcome the adoption of the regulatory reforms and encourage the authorities to effectively enforce prudential limits. Furthermore, an operational and adequate resolution regime is fundamental to ensure the stability of the financial system. Its full establishment should not be further delayed.

We agree with staff that fostering regional integration and closing structural reforms and investments gaps is key to promoting competitiveness of the region. We would appreciate if staff could give us further insights on the specific measures/reforms which would have a higher pay-off.

Mr. Ostros and Ms. Sand submitted the following statement:

We thank staff for the report and Mr. Sembene and Mr. N'Sonde for their informative buff statement. We agree with staff's appraisal and would like to offer the following comments.

We note the countries in the WAEMU continue to experience strong growth rates while inflation has remained subdued. However, growth is largely driven by public infrastructure investment contributing to larger than expected fiscal deficits, while public debt is on the rise. Progress has also been slow on structural reforms and regional integration, and this has held back private external investments which has been lower than expected. Although the outlook remains positive, vulnerabilities have increased. We recognize the risks to growth and macroeconomic stability which will require concerted efforts on the national and regional level to proceed with fiscal consolidation and to implement critical structural reforms to improve the business environment to ensure private investment picks-up.

In regards to fiscal policy, we note from the staff report that this year's fiscal deficits are not compatible with medium-term external stability. We agree with staff that fiscal consolidation is needed to preserve debt sustainability and support the recommendations of enhanced coordination and consistency between national fiscal policies. We would also like to reiterate the remarks by the BCEAO that the Fund could strive to ensure it gives consistent fiscal policy advice to the individual countries in connection with Article IV consultations and reviews of programs. Given that most countries in the economic and monetary union are engaged with the Fund also through lending programs, national fiscal policy is to a large extent determined by

Fund-agreed targets. In this regard, we encourage staff to ensure consistency across country teams and would like to ask if there is a framework in place to ensure such consistency, and if not, are there any plans to establish one?

We note the recent decisions of the BCAEO to tighten monetary policy somewhat. Going forward, we believe the focus should be on enhancing the monetary policy transmission mechanisms. We see merit in the proposal to boost the interbank market in order to improve liquidity management along with a deepening of financial markets.

We welcome the important progress made in modernizing and strengthening the financial sector. However, vulnerabilities remain and we encourage the authorities to accelerate efforts to improve the stability of the financial sector by strengthening and streamlining the supervisory, crisis management, and resolution framework. Fostering financial inclusion should also remain a top priority and we urge the authorities to follow through with the regional action plan to promote financial inclusion. We note that the WAEMU countries lag behind their piers with poor access to finance and financial services for the most vulnerable groups, so efforts in this area should be intensified.

Mr. Mahlinza and Mr. Odonye submitted the following statement:

We thank staff for a comprehensive report and Mr. Sembene and Mr. N'Sonde for their insightful buff statement. The performance of the West African Economic and Monetary Union (WAEMU) has remained strong with real GDP growth exceeding 6 percent in recent years and inflation under control. However, delayed fiscal consolidation, growing public infrastructure spending and lower-than-expected external financing have resulted in the expansion of public debt and widening deficits. Mindful of the need to safeguard the monetary union, which has served the community well for many years, it is important to preserve long term fiscal and debt sustainability in member countries. In this regard, we urge the WAEMU Commission to step up its policy coordination role to achieve coherence between domestic and regional policy objectives.

A well-articulated path towards a sustainable fiscal position and congruency between national fiscal policies and regional monetary policy is critical for the monetary union. Like staff, we emphasize that reducing vulnerabilities, maintaining macroeconomic stability and sustaining the growth momentum are key to the success of the monetary union. Maintaining higher fiscal deficits is incompatible with the union's medium-term external stability goal. In view of the challenges faced by WAEMU in getting member countries to adhere to their fiscal consolidation plans, what are the prospects for achieving sustainable fiscal positions in the medium term?

With regards to price stability, we support the hike in the credit facility rate and tightening of access to the refinancing window following the December 2016 decisions by the Monetary Policy Committee of the BCEAO. In this context, we consider the measures as appropriate especially, since they aim to 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. In retrospect, we would like to have staff assessment on the effect of the actions on private sector activity considering that the desire to expand infrastructure did not deter government from borrowing even at higher rates.

We welcome efforts by the authorities in strengthening financial stability as articulated in the buff statement. The bold efforts by the authorities to raise regulatory measures in June 2016, including adopting Basel II and Basel III capital standards and introducing consolidated supervision of cross-border banks, are commendable. In particular, we applaud the authorities for the smooth takeoff of the deposit guarantee fund. We encourage them to maintain the tempo by enforcing existing prudential regulations; preparing for the implementation of an upgraded prudential framework and consolidated supervision; making the financial safety net (FGD) operational; and developing an effective regional bank resolution regime. Further, we support enhancing financial inclusion but note that it should never be at the expense of financial sector stability.

Continued structural reforms remain vital for promoting private investment, competiveness and diversification in the union. Since these elements have a strong nexus with promoting sustainable and inclusive growth, we encourage the authorities to focus on improving the business environment, reducing barriers to regional trade, including cumbersome administrative procedures, and enhancing regional infrastructure.

Mr. Geadah and Mr. Al-Kohlany submitted the following statement:

The West African Economic and Monetary Union (WAEMU) continued to record strong economic growth and subdued inflation. However, fiscal and current account deficits widened and the reserve coverage weakened. Risks to the outlook stem from delays in fiscal consolidation, a decline in coca export prices, and tighter external financing conditions.

Sustaining the ongoing growth momentum would be facilitated by further structural reforms and better coordination among the union's members. We would like to highlight the following points:

There is a need to reduce the fiscal deficits. We welcome the authorities' acknowledgment of the need for fiscal consolidation, in line with the regional convergence criteria. We concur with staff that countries should rein in current expenditures and improve revenue collection, especially that tax ratios remain relatively low. Stronger coordination and consistency between national fiscal policies and the regional monetary policy is needed. In this regard, it would also be important to coordinate the fiscal targets in Fund programs in the region.

We note staff support for the tightening of monetary policy in late 2016 and their recommendation to the authorities to be ready for further tightening, if needed. However, as noted in the report, the reduction in reserves requirements in March seems to counter this tightening. Further information on the rationale for lowering the reserve requirements is welcome.

We also note the recent upgrade of the regulatory framework in an effort to bring it closer to Basel II/III standards. Updating the regulations alone will not resolve the problems facing the banking sector. A significant number of banks are not in compliance with the current—less strict—regulations, as 42 percent of banks do not meet minimum capital requirements. In addition, banks are facing high NPLs and concentration risk, and banks comprising 16 percent of the sector's assets are either under temporary administration or close supervision scrutiny. Stronger enforcement of prudential regulations is needed. To this end, enhancing the financial safety nets, including the Deposit Guarantee Fund, and strengthening cross border supervision are important measures.

While external reserves coverage has dropped, the current and projected medium-term reserve cover remains above the threshold required by the zone's monetary arrangement with France. However, staff assessment of reserves adequacy indicates that reserves are below the optimal buffer. The staff's comment on the treatment of the monetary arrangement with the French Treasury in the reserves adequacy assessment would be welcome.

Structural reforms aimed at enhancing the diversification of the economy, improving the business environment, increasing competitiveness, and improving financial inclusion would benefit growth and macroeconomic stability. We concur with staff that reducing barriers to regional trade, including cumbersome administrative procedures, are important steps towards addressing structural constraints to private investments. We also welcome the authorities' commitment to enhance human capital, reduce the cost and burden of doing business, and promote diversification, as indicated by Mr. Sembene and Mr. N'Sonde in their informative buff statement.

Mr. Alogeel and Mr. Keshava submitted the following statement:

We thank staff for a well-focused report and Mr. Sembene and Mr. N'Sonde for their helpful buff statement. We welcome the continued strong growth performance with subdued inflation in the WAEMU region. The medium-term outlook is also positive, but we note that vulnerabilities have increased. The authorities should therefore step up their reform efforts to safeguard macroeconomic and financial stability. To this end, priorities include sustained fiscal consolidation, improved coordination and consistency between national fiscal policies and regional monetary policy, and structural reforms to support competitiveness and diversification. We broadly agree with staff's policy recommendations and would like to confine ourselves to a few issues.

Fiscal consolidation in a growth-friendly manner is essential to reduce public debt and mitigate pressure on monetary policy and international reserves. In this connection, we encourage member governments to persevere with their planned fiscal consolidation with an objective to reach an overall regional fiscal deficit of 3 percent of GDP in 2019, in line with the WAEMU convergence criteria. To this end, priorities include improving domestic revenue mobilization, containing current expenditure, enhancing public spending efficiency, and strengthening public debt management. We understand that the Fund, the World Bank and other partners, including the African Development Bank, have been providing technical assistance to the WAEMU countries to strengthen public investment. We would welcome staff elaboration on follow-up measures taken by member countries to improve public investment. Are countries also exploring promotion of PPPs to support infrastructure investment, including to enhance regional infrastructure, and putting in place appropriate frameworks to manage risks?

We share staff's view that keeping monetary policy on hold in the current conditions is appropriate and it will be important to closely monitor the impact of recent measures. In addition, we underscore the need for continued efforts to enhance monetary policy effectiveness, including through further improving liquidity management, strengthening the interbank market, and deepening financial markets. On reserve adequacy, we see the need for a build-up in international reserves, as the reserve cover is below the staff's recommended optimal buffer against external shocks.

We commend the authorities for adopting a set of ambitious regulatory reforms in June 2016 that would help modernize the financial sector in the region. In this context, we echo staff recommendation to enforce existing prudential regulations, given that conditions in the banking sector remain challenging, while making preparations for the effective implementation of the upgraded regulatory framework. We look forward to the implementation of the five-year regional action plan adopted in June 2016 that aims at expanding access and use of financial services and products to 75 percent of the WAEMU adult population.

Finally, continued reform efforts to improve competitiveness and diversification as well as supporting regional integration are essential to sustain the current strong growth momentum. Here, we are encouraged to note in the statement of Mr. Sembene and Mr. N'Sonde that the regional authorities will encourage national authorities to coordinate reform efforts aimed at reducing the cost and burden of doing business, addressing infrastructure gaps, enhancing human capital, and promoting financial deepening.

With these remarks, we wish the WAEMU authorities further success.

Mr. Badirou-Gafari and Ms. White submitted the following joint statement:

We thank staff for this insightful and comprehensive report. We also thank Mr. Sembene and Mr. N'Sonde for their helpful buff statement.

We largely agree with staff appraisal on the economic and financial situation of West African Economic and Monetary Union (WAEMU). We would like to highlight the following issues for emphasis.

Economic Growth and Fiscal Imbalances

Economic growth is still strong and inflation remains low in WAEMU countries. Last year, Côte d'Ivoire and Senegal, the largest economies of the monetary Union, were among the best growth performers in Africa. In many WAEMU countries, growth acceleration has helped to pave the way towards the achievement of Sustainable Development Goals which is to be commended. However, public expenditure and notably public investment have remained the main growth driver. This growth pattern has resulted in growing fiscal imbalances and public debt. Meanwhile, reliance on non-concessional loans has increased.

As underlined in the staff's report, we are of the view that growth cannot continue to rely primarily on public spending and that fiscal consolidation has not to be deferred further. In WAEMU's countries where it is needed, we therefore encourage governments to implement growth-friendly fiscal adjustment. Moving forward, the WAEMU convergence criterion, set up at 3 percent of GDP for the fiscal deficit, should be seen as the target to reach, notably in the framework of ongoing IMF programs in WAEMU.

Economic Growth and External Buffers

The WAEMU growth drivers have also pushed the external buffers below the optimal levels that are needed to protect the Union from external shocks. Indeed, regional official reserves have come down to 3.7 months of imports in 2016 from 4.5 months of imports in 2015. We also take note of the staff's simulations which suggest that, without fiscal consolidation, the regional official reserve coverage could decrease to 2 months of imports over the medium term. Since fiscal deficits are a key driver of current account deficit and reserve depletion, strengthening external buffers necessitates to start fiscal consolidation at the monetary Union level.

Regarding the external sector, we note that the staff has encountered difficulties in making an in-depth assessment of the financial account situation. Could staff elaborate on the impediments to such an assessment and on the way BCEAO could help in terms of data gathering?

Downside Risks Weigh on the Outlook

We agree with staff that downside risks have to be taken into consideration, notably in the current context of lower buffers on the fiscal and external sides. The risks of further delay in fiscal consolidation has to be addressed by WAEMU governments. Regarding, the risk associated with the lack of progress in raising public investment efficiency (the second fiscal risk pointed out in the report), we would like staff to provide a dashboard presenting how the Infrastructure Policy Support Initiative is currently implemented in WAEMU, notably regarding the following tools: Public Investment Management Assessment, PIMA; Debt-Investment-Growth (DIG) modeling framework; The PPP Fiscal Risk Assessment Model (P-FRAM).

Regarding external and exogenous risks, we are of the view that the situation in Nigeria could continue to negatively spill over to some WAEMU countries such as Benin, Togo, Niger and Côte d'Ivoire through remittances and exports channels. In that context, we would like the staff to elaborate further on what would be the impacts for neighboring countries of the baseline scenario presented in the Nigeria's Article IV review. Would it possible to get such an assessment during the AFR Regional Briefing scheduled on April 7th?

Still on exogenous risks, we agree with staff that security-related risk remain high in the region.

Financial System Stability and Financial Inclusion

The situation of the banking sector is still challenging, notably in terms of capitalization, asset quality and credit concentration. The regulatory reforms adopted by the regional Council of Ministers in June 2016 aim at addressing those issues and strengthening the banking sector soundness. We agree with staff that enforcing existing prudential regulations, as well as preparing the implementation of the new set of reforms is crucial. Could staff indicate how the IMF is able to support this policy, through ongoing programs or technical assistance tools?

Regarding financial inclusion, the staff's report underlines that WAEMU countries lag behind peer countries. We would be grateful if the staff could provide more details about the impediments to financial inclusion that WAEMU countries have to tackle.

Ms. Horsman and Mr. Hart submitted the following statement:

We thank staff for this interesting report and Mr. Sembene and Mr. N'Sonde for the helpful buff statement. The report indicates that real GDP in the WAEMU region is expected to grow at around 6.5 percent over the next few years, inflation is low and stable, and the external sector is broadly in line with fundamentals. The staff are nevertheless concerned about the decline in reserves and growing public debt, the latter being deemed sustainable but vulnerable to shocks. The staff attribute the current account deficits to both fiscal deficits and a large reduction in the financial account. The recommended policy response focuses heavily on fiscal and structural policy. While this is generally appropriate in the context of a monetary union, we are concerned that there isn't a sufficiently clear discussion of the nature of the decline in reserves, or the rationale for the recommended fiscal anchor.

We believe that the report could have done more to clarify the relative impact of the various factors which are driving the recent decline in reserves. The fiscal deficits, while large, stayed at about the same level since last year. The staff note that other relevant factors include increasing reliance on domestic financing and the BCEAO's generous refinancing operations. In addition, they candidly admit that the large decline in the financial account surplus is not fully understood. It would seem important to get this issue clarified in order to adequately tailor the staff's policy advice. How important are the changes to the financial account for the decline in reserves in 2016? What is the relative impact on reserves of the BCEAO's accommodative refinancing policy, which some banks are using to finance a carry trade? Will the recently-introduced measures be sufficient to address this trend?

That said, we agree with the direction and composition of staff's fiscal policy advice. Clearly a balance needs to be struck between making necessary infrastructure investments while preserving fiscal and debt sustainability over the medium term. In particular, we welcome the emphasis on improving revenues through strengthening capacity, better administration, and widening the tax base. We also agree with the need to enhance governance through better public financial management, strengthened debt management capacity, and efforts to improve public investment efficiency. In light of the significant capacity constraints and security issues in the region, these reforms will likely take some time and require ongoing support and capacity development.

However, as a more general point, we note that staff have internalized the WAEMU convergence criteria into their policy recommendations without much explanation. Could staff elaborate why they view the WAEMU convergence criteria (and specifically the overall regional deficit of 3 percent by 2019) as a necessary target for the region?

Finally, we broadly agree with the rest of the report's recommendations regarding deepening the financial sector, enhancing supervision, and supporting financial inclusion while being mindful of risks to stability. We also agree with the need for significant improvements to the business climate to strengthen overall competitiveness.

Mr. Saraiva, Mr. Bellot and Ms. Florestal submitted the following statement:

We thank staff for the useful annual update on economic achievements and challenges faced by the West African Economic and Monetary Union and Messrs. Sembene and N'Sonde for their insightful buff statement.

Over the last few years, economic activity has been strong in the WAEMU region with a more synchronized growth among countries, inflation under control and fiscal balance anchored by the convergence criterion. Despite an expected pickup in 2017, inflation is likely to remain at low levels by 2021. Overall, staff assesses that the economic outlook remains positive and policies in line with Fund advice. However, vulnerabilities in the financial sector, fragilities in public balances and external problems—such as exposure to commodity prices and neighboring security challenges—could jeopardize macroeconomic and financial stability, undermining growth and poverty reduction. In this context, the strengthening of the financial conditions, the persistence of structural reforms and adequate fiscal policy are crucial to foster inclusive and sustainable economic growth.

Increasing vulnerabilities in the financial sector should be addressed not only by improvements in the macroprudential framework but also by undertaking structural reforms to strengthen the financial system. Reforms aiming at adequately reducing non-performing loans, creating an effective resolution legislation and building financial safety nets would enable the banking industry to expand credit without increasing contingent liabilities to the public sector. Additionally, fostering financial inclusion may contribute to accelerate poverty reduction while dissipating risks of credit concentration. These steps could reduce weaknesses that threaten financial stability and the ability of the financial sector to contribute to the growth and development of the region.

While we acknowledge the ongoing coordinated efforts of regional and national authorities, further steps to alleviate the ailing conditions of the financial system would be welcomed. Whereas existing prudential regulations are not well enforced, stricter prudential measures have just been enacted. Could staff clarify if there are intermediary targets and to what extent state-owned banks contributed to the weakening of financial sector indicators? Therefore, we see merit in taking resolute steps for the enforcement of existing regulations and the strengthening regional financial regulation.

The staff report emphasizes the heightened level of debt vulnerabilities because of increasing reliance on non-concessional loans. Nonetheless, only one country fails to observe the debt to GDP ratio convergence criterion. The report informs that it is the WAEMU authorities' view that fiscal policy was largely determined by Fund-agreed targets. Could staff elaborate on the status of programs with member countries and particularly on issues related to fiscal targets?

Regional reserves decreased at a rapid pace in 2016, but reserve coverage remained above the threshold required by the zone's monetary arrangement with France—although below what staff considers optimal. Additional efforts to rebuild regional reserves would require further monetary tightening and could, as underscored in the staff report, potentially affect growth and particularly private investments which have already been shrinking and displaced by the public sector.

We welcome the authorities' willingness to strengthen revenue mobilization, as pointed by Messrs. Sembene and N'Sonde, while improving public financial and debt management. As a multilateral institution, the Fund is well positioned to propose practical solutions that contribute to building tax capacity. For instance, as the platform for collaboration on tax becomes effective, we wonder whether it could help countries such as WAEMU members to raise revenues by broadening the tax base.

We join the WAEMU authorities and Fund staff in encouraging member countries to implement policies and structural reforms aimed at improving business climate, promoting private investment, boosting competitiveness and fostering diversification. Given the extent and the complicated nature of the problems in the WAEMU financial sector and public financial management, we encourage the Fund to actively seek donor support for technical assistance in its areas of expertise. Going forward, national authorities' resolve and ownership are key to undertake necessary reforms and lay the groundwork for sustained, strong and inclusive growth.

Mr. Palei and Ms. Atamanchuk submitted the following statement:

While the WAEMU continues to enjoy solid growth, vulnerabilities have increased on the account of shrinking external buffers, as well as rising fiscal deficits and public debt levels. The WAEMU authorities should promote inclusive growth and reduce poverty in the WAEMU countries, particularly through strengthening the fiscal frameworks, closing infrastructure gaps, improving the quality of investment, and deepening financial markets. We broadly concur with staff's assessment and recommendations and would like to offer the following comments.

Strong fiscal discipline is crucial for the WAEMU's economic stability. We note that observance of the key fiscal convergence criterion—the overall fiscal balance to GDP ratio—remains challenging, as seven out of eight countries missed it in 2016. In this context, a growth-friendly reduction of non-priority current spending and boosting tax collection should help members reduce deficits and comply with the convergence criterion. We also encourage the authorities to improve the PFM and public investment efficiency.

We would be interested to hear staff's opinion on whether the current criterion on total debt-to-GDP ratio is useful, given that all countries, except one, have public debt ratios substantially below the ceiling of 70 percent of GDP. We recall that a few years ago, staff suggested to lower the criterion on public debt to reduce the risk of debt distress. Comments are welcome. We invite the WAEMU countries' authorities to continue consultations with staff on fiscal recommendations articulated in the report.

Monetary policy has tightened, and inflation remains low. We thank staff for a clear overview of the monetary policy framework (Box 1). We note that staff welcome the December 2016 decision of the BCEAO to increase its credit facility rate. While we agree with staff that tighter monetary stance is appropriate for the WAEMU, we are concerned that the resulting increase in the spread between the minimum bid rate and the credit facility may increase the interbank rate volatility. Comments are welcome.

While we agree with staff's analysis and recommendations on promoting financial stability (paragraphs 15-21), we note that more active financial sector development would improve the effectiveness of the WAEMU macro policies. Relatively shallow financial sector constrains the scope of fiscal policy, as governments face higher borrowing costs, significant rollover risks, and severe limits on the amounts they can raise in the market. It also constrains the efficiency of the transmission mechanism by lowering the path-through of the interest rate and asset price channels. In this regard, further development of the financial sector should become a priority. We would be interested to hear comments on the authorities' plans in this area.

Given the uncertainty and significant downside risks in the external environment outlook discussed in the RAM, regional integration should contribute to growth and competitiveness of the WAEMU countries. The WAEMU members can benefit from promoting regional trade. Are there any discussions within the union on adopting measures to give a new momentum to regional integration?

Mr. Hiroshima and Mr. Shoji submitted the following statement:

We thank staff for the comprehensive report and Mr. Sembene and Mr. N'Sonde for their informative statement. We welcome that the WAEMU shows strong economic growth and low inflation. Meanwhile, we also note the vulnerabilities arising from loose fiscal policies in the country level, uncertain global economy and security risks. As we broadly concur with the thrust of the staff's evaluation and appraisals, we will limit our comments to the following points for emphasis:

Fiscal Policy

We agree with staff that a fiscal policy is the first line of defense and growth-friendly fiscal consolidation is necessary to reduce high fiscal deficits. While we recognize the importance of addressing the infrastructure gap in the region, we also encourage national authorities to well prioritize projects and increase public investment efficiency. While the key WAEMU convergence criteria remain unmet, could the WAEMU Commission consider additional measures to incentivize WAEMU countries to observe these criteria? The staff's comments are welcome.

Monetary Policy

We note that some banks prefer to utilize BCEAO's refinancing to invest government securities but this strategy has contributed to widening fiscal deficits. In this regard, we welcome that the BCEAO recently increased its lending facility rate and introduced a cap on the banks' recourse on the lending facility. Is the additional 100bp increase in lending facility rate at the end of 2016 sufficient to increase transactions in the interbank market and reduce the purchases of government securities? The staff's comments would be appreciated. That said, the recent decision to reduce reserve requirements would offset the effect by the above-mentioned measures.

Financial Sector

A sound banking system is indispensable for facilitating credit to the private sector. In this regard, we welcome the ambitious regulatory reforms agreed by the regional ministerial level, including the adoption of Base II and III capital standards and the tightening of the large exposure limit. Given the high credit concentration risks and gross NPL ratio in the region, we encourage the BCEAO to timely and effectively implement the new regulations.

Mr. Doornbosch and Mr. Clicq submitted the following statement:

We thank staff for the report and Messrs. Sembene and N'Sonde for their helpful statement. The WAEMU region achieved strong economic growth over the last five years, mainly by increasing public investments. To maintain the growth momentum in the medium term, more efforts will be needed to improve the business climate, competitiveness, access to finance and the efficiency of the public investments. We call on the authorities to improve the coordination and consistency between national fiscal policies and regional monetary policy. We share staff's concerns about the recurrent delays in financial consolidation, the rising public debt levels and the shrinking external buffers. We welcome that the authorities broadly agree with the staff's assessment and policy recommendations and offer the following comments for emphasis.

Growth friendly consolidation should not be delayed. The fiscal strategy for the WAEMU authorities should be structured around the following principles: (i) enhancing revenue mobilization, (ii) containing current expenditure and (iii) using the available fiscal space for efficient public investments. There is clear scope for better exploring concessional financing options and developing PPPs to finance large infrastructure works.

Monetary policy needs to become more effective. The staff offers some valuable recommendations on how to develop the interbank market, to better calibrate open market operations and to improve the monetary transmission channels. Will the BCEAO benefit from Fund's TA in these areas?

Enforcing prudential regulations is essential. We are surprised that only 57 of the 102 banks complied with the minimum share capital at the end of June 2016. Can staff provide an update of this figure and comment on the likelihood that banks will meet the new capital requirements by June 2017? We also recommend the WAEMU authorities to fully implement the regional action plan for financial inclusion.

We encourage the WAEMU authorities and institutions to improve the quality, coverage and timeliness of regional data.

Mr. Temiz and Mr. Varga submitted the following statement:

We thank staff for the well-written report and Messrs. Sembene and N'Sonde for their informative buff statement. We would like to emphasize the Fund's important role in stabilizing the WAEMU members' economies, with six of the eight WAEMU members currently under a Fund program.

While real GDP growth among the WAEMU countries has been strong over the last five years, real convergence to the world economy is still lacking. The average annual GDP growth in the WAEMU region was low when juxtaposed against the overall population increase over the same period resulting in the annual GDP per capita growth of only 3.4 percent on average. When excluding the positive performance of Côte d'Ivoire, with the help of favorable commodity prices, both the average nominal and per capita GDP growth were approximately one percent lower for every year.

The fiscal consolidation plans are back loaded and appear beyond reach, given the recent track record. Even if the governments implement their consolidation agenda, seven countries will not meet the WAEMU's three percent budget deficit convergence criterion on the overall fiscal balance until 2019. Moreover, as five countries missed their initial fiscal deficit target for 2016, even this not-very-ambitious consolidation path does not seem feasible. While the reason for the higher deficits was mainly the over-performance in public investment spending, we note that the Fund's earlier work indicated the low effectiveness of such investments for maintaining growth over the medium term in the region. The staff's comments on the effectiveness of the convergence criteria in guiding WAEMU members' fiscal policies, especially in the program countries, are welcome.

We welcome the BCEAO's (Banque Centrale des Etats de l'Afrique de l'Ouest) changes in its lending facilities, which will boost the interbank market and prevent banks from carry trade operations in government bond markets. We note that selected pan-African and local banks are purchasing significant amounts of government securities and are using the BCEAO's lending facilities to finance their balance sheet increase at relatively low cost, with a potential to crowd out private lending. Indeed, private sector credit growth was only 9.7 percent compared to the public sector's 43.9 percent in 2016. Growing concentration and high non-performing loans compound financial vulnerabilities. We encourage the authorities to speed up the work on the common resolution framework and perform asset quality reviews as necessary to mitigate potential risks.

We welcome the recent banking regulatory reforms which would enhance financial stability, improve the role of the interbank market and boost financial inclusion. We welcome the launch of the recent colleges for cross-border banks and the ongoing implementation of Basel II and III capital standards, the introduction of consolidated supervision and the tightening of the large exposure limits. We encourage the authorities to enforce these new regulations rigorously.

Structural reforms are progressing, but more has to be done to achieve long-term sustainable growth. The four countries in the region, which had already completed at least one review under their Fund program, are making encouraging progress in implementing structural benchmarks. These reforms help to improve competitiveness, but the overall progress is much more limited compared to other African peers. We encourage staff to be more rigorous on the follow-up of structural reforms progress during the next reviews.

Mr. Sun and Mr. Fan submitted the following statement:

We thank staff for the comprehensive report and Messrs. Sembene and N'Sonde for the informative buff statement. The WEAMU region has enjoyed high real GDP growth of about 6 percent for five years in a row, albeit with slow progress in fiscal consolidation. We broadly agree with staff's analysis and policy recommendations and would limit our comments to the following.

Improving revenue mobilization and public spending quality is key for a successful fiscal consolidation. Given the economic development stage most WAEMU countries are facing, enhancing efficient public infrastructure spending is necessary to close the infrastructure gap for long-term growth. The WAEMU authorities are encouraged to further improve the quality and efficiency of expenditure, and to avoid squeezing out private investments. We agree that further development of alternative forms of financing is needed to support infrastructure investment. In this regard, promoting public private partnership (PPP) will not only ease fiscal pressure but also improve investment efficiency. Since PPP is widely used in some countries, we encourage the authorities to learn from other countries' experiences. More broadly, it is important to enhance coordination and consistency between national fiscal policies and regional monetary policy, as staff rightly pointed out.

For a monetary union like the WAEMU, enhancing monetary transmission mechanism is crucial for economic integration and financial development. We welcome BCEAO's recent shift in its monetary policy stance which has led to a decrease in banks' refinancing with the central bank, among others. These measures can help reduce market segmentation, contain excess liquidity, and more importantly, deepen financial markets, especially the interbank market in the region. Given that the level of foreign reserves is relatively low, the WAEMU authorities are encouraged to pursue prudent reserve management to build the necessary buffers. In addition, we welcome the measures to diversify the reserve assets, in line with the new SDR basket.

The ambitious regulatory reform agenda needs to be vigorously implemented to ensure financial stability. Adoption of strict capital requirements, notably Basel II and Basel III standards, can improve banks' resilience. In addition, introducing consolidated supervision of cross-border banks and developing an effective regional bank resolution regime are necessary steps to take going forward. While the efforts for financial inclusion, particularly the development of mobile banking, is welcome, upgrading the prudential framework and anti-money laundering system are also important.

Finally, we encourage the authorities to make the newly established deposit insurance fund operational, and we emphasize the importance of enhancing regional infrastructure and the role of structural reforms.

Mr. McDonald, Ms. Pollard and Ms. Medearis submitted the following statement:

The West African Economic and Monetary Union (WAEMU) region sustained its strong headline growth in 2016, but mounting risks overshadow and threaten to reverse the gains of recent years. Large public infrastructure investment being undertaken in many WAEMU countries, while needed to help achieve development goals, has pushed up deficit and debt ratios and delayed fiscal consolidation and critical reforms. We agree with staff and the WAEMU regional authorities that greater coordination and consistency between national fiscal policies and regional monetary policies is needed to ensure regional fiscal and external stability. As such, we would have appreciated a more detailed description of the current and desired mechanisms for policy coordination at the country and monetary union level and the role the Fund can play in promoting such coordination, particularly in the context of Fund programs for WAEMU members.

The staff's baseline outlook—a continuation of roughly 6.5 percent growth over the medium term, with public debt and fiscal and current account deficits peaking this year and declining steeply thereafter—appears overly optimistic. The staff's models demonstrate how a plausible moderation in global growth and a decline in commodity prices (including cocoa) cuts 4 percentage points from this baseline by 2019. Downside risks predominate, per the fan chart on page 11.

Ongoing, larger-than-expected fiscal deficits as a result of delayed adjustment are driving current account deterioration and the sharp decline in reserves. While we agree with staff that the national authorities must not delay fiscal consolidation, the adjustment needs to be well managed at both the national and regional level, with a focus on domestic revenue mobilization and strengthening public financial management and public investment management. We welcome the statement by Messrs. Sembene and N'Sonde that the WAEMU authorities are mindful of the need for fiscal policies to be calibrated to take into account regional external stability considerations.

In this context, the BCEAO, West African Development Bank (BOAD), and WAEMU Commission have an important role to play in supporting fiscal and structural reform efforts at the national level. Lagging structural reforms are impeding private sector-led growth and further depressing members' already poor business climate and competitiveness rankings. We concur with staff that accelerating the pace of structural reforms to improve the business environment and foster greater regional integration (e.g., reducing cumbersome administrative procedures hampering regional trade) will help improve WAEMU economies' competitiveness and resilience.

Given heightened risks to regional debt sustainability illustrated in the DSA, WAEMU authorities needs to monitor closely risks associated with increased reliance on domestic debt, PPPs, and non-concessional borrowing.

In light of the need for consistency between monetary and fiscal policy, and the number of active Fund programs in member countries, both the Fund and BCEAO should work with national authorities to develop plans for improving coordination and consistency between national and regional policies. Despite important differences, such as the degree of commodity-dependence, the experience of the Central African Economic and Monetary Community stands as a relevant example that demonstrates the risk of delayed fiscal adjustment, regional reserve depletion and inadequate reform momentum, and the crucial importance of coordination at the regional level to ensure effective functioning of the monetary union.

It is encouraging to see broad agreement between the BCEAO and staff on recent steps the central bank has taken to tighten monetary policy and stem the deterioration in reserve coverage. Both the staff report and the buff statement of Messrs. Sembene and N'Sonde mention the central banks' intention to improve compliance with regional regulations requiring WAEMU members to repatriate 80 percent of export receipts. Could staff please elaborate on the nature and implications of countries not complying with the requirement, and describe and comment on the effectiveness of the payment and borrowing arrangements set out in WAEMU?

We read with interest Messrs. Sembene and N'Sonde's statement that the WAEMU authorities will diversify reserve assets to currencies offering higher yields. We would be interested in staff's views on this planned diversification.

The BCEAO has taken several significant steps to strengthen financial stability and develop the interbank market over the last year, such as approving a package of regulatory reforms in June 2016, including the adoption of Basel II/III standards, and discouraging banks from freely tapping the exceptional liquidity facility. The interbank market has seen a pickup in activity since the BCEAO increased the lending window spread at end-2016. However, the market remains shallow, limiting the development of capital markets and effective monetary policy transmission. Stability is further undermined by the uneven enforcement of the prudential framework and the slow pace of reform efforts, such as operationalization of the deposit insurance fund and adoption of an effective resolution framework. Could staff elaborate on the challenges to enforcement of existing prudential regulations?

Mr. Sembene made the following statement:

I want to raise one issue that some Directors have raised in their gray statement, which relates to the need for well-coordinated and consistent national fiscal and monetary policies. We fully agree with that need, and I believe the authorities also agree with that need.

The question now is to what extent the Fund should contribute to that outcome. This is the primary responsibility of the national authorities and we fully agree with that. At the same time, the authorities have let the staff know that there is scope for the Fund to play an important role in the context of a program relationship with the various individual members of the West African Economic and Monetary Union (WAEMU). In addition, we have to keep in mind that lack of coordination has many driving factors, but one of the factors has to do with the limited capacity of the regional institution, including the WAEMU Commission and the Central Bank of West African States (BCEAO). The Fund has an important role to play in building those capacities and continuing the useful and helpful policy advice that it has been providing to those institutions. We believe that the Fund can play a big role in ensuring the suitable coordination of fiscal and monetary policies.

The staff representative from the African Department (Mr. Loko), in response to questions and comments from Executive Directors, made the following statement:[1]

> I thank Directors for their insightful comments and questions, which will be helpful as we continue our dialogue with both the regional and national authorities of the WAEMU. We have already provided answers to the more technical questions, so I will elaborate on a few remaining issues.
>
> Directors asked about the coordination between national fiscal policies and the regional monetary policies, and the effectiveness of the surveillance framework. WAEMU countries have committed to harmonizing their fiscal policies through a set of fiscal convergence criteria adopted in January 2015. These criteria, which are expected to be met by 2019, include a fiscal deficit ceiling of 3 percent of GDP, a tax-revenue-to-GDP floor of 20 percent, a wage bill ceiling of 35 percent of GDP, and a public debt ceiling of 70 percent of GDP. Therefore, increasing domestic revenue, controlling the wage bill, and reducing the deficit to 3 percent of GDP by 2019 are important elements in programs with the Fund.
>
> As emphasized in the staff report, regional stability hinges on country-level fiscal consolidation. In the staff's view, current deficit levels are not sustainable, as evidenced by the decline in BCEAO reserves in 2016. Does this mean that 2017 fiscal targets, most of which are reflected in Fund-supported programs, are too high? It does not. Assuming that the countries will be able to tap into more external financing—given that Côte d'Ivoire and Senegal will likely go ahead with the planned bond issuances—reserves should stabilize at 3.5 months of prospective imports in 2017. Hence, country program parameters for 2017 can be maintained. But program discussions will have to make sure that the planned consolidation for 2018 and 2019 is supported by credible measures. Deficits needs to be reduced significantly in 2018 and 2019 to preserve regional financial stability.
>
> Several Directors also asked how to ensure that countries implement their fiscal consolidation plans. As noted by Mr. Sembene, we believe the primary responsibility lies with the countries themselves, with the support of existing regional institutions and mechanisms.

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

Under the existing surveillance framework, the WAEMU Commission is tasked with harmonizing fiscal policies between the eight countries. However, the commission has pointed out on many occasions that it does not have the mandate to enforce fiscal consolidation plans. It is therefore urgent to reinforce the WAEMU Commission and strengthen its capacity to monitor and coordinate national fiscal policies. The Fund can support these efforts. With six out of eight countries currently receiving Fund program support, pending requests from the other two, the Find could help by ensuring consistency between national fiscal policies, as reflected in Fund-supported programs, and regional monetary policy and reserve targets. This will require close coordination between country teams at headquarters before agreeing on national program budget targets with the authorities, taking regional objectives fully into account.

Some Directors inquired about the impact on growth if the WAEMU countries were to return to the planned fiscal consolidation path. To clarify, the baseline scenario already assumes that countries will implement the fiscal consolidation plans in line with the WAEMU criteria. Growth has been so far mostly driven by public investment, but the baseline scenario also assumes that private sector-led growth will pick up on the back of improved business environment. Under this assumption, growth is projected to stay above 6 percent over the medium term.

On monetary policy, some Directors asked about the impact of the increase in the BCEAO lending facility rate on the interbank and the government security markets, and the rationale for lowering the reserve requirements. The increase in the BCEAO's credit facility rate in December 2016 and the tighter access through its lending window have led to a welcome increase in transactions on the interbank market, but also pushed some banks to reduce the balance sheet. It therefore increased the cost of regional financing, providing an incentive for the government to rebalance the financing strategy, while banks are reassessing the portfolio holdings.

The BCEAO decision to limit access to refinancing by banks to a maximum amount of twice a bank's capital starting in June 2017 implies that the banking system will have to reduce the level of refinancing by about CFAF 500 billion before June 2017. On the other hand, development in autonomous liquidity factors, in particular in the decline in net foreign assets, has increased the need for liquidity in the market. Consequently, the authorities decided in March 2017 to reduce the reserve requirement ratio to 3 percent of deposits from 5 percent.

This measure should provide additional liquidity of about CFAF 300 billion to the banking sector, only partially offsetting the tighter refinancing limit. However, the staff estimates that net debt is likely to be larger still since some of the additional liquidity will accrue to banks that already have excess liquidity and were not relying on refinancing in the first place.

Some Directors asked about the staff's assessment of the effects of recent monetary tightening on private sector activity. Monetary tightening could potentially reduce both private and public investment. However, the impact on the private sector in the WAEMU countries is expected to be limited as the banks in liquidity need and that are resorting to refinancing have not been providing significant credit to the private sector. They have engaged in a carry trade by acquiring government paper and benefiting from the interest rate differential. On the other hand, the impact of the government securities market could be important, as shown by the undersubscription of most government security issuances since January 2017.

Finally, on the financial sector, there were questions about the Fund's support for the implementation of the new prudential regulations. The authorities adopted a set of new regulatory reforms in June 2016. The new regulations include the adoption of Basel II and III capital standards and the introduction of consolidated supervision.

Traditional implementation arrangements were also introduced spanning from 2018 until 2022. The contribution of the Fund, mainly through the West Africa Regional Technical Assistance Center (AFRITAC West) center, was critical in assisting the authorities to draft the new prudential regulations. The AFRITAC West center is now helping the authorities to develop application circulars and build the region's supervisory capacity on the new prudential regulations.

Mr. Sembene made the following concluding statement:

I thank the Board and management for their continuous support to the WAEMU region. In particular, I thank the Acting Chair for his personal interest in the region, his participation in the last high-level conference on financial inclusion at the BCEAO was greatly appreciated. I also thank Directors for the quality of the discussions and the valuable recommendations. I will convey these to the authorities. I also want to express my appreciation to the staff, particularly Mr. Loko and his team, for their dedication and valuable policy advice they provided to the WAEMU authorities. They are also to be commended for the comprehensive responses that they have given to Directors' questions.

Turning to the issues raised by Directors, we appreciate the recognition that macroeconomic performance in the WAEMU region has remained strong in recent years. The pegged regime has continued to provide an effective anchor for the members' policies, while reserving macroeconomic stability. Directors have also underscored the fact that emerging vulnerabilities in the region have been noticed, stemming notably from larger-than-expected fiscal deficits, public debt dynamics, and reduced external buffers. It is noteworthy that these vulnerabilities are aggravated by the impact of some exogenous shocks, notably commodity export prices and external security.

The risk to financial sector stability also raised some concerns, notably due to banks' exposure to public sector borrowing. The WAEMU authorities acknowledge the need to pursue their fiscal consolidation plan with a view to safeguarding macroeconomic and external stability and preserving fiscal and debt sustainability.

Given the critical importance of closing the existing infrastructure gaps for improved competitiveness and durable growth, this will require sustained efforts to increase fiscal space, notably by raising domestic revenues, enhancing the quality of public spending, and improving the management and prioritization of public investment. At the same time, the authorities will need to pay due attention to Directors' call for promoting alternative forms of financing, such as public-private partnerships (PPPs), to meet much needed infrastructure investment needs.

There is also ample scope for the regional authorities, particularly the WAEMU Commission, to play an increased role in ensuring that individual country fiscal programs and associated financing plans are sound and consistent with the need to preserve debt sustainability.

Directors and have rightly emphasized the need to improve coordination and consistency between national fiscal policies and the regional monetary policy and financial stability. To this end, the WAEMU authorities, particularly the WAEMU Commission, are mindful of the primary responsibilities in shaping this outcome, and they are determined to continue working closely with national authorities.

But the Fund has an important role to play in this regard, notably through its program engagement with the WAEMU's individual members, but also through policy support and capacity building for regional WAEMU institutions such as the WAEMU Commission and the BCEAO, to help them better perform their respective roles in terms of coordination and harmonization of fiscal policy across WAEMU members, and also to improve consistency between national fiscal policies and regional monetary policy.

The monetary authorities attach high value to preserving the integrity and credibility of the currency union and the peg, which has served their economies well. We welcome the staff's positive assessment of the December 2016 decision of the monetary policy committee of the BCEAO to increase its credit facility weight and tighten access to the refinancing window. Going forward, the authorities will build on the recent decisions and stand ready to take necessary actions to strengthen the external positions recommended by many Directors.

In parallel, the WAEMU authorities—particularly the BCEAO—are committed to accelerating reforms and strengthening the financial regulatory framework, enhancing compliance with prudential norms, improving financial safety nets, continuing to strengthen the monetary transmission mechanism, deepening the interbank and financial markets and operationalizing the regimes.

As well documented in the staff report, and in our statement, several reform actions are already underway to advance these institutional and policy reforms. I would like to assure Directors that it is the intention of the WAEMU authorities to follow through on their ongoing agenda to ensure a strong and well-functioning financial sector.

Finally, I would like to emphasize the importance that the WAEMU authorities accord to advancing regional integration as a source of growth and development. They also indicated their willingness to improve the quality and cooperation of data, as called for by Directors.

In conclusion, I reiterate that the WAEMU authorities look forward to maintaining a close and productive collaboration with the Fund in the institution's core areas of expertise. They continue to count on Fund policy advice and support for their capacity development initiatives, at both the regional and country level.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They welcomed the region's continued strong economic performance, with robust growth and low inflation. Directors noted, however, that risks to public debt sustainability and external stability have risen. They underscored that sustaining high growth would require well-coordinated and consistent national fiscal policies and regional monetary policy to contain vulnerabilities and safeguard macroeconomic stability. While the main responsibility in this regard falls on national and regional authorities, Directors noted that the Fund could play a key role through policy advice and capacity building. Structural reforms will also need to be accelerated to improve the business environment, boost competitiveness, and promote diversification.

Directors underscored that growth-friendly fiscal consolidation is key to reducing public debt and rebuilding foreign reserves buffers. They urged Member countries to adhere to their current budget deficit reduction plans. Directors emphasized that adjustment efforts should be carefully calibrated and should focus on reforms to enhance revenue mobilization and contain current expenditure while protecting priority capital and social spending. They encouraged the authorities to further improve public financial and debt management, enhance spending quality and efficiency, and develop alternative forms of financing to support infrastructure investment while being mindful of associated risks.

Directors supported the current monetary policy stance. They welcomed recent monetary policy decisions to tighten access to the refinancing window. They noted, however, that the lowering of reserve requirements aimed at enhancing liquidity would partly offset the December tightening. Directors called on the authorities to remain vigilant and stand ready to further tighten monetary policy if pressures on external reserves continue. They encouraged them to take steps to further improve liquidity management, energize the interbank market, deepen financial markets, and strengthen monetary policy transmission.

Directors commended the authorities for the ambitious set of regulatory reforms to modernize the financial sector. They highlighted the importance of adequately preparing for the effective implementation of the upgraded regulatory and prudential frameworks, making the financial safety net operational, and developing an effective regional bank resolution regime. They also encouraged the authorities to step up efforts to address the current pockets of vulnerability in the banking system by enforcing existing prudential regulations.

Directors welcomed the new regional action plan and strategy for financial inclusion. They called for its rapid implementation, emphasizing that financial deepening and inclusion are essential to sustain high and inclusive growth. They highlighted the importance of 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.

Directors urged the authorities to intensify the pace of structural reforms to sustain the growth momentum. They called, in particular, for continued efforts to promote private investment, competiveness, and diversification by improving the business environment, reducing barriers to regional trade including cumbersome administrative procedures, and enhancing regional infrastructure.

Directors encouraged the authorities to continue their efforts to improve the quality, coverage, and timeliness of regional data, in particular external sector statistics and financial soundness indicators.

The views expressed by Executive Directors today will form part of the Article IV consultations with individual member countries that take place until the next Board discussion of WAEMU common policies. The next Article IV consultation discussion with the WAEMU regional authorities will be held on the 12-month cycle in accordance with the Executive Board decision on the modalities for surveillance over WAEMU policies.

APPROVAL: February 1, 2018

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook and Risks

1. ***Would like the staff to elaborate further on what would be the impacts for neighboring countries of the baseline scenario presented in the Nigeria's Article IV review. Would it possible to get such an assessment during the AFR Regional Briefing scheduled on April 7th?***

- WAEMU countries, particularly Benin and Niger, are deeply interconnected with Nigeria. Spillovers could occur through different channels including trade, remittances, and the financial sector. The staff estimates that a 1 percentage point lower growth in Nigeria would reduce WAEMU real GDP by 0.2 percent. In the case of Benin, a 1 percentage point reduction in Nigerian growth is associated with 0.3 percentage point reduction in Benin's growth rate.

Fiscal Policy and Debt Sustainability

2. ***Could staff indicate the extent of public support for social protection programs devoted to poverty alleviation?***

- The average share of public expenditure devoted to health spending is about 2.7 percent of GDP and 4.4 percent on education spending. As illustrated in the SIP of last year's Article IV consultation, there is scope for increasing the efficiency of spending. The staff's analysis showed that social spending on WAEMU countries is less efficient than in some peer countries in Africa.

3. ***We would appreciate if staff could give us further information on the instruments available to ensure compliance with convergence criteria and whether they are judged as sufficient.***

- The institutional set up of the WAEMU is adequate for effective policy coordination but there is scope for increasing the effectiveness of the implementation. Governments are expected to approve multi-year programs and submit them to the WAEMU Commission for assessment of consistency with the convergence criteria. The Commission analyses the programs and the realism of their assumptions and provides recommendation on adjustments, if needed. To increase peer pressure, the reports are shared to the Council of WAEMU Ministers, the decision-making body of the union, as well as published on the website of the Commission. Ministry of

Finance share the borrowing plans with BCEAO and coordinate through the WAEMU Securities agency. However, while the Commission is charged with the harmonization of tax policy and monitoring the abidance with the convergence criteria, its ability to influence national decisions on the level of fiscal deficits and source of financing is limited.

4. ***We would welcome staff elaboration on follow-up measures taken by member countries to improve public investment. Are countries also exploring promotion of PPPs to support infrastructure investment, including to enhance regional infrastructure, and putting in place appropriate frameworks to manage risks?***

- Public-private partnerships (PPPs) could represent an alternative form of financing to support infrastructure investment while preserving debt sustainability. There are currently few PPPs projects in Côte d'Ivoire and Senegal, but most WAEMU countries envisage to rely on PPPs in the context of their National Development Plan. The authorities are aware of the risks posed by PPPs and have been working with development partners, including the Fund to put in place the appropriate legal and institutional frameworks as well as adequate accounting and reporting frameworks to promote efficiency and manage risks. In this context, WAEMU countries could benefit from Fund technical assistance to undertake (i) Public Investment Management Assessment (PIMA) of practices and institutional capacity related to public investment management; and (ii) PPP Fiscal Assessment Model (PFRAM) to monitor fiscal risks stemming from PPP projects. A FAD technical assistance mission on PPPs as part of the PFRAM is scheduled in 2017 for Cote d'Ivoire.

5. ***We would like staff to provide a dashboard presenting how the Infrastructure Policy Support Initiative is currently implemented in WAEMU, notably regarding the following tools: Public Investment Management Assessment, PIMA; Debt-Investment-Growth (DIG) modeling framework; The PPP Fiscal Risk Assessment Model (P-FRAM).***

- The Infrastructure Policy Support Initiative (IPSI) instrument is a collection of tools, some still in their pilot phase. All WAEMU countries have participated in PIMA workshops in support of the WAEMU PFM directives. In addition, some these tools have been applied in Cote d'Ivoire (PIMA) as well as Benin, Burkina Faso, Togo (DIG) and Senegal (DIG and PFRAM). We see the IPSI as an important technical assistance input for public investment management reforms, as well as for the discussions of IMF country teams on structural reforms as part of the surveillance process.

6. ***For instance, as the platform for collaboration on tax becomes effective, we wonder whether it could help countries such as WAEMU members to raise revenues by broadening the tax base.***

- Broadening the tax base is critical to improving tax collection and meeting the WAEMU convergence criteria of 20 percent of tax to GDP ratio. In this context, enhancing collaboration and revenue administration will help broaden the tax base, including by reducing tax expenditures, increase revenue and expand fiscal space for much-needed infrastructure and social spending. The IMF has been providing substantial technical assistance to WAEMU countries to strengthen control and revenue administration

7. ***Is the current criterion on total debt-to-GDP is useful, given that all countries, except one, have public debt ratios substantially below the ceiling of 70 percent of GDP? We recall that a few years ago, staff suggested to lower the criterion on public debt to reduce the risk of debt distress.***

- After debt relief, the debt criterion (with a ceiling of 70 percent of GDP) is no longer constraining and may now be high from a debt vulnerability perspective. The 70 percent of debt-to-GDP ratio should be viewed as an upper limit and not an optimal level towards which to converge; and debt management should be driven by regular debt sustainability analyses rather than by the debt criterion. In this context, country teams assess debt sustainability based on the thresholds of the Fund-Bank Debt Sustainability Analysis (DSA) which are lower than the ceiling of 70 percent.

Monetary Policy

8. ***We agree with staff that tighter monetary stance is appropriate for the WAEMU, we are concerned that the resulting increase in the spread between the minimum bid rate and the credit facility may increase the interbank rate volatility. Comments are welcome***

- The optimal width the interest rate corridor depends on the transaction cost in the market. If the corridor is smaller than the transaction costs in the market, banks would only rely on the central bank refinancing facilities. As the WAEMU interbank market remains segmented and underdeveloped, the corridor should be rather large to encourage interbank transactions. The higher spread between the policy rate and the lending rate gave more scope to find the right transaction price on the interbank market and helped restart it. However, to avoid excessive volatility of the interbank rate, the BCEAO must accurately forecast liquidity demand and inject or absorb the appropriate amount of liquidity in its interventions.

9. ***Will the BCEAO benefit from Fund's TA in the areas of enhancing the interbank market and improving monetary transmission?***

- An MCM technical assistance mission took place in January 2017 on the topic of improving monetary policy effectiveness and the Fund is ready to provide more.

10. ***Could staff please elaborate on the nature and implications of countries not complying with the requirement on repatriating export receipts, and describe and comment on the effectiveness of the payment and borrowing arrangements set out in WAEMU?***

- The Treaty of the West African Monetary Union (Article 3) poses the fundamental principle of the pooling of foreign exchange reserves. All WAEMU residents (governments and economic agents) are required to repatriate all foreign exchange proceeds and all banks are obliged to collect and surrender a minimum of 80 percent of all foreign currency proceeds to the BCEAO. Export proceeds need to be repatriated within 1 month of the transaction and accounts in foreign currency (held abroad or domestically) are subject to approval by the Minister of Finance after favorable opinion of the BCEAO. In several member countries, exporting enterprises, notably in oil and mining industries have been allowed to hold foreign exchange accounts abroad by their national authorities. In 2012, the BCEAO implemented a stricter monitoring of export proceeds and repatriation; as a result, the average overall repatriation rate has tripled from 12.8 to 34.3 percent of export proceeds between 2012 to 2015.

External Sector

11. ***How important are the changes to the financial account for the decline in reserves in 2016? What is the relative impact on reserves of the BCEAO's accommodative refinancing policy, which some banks are using to finance a carry trade? Will the recently-introduced measures be sufficient to address this trend?***

- The staff considers the large fiscal deficits as the likely main factor behind the current account deterioration and reserve loss in 2016. At the same time, the financial account is estimated to be weaker due to lower portfolio and other—official and private—investment inflows. In 2016, capital transfers remained stable at about 2 percent of GDP. However, portfolio and other investments (mainly official loans) are expected to decline by almost 4 percent reflecting several factors including lower than anticipated official external loans, and the non-issuance of Eurobonds. Senegal and Cote d'Ivoire issued Eurobonds for US$1.3 billion in 2014 and 1 billion in 2015.

12. ***Could staff elaborate on the impediments to assessing the financial account and the way BCEAO could help in terms of data gathering?***

- The BCEAO— also with Fund technical assistance—has made a very significant progress in terms of data gathering, validation, and analysis. STA is working with the BCEAO on the quality, availability and timeliness of external sector statistics as part of a Japan-funded three-year project to improve External Sector Statistics in 17 Francophone countries in West and Central Africa.

13. ***The staff's comment on the treatment of the monetary arrangement with the French Treasury in the reserves adequacy assessment would be welcome***.

- 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. As in the previous Article IV reports, the staff does not take into account the access to reserves guaranteed by the French Treasury in the reserve adequacy assessment (computation) using standard and alternative metrics.

Financial Sector

14. ***Could staff indicate how the IMF is able to support prudential regulations, through ongoing programs or technical assistance tools?***

- The IMF, mainly through its AFRITAC West (AFW) Center, is helping the authorities further building the region's supervisory capacity on the new prudential regulations through hands-on training, enhancing supervisory procedures and manual, and developing application circulars as needed. AFW contribution was essential in assisting authorities to draft the prudential regulations and is also currently helping in enhancing the risk-based assessment tool used by the region's supervisory authority.

15. ***Could staff clarify if there are intermediary targets and to what extent state-owned banks contributed to the weakening of financial sector indicators?***

- The new prudential regulations will be introduced gradually from 2018 till 2022, which gives banks sufficient time to comply with the new stricter framework. The banks are also expected to provide the BCEAO with a timetable and steps to meet the deadline. Given that many of the weak or problem banks are state-owned, one can preliminarily conclude that they have contributed to the weakening of the financial sector prudential indicators. However, staff was not provided with bank-by-bank information to confirm that conclusion.

16. ***We are surprised that only 57 of the 102 banks complied with the minimum share capital at the end of June 2016. Can staff provide an update of this figure and comment on the likelihood that banks will meet the new capital requirements by June 2017?***

- The compliance rate at end-June 2016 is low but this measure will take effect only in June 2017. The Banking Commission asserted that it is closely following up on this and it expects that most banks will be complying with the new rules by June 2017.

17. ***Further development of the financial sector should become a priority. We would be interested to hear comments on the authorities' plans in this area.***

- Authorities are working on various fronts to further develop the financial sector. They are working towards energizing further the interbank market and promoting further the securities market and its regulation and supervision. They are also addressing weaknesses in microfinance companies and subjecting the large among them to the supervision of the WAMU Banking Commission. In addition, authorities are working further on strengthening the framework for mobile payments. All these efforts and measures clearly signal authorities' commitment to developing the financial sector.

18. ***We would be grateful if the staff could provide more details about the impediments to financial inclusion that WAEMU countries have to tackle.***

- The main impediments to financial inclusion in the WAEMU relate to the high cost of providing financial services, the weak and long legal and judicial processes, and deficiencies in the business environment. This has led to financial access gaps across gender, age, education and income groups.

19. ***Could staff elaborate on the challenges to enforcement of existing prudential regulations?***

- The main challenges are the ability of WAMU Banking Commission to take more timely corrective measures to address banking problems, and the difficulties of coordinating decisions between regional and national authorities to limit financial stability risks. To help overcome these challenges, the authorities are developing a regional resolution framework with robust resolution powers and independence.

Structural Reforms

20. ***We would appreciate if staff could give us further insights on the specific measures/reforms which would have a higher pay-off.***

- Structural competitiveness indicators show some improvement, but still indicate significant bottlenecks in registering property, dealing with construction permits, getting credit and electricity, paying taxes, etc.The region's lagging infrastructure, high costs of inputs such as communication, transport and electricity are also hampering competitiveness in the WAEMU. The staff previous analyses indicate that the actions aiming at improving challenging business, regulatory, and legal environments, reducing substantial infrastructure gaps, increasing structural transformation and innovation, and enhancing institutional and public investment management capacities are associated with the larger productivity pay-offs for WAEMU region. To increase competitiveness, countries will need to not only ensure macroeconomic stability but also improve the business climate, reduce the hard infrastructure gap, and invest in soft infrastructure such as skills and technology. Structural transformation is needed and would require strengthening agricultural programs and promoting exports with both regional and global value chains.

21. ***Are there any discussions within the union on adopting measures to give a new momentum to regional integration?***

- Discussion on how to further promote regional integration are always on-going including within WAEMU. In order to further promote regional integration in WAEMU, several regional infrastructure projects (rail, highways) are in the pipeline.