EXECUTIVE BOARD MEETING

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March 13, 2018

To:	Members of the Executive Board
From:	The Secretary
Subject:	**West African Economic and Monetary Union—Staff Report on Common Policies of Member Countries**

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***Unless an objection from the authorities is received prior to the conclusion of the Board's consideration, the document will be published.**

INTERNATIONAL MONETARY FUND

WEST AFRICAN ECONOMIC AND MONETARY UNION

STAFF REPORT ON COMMON POLICIES OF MEMBER COUNTRIES

March 12, 2018

KEY ISSUES

Context. Economic activity remained strong in 2017 but vulnerabilities persisted despite monetary policy tightening. Fiscal and external current account deficits widened and public debt became more burdensome, while international reserves rebounded somewhat following sizable Eurobond issues. Important steps were undertaken to improve financial stability, including through the move to a prudential regime in line with Basle II/III, but more needs to be done to bring banks to strengthen their capital and liquidity buffers and reduce concentration risk. The medium-term outlook remains positive provided planned fiscal consolidation and structural reforms are implemented. Risks to the outlook relate to further delays in fiscal adjustment, which would jeopardize debt sustainability and external viability, as well as lackluster structural reform implementation which would threaten the growth momentum. Other downside risks entail adverse terms of trade and weather shocks, a global growth slowdown, tighter international financing conditions and a volatile security situation. The materialization of such risks would call for timely and well-coordinated national and regional policy responses.

Policy Recommendations

- **Fiscal and monetary policy**. Growth-friendly fiscal consolidation is essential to lower public debt, lift pressures on international reserves, and preserve external viability over the medium term. The regional central bank should stand ready to further tighten monetary policy in case pressures persist on the money market and on foreign exchange reserves.
- **Financial sector.** The short-term refinancing of sovereign bonds has constrained monetary policy in 2017 and it will be important to restore room for monetary policy to backstop financial stability. To this end, the authorities should use bank supervision and resolution tools to improve bank balance sheets and resolve fragile banks.
- **Competitiveness and diversification.** Structural policies aimed at improving competitiveness and fostering regional integration are critical to making the growth momentum sustainable and more inclusive.

Approved By
Roger Nord and Johannes Wiegand

Discussions were held in Ouagadougou, Lomé, Abidjan, and Dakar during January 11–24. The staff team comprised Mr. Ghura (head), Messrs. Balima, Féler, Gorbanyov, Versailles (all AFR) and Mr. Khallouf (MCM). The mission was assisted by Mmes. Diouf and Sancak (resident representatives in Burkina Faso and Senegal), Messrs. Gijon and Tapsoba (resident representatives in Côte d'Ivoire and Togo), and Mr. Lemarchand (Afritac-West). Messrs. Nord (AFR), N'Sondé (OED), and Barhoumi (resident representatives in Benin) participated in the meetings with the BCEAO in Dakar.

The West African Economic and Monetary Union (WAEMU) and the West African Monetary Union (WAMU) cover the same eight countries: Benin, Burkina Faso, Côte d'Ivoire, Guinea- Bissau, Mali, Niger, Senegal, and Togo. They share the same currency, the CFA franc (XOF), which is pegged to the euro.

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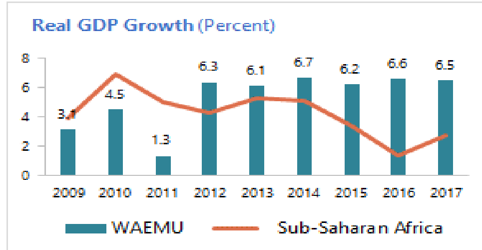
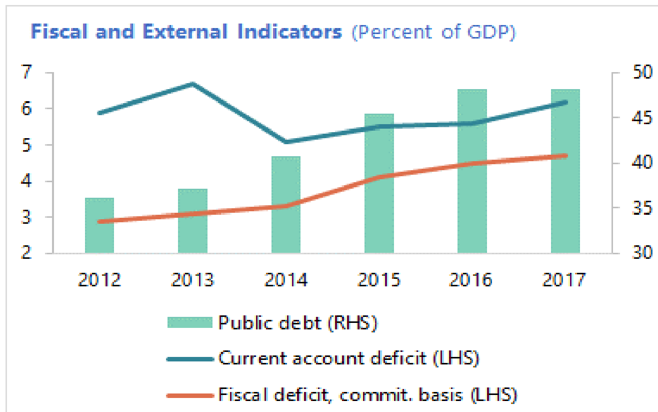
CONTEXT: ROBUST GROWTH BUT INCREASING VULNERABILITIES

1. **The WAEMU has been one of the fastest growing regions in sub-Saharan Africa (SSA) in recent years.** Despite lower terms of trade, social tensions, and security challenges within the region, the WAEMU's real GDP growth rate is estimated to have exceeded 6 percent in 2017 with subdued inflation for the sixth consecutive year, compared to an average of 3.7 percent for SSA.



Real GDP Growth (Percent)

2. **Internal and external imbalances widened despite monetary policy tightening.** Sustained public spending, notably to address infrastructure gaps, has supported domestic demand but also contributed to fiscal and external current account deficits and rising public debt burdens. Tighter monetary policy by the BCEAO[1] helped curb banks' holdings of public securities, and the ensuing pressures on the regional debt market were eased by a shift towards external financing of fiscal deficits. Macroeconomic imbalances maintained pressures on international reserves, which nonetheless recovered part of their 2016 drop owing to sizable Eurobonds issues.



Fiscal and External Indicators (Percent of GDP)

3. **Policies have been broadly in line with past Fund advice, although implementation in some areas has lagged (Annex I).** The curbing by the BCEAO of its refinancing in 2017 boosted activity on the interbank market. Important steps were also undertaken to promote financial stability, including through the move to Basle II/III prudential standards, the introduction of a new banking chart of account and a new framework for the resolution of ailing banks, and the completion of stress tests. Nonetheless, conditions in the banking system remain somewhat challenging. Credit and concentration risks are important and the gross non-performing loan ratio remains high while some troubled banks remain unresolved. At the national level, there has been no progress on fiscal consolidation. In addition, limited improvements in the business climate continue to hamper the region's competitiveness and private sector development.

[1] The BCEAO (*Banque Centrale des Etats de l'Afrique de l'Ouest*) is the WAMU's central bank and the WAMU Banking Commission is the financial sector supervisor. The WAEMU Commission and the BOAD (*Banque Ouest Africaine de Développement*) focus on economic integration and development of the WAEMU.

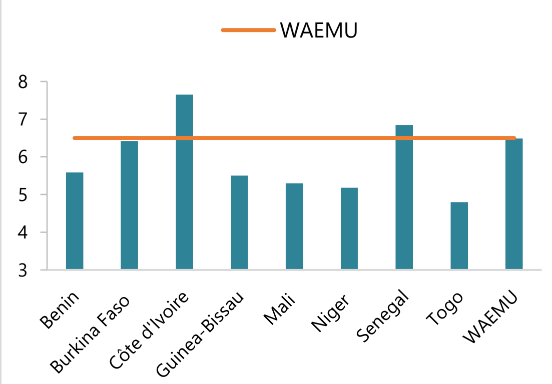
RECENT ECONOMIC DEVELOPMENTS, OUTLOOK AND RISKS

A. Recent Developments

4. Economic activity remained strong though vulnerabilities persist:

- **Strong economic growth continued in 2017**. Despite unfavorable terms of trade, social tensions, and security challenges, WAEMU's economic growth is estimated at 6.5 percent in 2017, driven mainly by domestic demand, including public investment. Growth was above the regional average in Côte d'Ivoire, the WAEMU's largest economy, and the lowest in Togo partly due to the adverse impact of social tensions.

Real GDP Growth in 2017 (Percent)



- **Inflation has remained subdued.** The low inflation in 2017 of 0.8 percent benefitted from higher domestic agricultural production.

- **Fiscal deficits remained high.** The aggregate fiscal deficit (on a commitment basis) is estimated at 4.7 percent of GDP in 2017, compared to 4.5 percent of GDP in 2016. The widening deficit reflected the fiscal accomodation by Côte d'Ivoire in response to terms-of-trade and social shocks, but also difficulties by WAEMU governments to raise revenue yields and contain public expenditure amidst large development needs.

- **The interest cost of public debt rose.** The public debt burden at end-2017 is estimated to have remained at its end-2016 level of about 48 percent of GDP, as the contribution of the fiscal deficits was offset by the impact of strong nominal GDP growth and valuation effects due to the appreciation of the Euro (to which the CFAF is pegged) relative to the U.S. dollar. Interest payments as a share of revenue, however, rose to an estimated 8.6 percent in 2017 (from 8.1 percent in 2016). This said, the latest DSAs for WAEMU countries show that risks of debt distress have remained either low (Senegal) or moderate (all other WAEMU members) since the 2017 Article IV regional consultation.

- **Monetary policy was tightened.** In December 2016, the BCEAO doubled the spread between its policy rate and the marginal credit facility rate (to 200 basis points) and limited banks' access to its credit facility to twice their regulatory capital. However, in March 2017 the BCEAO lowered the bank required reserves ratio from 5 percent to 3 percent, which eased liquidity constraints somewhat. Overall, monetary policy was tightened by the BCEAO's actions as indicated by the interbank market rate hike. These actions also stimulated the interbank market, reduced banks' appetite for government debt, and contributed to the decisions by the two largest WAEMU sovereigns to tap the Eurobond markets for deficit financing. These Eurobond issues together with the one by the BOAD, contributed to a 10.3 percent growth in net foreign assets, while the growth of broad money (M2) slowed to 7.5 percent in 2017 (from 10.7 percent in 2016). Since September 2017, however, renewed liquidity pressures have pushed up the interbank market rate and maintained the average refinancing rate at the ceiling of the BCEAO's policy corridor.

- **The external current account deficit widened in 2017.** Reflecting deteriorated terms-of-trade and public saving-investment balances, the current account deficit (including grants) is estimated to have reached 6 percent of GDP in 2017. Nonetheless, the EBA-lite assessment shows that WAEMU's real exchange rate is broadly in line with fundamentals despite the strengthening of the Euro (and thus the CFA franc) against the U.S. dollar and deteriorated terms-of-trade (Annex II).

- **External buffers have increased somewhat due to sizable Eurobond issues.** External reserves increased by CFAF 655 billion (US$1.2 billion) to reach CFAF 7,184 billion (US$13.1 billion) at end-2017. This increase made up for about two thirds of the CFAF 993 billion loss incurred in 2016, as the bulk of net capital inflows in 2017, including US$3.1 billion in net proceeds from the Eurobonds issued by Côte d'Ivoire, Senegal and the BOAD helped to finance the wider external current account deficit. External reserves' cover of prospective extra-regional imports of goods and services is estimated to have increased from 4.0 months at end 2016 to 4.2 months at end 2017.

Gross International Reserves (Billions of CFAF)

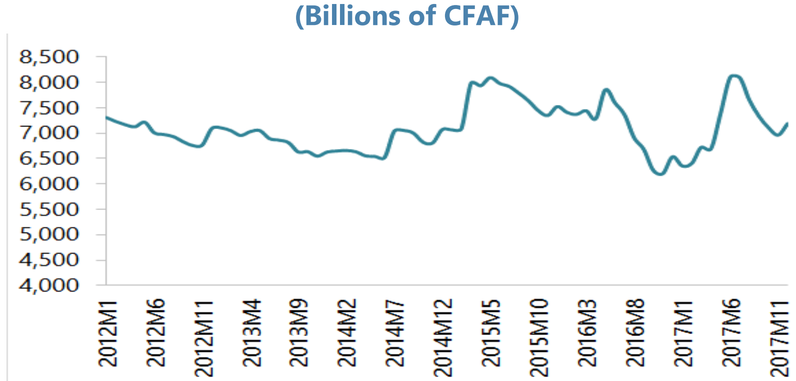
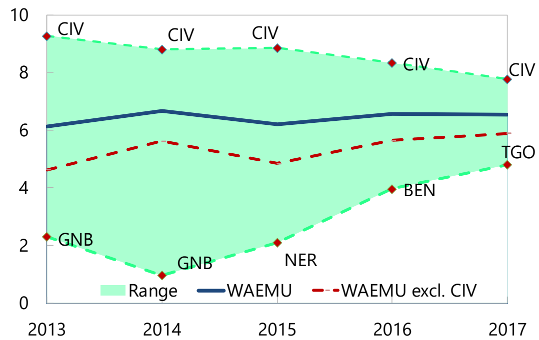


Figure 1. WAEMU: Recent Economic Developments

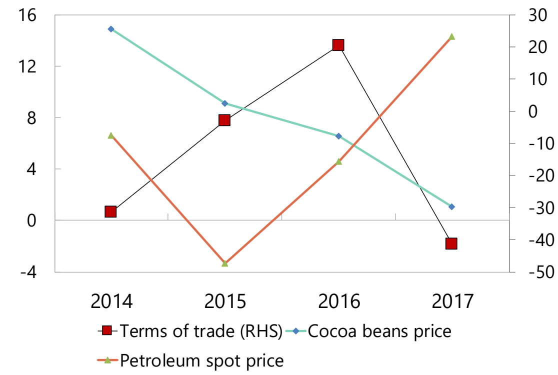
Economic activity has remained strong in 2017 ...

Real GDP Growth
(Annual, Percent)



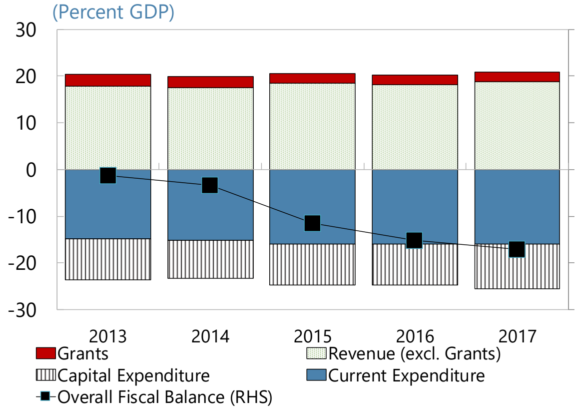
... despite a terms of trade decline.

Terms of Trade
(Annual Changes, Percent)



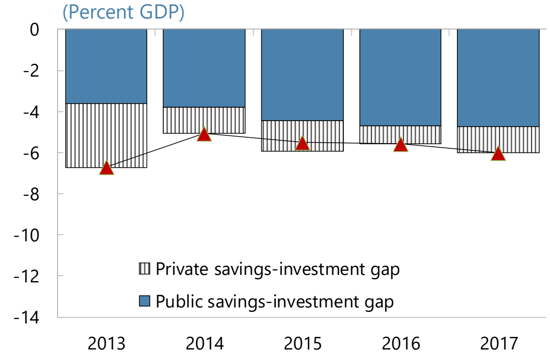
Ongoing capital expenditures have kept the fiscal deficit high ...

Overall Fiscal Balance and Components
(Percent GDP)



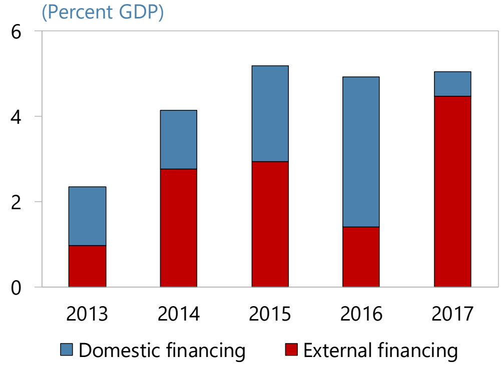
... thus widening the current account deficit.

Drivers of the Current Account
(Percent GDP)



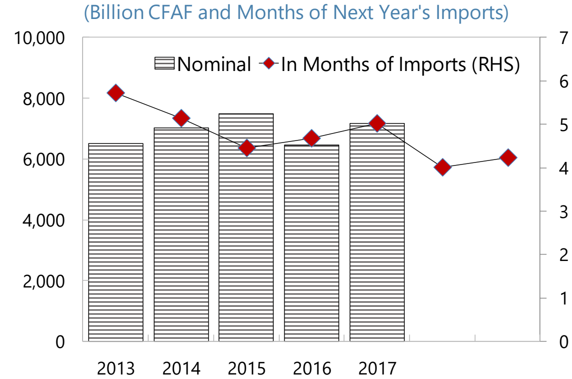
A switch in the fiscal financing ...

Fiscal Financing
(Percent GDP)



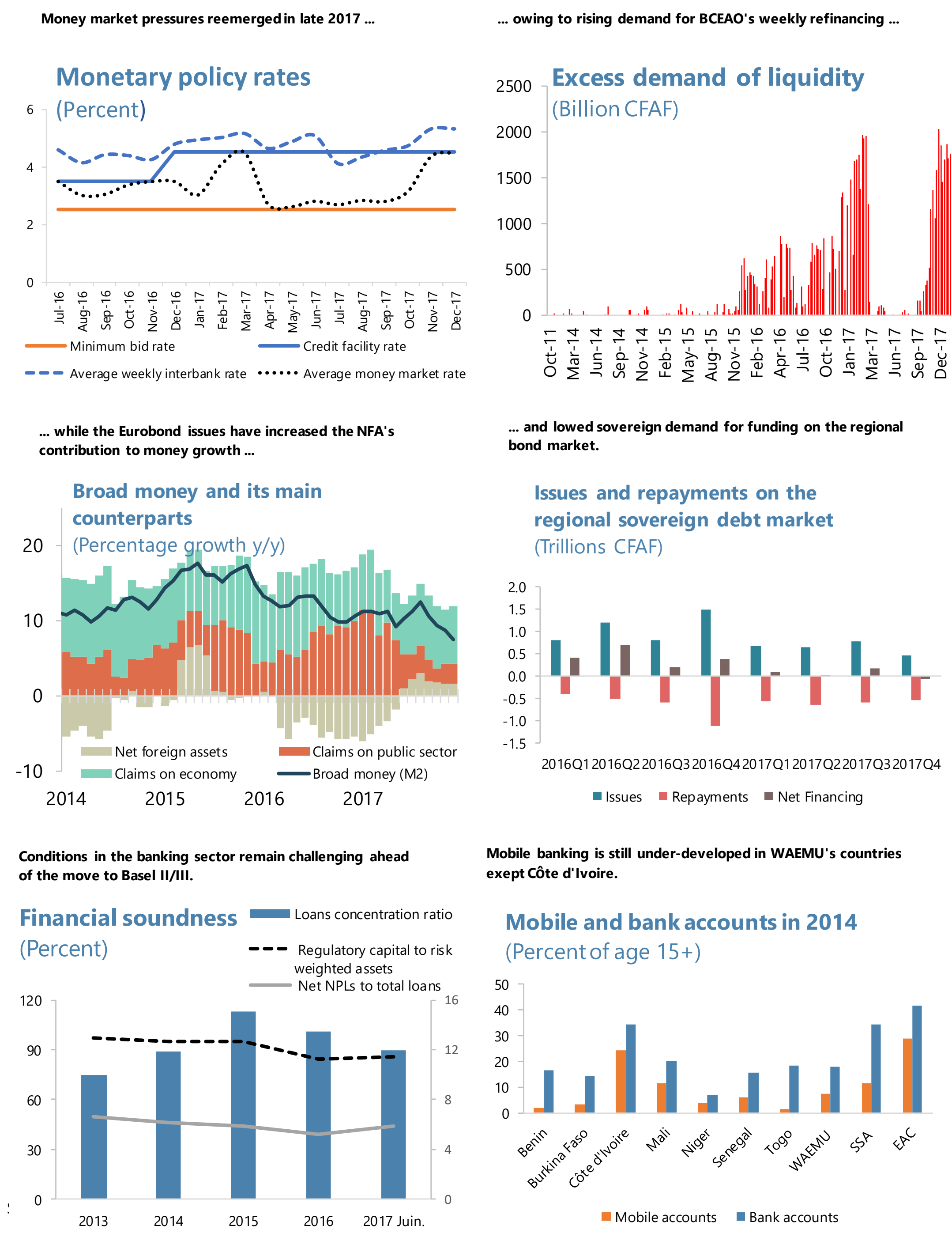
... has helped a slight increase in reserves in 2017.

Gross International Reserves
(Billion CFAF and Months of Next Year's Imports)



Sources: BCEAO; and IMF staff calculations.

Figure 2. WAEMU: Recent Financial Sector Developments



Sources: WAEMU authorities; and Global Mobile Money Dataset.

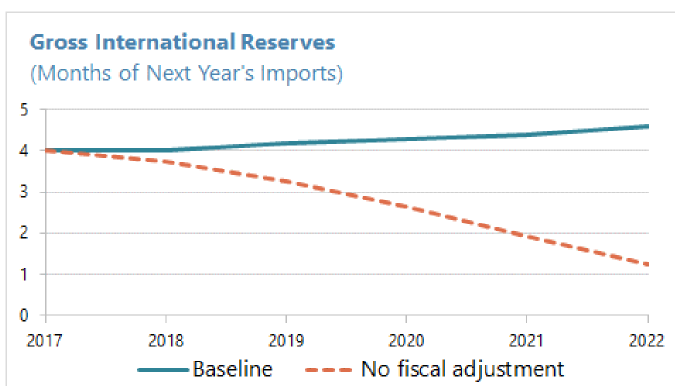
B. Outlook and Risks

5. The medium-term outlook is positive, but hinges crucially on planned fiscal consolidation and decisive implementation of structural reforms by member countries. The region's GDP growth is projected to stay above 6 percent with continued low inflation over the medium term. The baseline projections reflect the commitments by all WAEMU countries, except Niger, to lower their fiscal deficits to within the WAEMU's convergence criterion of 3 percent of GDP by 2019 in the context of Fund supported programs.[2] As a result, the aggregate fiscal deficit for the currency union would decline to 4 percent of GDP in 2018 and 2.9 percent in 2019, allowing public debt to decrease to 45.8 percent of GDP over the medium term. After rising in 2018 due to unfavorable terms-of-trade and public investment drives, the external current account deficit is projected to gradually decline over the medium term, reaching about 5 percent of GDP by 2022 (Figure 3).

6. External reserves would recover, but remain somewhat below optimal levels. Assuming that the current account deficit continues to be financed by FDI and other investments, international reserves are projected to gradually increase to 4.6 months of imports by 2022. Over the medium term, the ratio of external reserves to base money would remain well above the 20 percent threshold required by the monetary arrangement with France. Staff estimates suggest that WAEMU external reserves should ideally be within a range of 5 to 7 months of prospective extra-regional imports of goods and services (Annex III).

7. Risks to the outlook are mainly on the downside and their materialization could jeopardize the growth momentum and external viability (Annex IV):

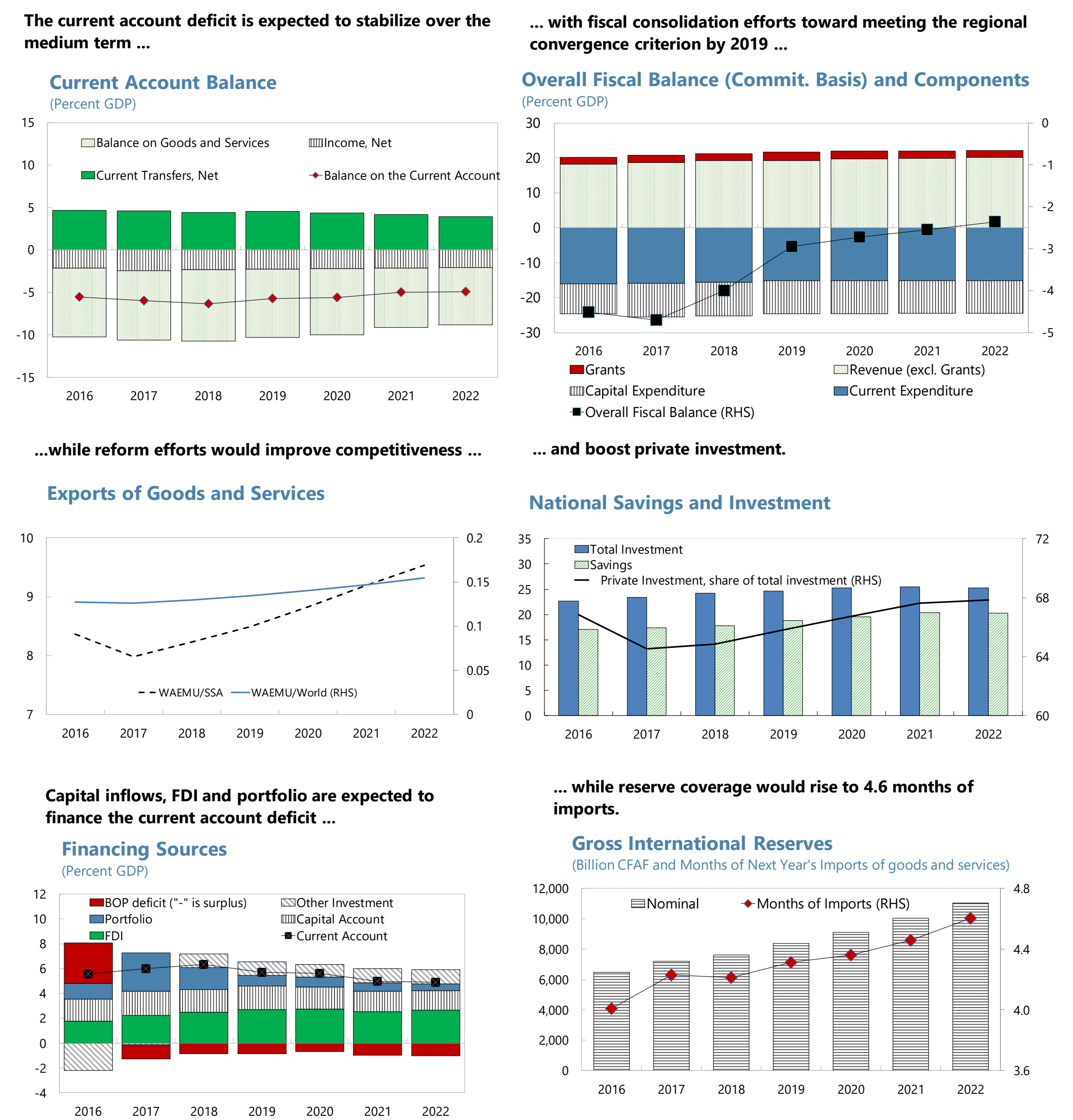
- *Fiscal consolidation delays*. Risks of fiscal slippages in several WAEMU countries reflect spending pressures from social demands and security concerns, as well as slower-than-projected pace of revenue mobilization. Further slippages in fiscal consolidation plans would raise public debt and servicing costs and widen the external current account deficit, potentially jeopardizing external stability. Staff simulations indicate that if national fiscal deficits remained at their 2017 levels, foreign reserves would fall to less than two months of imports by 2022, compared to the baseline projection of 4.6 months (text chart). It is therefore important to respond promptly to



[2] Niger has committed to bringing its budget deficit to 3 percent of GDP by 2021 under its Fund-supported program.

any emerging fiscal slippage with steps to reinforce budget management and accelerate revenue mobilization. Such slippages could also require steps to tighten monetary policy and adjust the external-domestic financing mix with a view to limiting the risks of tensions on the regional sovereign debt market.

Figure 3. WAEMU: Medium-Term Prospects



Sources: BCEAO; World Economic Outlook; and IMF staff calculations.

- *Delays in the implementation of the structural reforms* could hamper the private sector from playing a larger role as the engine of growth.

- *Persistent security problems in the region* could weaken fiscal positions, reduce foreign direct investment and delay the implementation of major projects.

- *Higher international oil prices* would adversely impact the external current account as the WAEMU is a net oil importer. The impact on inflation and budget deficits would depend on how much the oil price increase is passed through to domestic petroleum prices.

- *A tightening of financing conditions at the international level and a slowdown in world growth* could also affect the economies of the region. The WAEMU's exposure to global financial markets has increased due to Eurobond issuances by its two largest countries and the BOAD. Monetary policy normalizations in Europe and USA could translate into higher regional risk premia and reduced external financing. The latter could compound reserves pressures, as would lower-than-projected exports. In addition, a materialization of downside risks to the current global recovery could hamper growth in the WAEMU through the terms-of-trade, remittances, and FDI channels.

8. **Authorities' views**: The regional authorities broadly agreed with staff views on the outlook and risks. They were particularly concerned about potential fiscal slippages—owing to pressures from security spending and lackluster revenue mobilization—and their impact on reserves and public debt sustainability. The authorities noted the vulnerability of the WAEMU to adverse changes in climatic conditions, given the importance of the primary sector activities in member countries. They agreed that, should downside risks materialize, fiscal adjustment and further monetary policy tightening, along with adjustment in the external/domestic financing mix, will be required to preserve external viability. Staff and the regional authorities concurred on the need to step up efforts to rebuild policy buffers to avoid the need for abrupt policy responses, should downside risks materialize.

POLICY DISCUSSIONS

Sustaining the growth momentum and the currency peg will require continued macroeconomic stability, anchored on credible fiscal consolidation, appropriate monetary policy, and accelerated structural reforms to promote financial stability and competitiveness.

A. Macroeconomic Policies: Sustaining the Growth Momentum While Preserving Debt Sustainability and External Stability

Background

9. **The growth momentum of recent years has been accompanied by an erosion of policy buffers.** Growth has been largely driven by domestic demand, particularly public

investment. As a result, internal and external balances have been widening. Securities challenges within the region combined with wage demands have increased pressures on government spending, while the fiscal space has remained limited and public debt service has increased in several member countries. The persistence of large fiscal and external current account deficits has maintained pressure on foreign exchange reserves.

Staff's Recommendations

10. International reserves should increase to provide higher buffers against shocks. The recovery in reserves in 2017 masks continued underlying pressures on reserves, which would have continued their slide that started in 2016 were it not for the extraordinary level of Eurobond issues in 2017. This warrants a reinforced effort to strengthen external competitiveness through structural reforms and reduce fiscal imbalances to build reserves towards at least 5 months of import cover.

11. Growth-friendly fiscal consolidation is needed to lower public debt and lift pressures on monetary policy and reserves. Effective fiscal consolidation is essential to preserving external viability over the medium term. It must also be supported by a more comprehensive accounting for risks to fiscal and debt sustainability, stronger regional surveillance efforts, and improved debt management. Staff urged the authorities to pursue the following policy priorities:

- Building fiscal space: Governments should bolster revenues and prioritize spending to meet the WAEMU fiscal deficit criterion of 3 percent of GDP by 2019 and beyond while creating fiscal space for priority infrastructure and social spending. In the event of deviations from current program targets, additional fiscal measures would be needed. Tax policy measures could include hiking rates on excises, VAT on exempted products and real property tax, and reducing the scope for tax exemptions. Spending measures could include bringing wage bills within 35 percent of domestic revenue (WAEMU convergence criterion) and better targeting subsidies and social assistance to protect the most vulnerable. Several key WAEMU convergence criteria remain unobserved, and current projections suggest that breaches will persist for second-order criteria in most countries over the medium term. The mission encouraged the WAEMU Commission to

Text Table 1. WAEMU: Number of Countries Violating Convergence Criteria 2015-22

	2015	2016	2017	2018	2019	2020	2021	2022
			Est.	Projections				
First-order criteria								
Overal Balance/GDP (≥ -3 percent)	5	8	5	6	1	1	0	0
Average consumer price inflation (≤3 percent)	0	0	0	0	0	0	0	0
Total debt/GDP (≤ 70 percent)	1	1	1	1	0	0	0	0
Second-order criteria								
Wages and salaries/tax revenue (≤ 35 percent)	6	6	6	6	5	5	4	4
Tax revenue/GDP (≥ 20 percent)	8	7	7	7	7	7	7	7

Sources: WAEMU; BCEAO; and IMF staff estimates and projections.

increase dissemination of the Union countries' convergence criteria efforts and bring its views of fiscal risks to the attention of the next meeting of the WAEMU Head of States.

- Capturing fiscal risks: Governments should expand the fiscal account coverage and implement the WAEMU Directive on the transition to the GFSM 2001 fiscal reporting standards. There is also a need to better capture contingent liabilities arising from troubled public entities, including banks, and from increasing recourse to PPPs.[3]

- Increasing the efficiency of public investment: WAEMU member governments should improve public investment management, focusing on priority areas identified by recent PIMA missions, such as the planning and selection of public-private partnerships, the preparation of multiyear budgeting, the effectiveness of project appraisal and selection, the monitoring of project during implementation, and the accounting of infrastructure assets.[4]

- Strengthening debt coverage and management: With rising public debt in recent years, the authorities should closely monitor all public contracted and guaranteed debt, including by widening coverage to state-owned enterprises and refraining from pre financing operations. WAEMU sovereigns should continue to seek the best possible terms on new borrowings, with a view to limiting debt service costs and FX risks. Issuing Eurobonds in euros (to which the CFA franc is pegged), including for liability management, would lower FX risks. While not a substitute for the criticality of lowering the fiscal deficits to improve the regional FX reserves, Eurobonds could contribute to the latter.

12. While national fiscal policies must deliver the necessary deficit reductions, monetary conditions should be tightened if external pressures persist:

- The BCEAO should stand ready to further tighten monetary policy in case the pressures persisted on the money market and on foreign exchange reserves.

- The BCEAO should steer liquidity based on autonomous factors[5] while gradually reducing the banking system's dependence on central bank refinancing. It must also monitor closely some banks that engaged in the sovereign debt carry trade and in need of significant deleveraging, while raising their capital and liquidity buffers. However, with an underdeveloped secondary debt market, those banks may find it difficult to reduce

[3] The sources of fiscal risks in the WAEMU are covered in an accompanying Selected Issues Paper.

[4] See the chapter on Improving Public Investment in the WAEMU in an accompanying Selected Issues Paper.

[5] Autonomous factors are the items in the BCEAO's balance sheet that have an impact on banks' reserves at the BCEAO (also called "banking sector liquidity"), which are not under the control of the BCEAO. These include currency in circulation outside banks, governments' deposits at the BCEAO, and the BCEAO's net foreign assets, and other items net.

rapidly their sovereign exposures, which could effectively prevent a rapid retraction of central bank liquidity.

13. The BCEAO should further improve the functioning of the interbank money market. Transaction volumes on this market remain small even after having doubled in 2017. Some reforms underway such as the creation of a repo contract framework should help develop a more dynamic market on which liquidity would be actively transacted between banking groups. Importantly, the new Basel II/III prudential regime should improve balance sheets and the evaluation of counterparty credit risks, which would stimulate interbank transactions. In the future, the BCEAO should calibrate its liquidity injections depending on the interbank market situation and steer the average interbank rate into its monetary policy corridor.

14. To improve monetary policy transmission and support the development of the interbank market, the authorities should eliminate the current fragmentation of the debt securities market. Sovereign issues are currently supervised and deposited in two separate market clusters, depending on their issuance mode, i.e., auction or syndication (Annex V). Achieving an integrated bond market and the fungibility of securities for each issuer would help develop active secondary trading, which is essential in turn to get robust yield curves and to price sovereign risks. It would be vital also to broaden the investor base, notably to non-bank institutional investors who could contribute further depth and market liquidity. Staff suggested that the BCEAO consider applying different discounts to government securities pledged as collateral for central bank refinancing, based on an assessment of each sovereign's credit risk. Such risk could be determined based on debt sustainability and WAEMU convergence criteria.

Authorities' Views

15. The regional authorities concurred that widening macroeconomic imbalances have been fueled by high fiscal deficits. They therefore intend to keep alerting member governments of the need for an effective implementation of their fiscal adjustment plans in line with regional convergence criteria. The regional authorities however also pointed to the significant implementation risks of these plans, and underscored the important role of current IMF supported programs in helping reduce such risks. The authorities concurred on the need to better capture fiscal risks and noted with satisfaction the recovery of international reserves in 2017 while acknowledging that this was made possible by issuances of Eurobonds. The BCEAO agreed that external buffers need to be consolidated over the medium, and indicated that achieving this objective would depend on the effectiveness of its efforts to improve compliance with the regulations on repatriation of export receipts.

16. The BCEAO broadly agreed with staff on the need for monetary policy adjustment in case of renewed pressures on the money market or reserves. Notwithstanding the current low inflation environment, the BCEAO concurred with staff that renewed pressures on external reserves or sustained excess demand for refinancing would warrant monetary policy action. To help ease liquidity tensions in the money market, the BCEAO strongly called upon banks exhibiting liquidity shortages to increase their capital and liquidity buffers while appropriately deleveraging by mid-2018. The BCEAO had reservations about the suggested application of different discounts to government securities pledged as collateral for central bank refinancing for two main reasons. First, it considered that this would be inconsistent with the principle under current prudential regulations which treats equally member governments on sovereign risk weights. Second, it argued that the BCEAO would overstep its role by applying differentiated discounts to government securities pledged by banks for central bank refinancing, noting that each bank needed to undertake its own assessment of sovereign risk of member states, based on economic and financial information available before each government security issuance. The BCEAO thus considered that it should not directly influence the credit risk taken by banks when purchasing government securities.

B. Promoting Financial Stability and Inclusion

Background

17. Progress has been made by WAEMU countries on financial development and inclusion, although they still lag their peers. Mobile payments have picked up in recent years and should help large segments of the population participate in the market economy. Monitoring committees were put in place at the national and regional levels in 2017 for implementation of the regional strategy for the promotion of financial inclusion approved in June 2016 by the WAEMU's Council of Ministers. The implementation of this strategy is expected to benefit from financial support from bilateral and multilateral donors starting in 2018, as well as technical assistance from the World Bank.

18. The banking system is stable and profitable overall, though there are pockets of vulnerabilities.[6] The overall capital adequacy ratio (CAR) for the sector under Basel I was 11.4 percent at mid-2017, indicating that large groups are stable and sound. However, some banks remain under-capitalized, while several smaller banks had not met the minimum social capital of FCFA 10 billion required at end-June 2017. The authorities have asked banks to comply with their capital obligations at end-June 2018, and are closely monitoring some of these banks, expected to rebalance their assets and resources by raising additional capital and/or deleveraging.

19. The quality and funding structure of assets exhibit weaknesses. Banks' exposures to sovereign debts have been often funded on short-term central bank refinancing, exposing banks to the risk of tighter monetary conditions. Banks also exhibit a high risk concentration, with exposures to top 5 borrowers reaching 90 percent of equity at end-June 2017. At 15 percent of total loans at end-June 2017, gross NPLs remain elevated, although they are covered by provisions for two-thirds. Stress-tests run by the BCEAO have confirmed that equity would be adversely affected in the event of a strong shock on credit quality. In addition, a few non-profitable banks, mostly public institutions, report negative equity. Two state-owned banks

[6] See chapter on WAEMU's banking system in an accompanying Selected Issues Paper.

in Togo and a private one in Guinea Bissau are of national systemic importance and should be resolved.

20. The regional supervisory authorities (Banking Commission) are implementing essential financial reforms.

- Prudential regulation has moved to Basel II/III standards in January 2018, with changes phased in over a five-year period, which would bring a more risk-sensitive and better quality capital coverage. Banks should have capital in excess of 8.6 percent of risk-weighted assets at end-2018. Banks have been prepared by policymakers and supervisors to ensure compliance.

- Bank supervision is shifting to a more risk-based and consolidated approach. The Banking Commission is adopting new criteria in line with Pillar 2 of Basel standards. It has launched the consolidated supervision of cross-border groups and has readied its tools to that end.

- The Banking Commission has been endowed with new resolution powers in late 2017. The amendment to the Banking Commission's Statutes ensures that all member countries are committed to cooperate with this institution, based on its independent resolution decision-making. That should permit actual progress on the resolution of banks with persisting negative equity.

21. The authorities are rolling out a financial safety net to protect against systemic risk. This safety net includes: (i) a financial guarantee fund to ensure settlement finality for the interbank payment clearing system; (ii) a bank deposit guarantee scheme funded by deposit institutions; and (iii) a bank resolution fund, which should be backed by a creditor bail-in mechanism. The assessment of systemic risks has started and a committee for financial stability includes the BCEAO, the Banking Commission and the financial market regulator (CREPMF[7]).

Staff's Recommendations

22. Staff emphasized that policymakers should:

- Bring vulnerable banks to deleverage and strengthen their capital and liquidity buffers. The refinancing of sovereign bonds has somewhat constrained monetary policy in 2017. Hence, the authorities should recreate room for monetary policy to backstop financial stability. To that end, they should use bank supervision and resolution tools to improve balance sheets and resolve fragile banks.

[7] *Conseil Régional de l'Epargne Publique et des Marchés Financiers.*

- Bring banks to diversify their bond portfolios, to contain risk concentration. Risk diversification would reduce systemic risk, improve sovereign risk pricing and stimulate trading liquidity.

- Ensure that microfinance institutions are closely supervised, and that prudential safeguards are established, notably to protect client funds that are entrusted with payment service providers. Given that the micro-finance sector consists of about 630 institutions, with deposits and loans equivalent to about 6.5 percent of banking sector aggregates, it is critical that risks be brought under effective supervision.

- Promote financial inclusion including through lower financial service costs, and by promoting financial literacy and financial consumer credit protection. Closely supervise microfinance institutions and ensure that prudential safeguards are established, notably to protect client funds entrusted to mobile payment service providers.

- Strengthen AML/CFT supervision to ensure compliance with preventive measures, in particular, those related to domestic politically-exposed persons, and implement dissuasive sanctions for breach of compliance.

Authorities' Views

23. The authorities agreed with the staff that bank weaknesses should be addressed to ensure financial stability. They noted that the new prudential regulation and supervision regime should help strengthen the banking sector's resilience, through improved asset quality and a stronger capital base. The authorities also underscored their current close monitoring of banks that should deleverage rapidly and strengthen their capital and liquidity buffers. They further considered that the Banking Commission's new bank resolution powers will permit addressing effectively the situation of ailing banks. They reiterated their commitment to promote financial inclusion and closely monitor micro-finance institutions. The authorities also noted their commitment to continuing to make the 2015 AML/CFT law operational, as reflected in September 2017 instructions requiring banks to set up efficient information systems to ensure the traceability of financial operations and setting thresholds for the declaration of cash payments and transactions.

C. Fostering Sustainable Growth

24. Sustaining the growth momentum will require efforts to improve competitiveness and promote diversification. Medium-term growth will continue to be driven by domestic demand but with an increasing role of private investment as fiscal consolidation takes hold and the business climate improves with structural reforms.[8]

[8] See chapter on WAEMU's growth acceleration of an accompanying Selected Issues Paper.

- **Background.** Survey-based indicators show that regional structural competitiveness improved in 2017, but less than in other African and Asian benchmark countries with strong growth (Annex II). The WAEMU region scores low in business climate and global competitiveness indicators with significant obstacles persisting in, for instance, registering property, dealing with construction permits, getting credit and electricity, paying taxes, and the availability of infrastructure, technology, and specialized labor. In addition, governance indicators remain weak while logistics performance needs improvements. Despite high public investment spending during the past decade, the infrastructure gap remains important compared to other regions, reflecting large initial gaps as well as low public investment efficiency.

- **Policies.** Improving competitiveness and resilience to shocks and sustaining the recent growth performance in the WAEMU would require efforts to maintain macroeconomic stability, improve trade performance, promote efficient public and private investments, and lower costs of inputs such as transport and electricity. The national authorities should take steps to improve the efficiency of public investments as well as the investment climate by easing the above-noted impediments to doing business. At the regional level, the WAEMU Commission is taking steps to enhance the effectiveness of regional structural funds in cross-border infrastructure projects.

Authorities' Views

25. The authorities broadly agreed with staff's views. They highlighted ongoing efforts through regional structural funds for projects covering energy, transport, and agriculture, as well as the preparation of a community investment code to improve the business climate and competitiveness, and reduce the infrastructure gap.

OTHER ISSUES

26. A safeguards assessment of the BCEAO is substantially complete. The 2018 assessment, conducted on a four-year cycle for regional central banks, found that the BCEAO continues to maintain a strong internal control environment. Key recommendations from the last assessment in 2013 have been implemented. The bank adopted International Financial Reporting Standards (IFRS) in 2015 and the selection criteria for the external auditors has been strengthened. The audited financial statements in the period since the last assessment have had unmodified (clean) audit opinions and are published on a timely basis.

27. It is important to further strengthen the quality, timeliness, and dissemination of economic statistics. Progress was made in recent years as illustrated by the dissemination of WAEMU countries' data on the Open Data Platform developed by the African Development Bank in collaboration with the Fund and Senegal's adherence to the SDDS in late 2017. However much remains to be done, notably to improve consistency between national and regional data and address weaknesses of balance of payment data. Staff underscored the need to accelerate the transition of all WAEMU member-countries to the GFSM 2001 fiscal reporting, which would facilitate the compilation of consolidated public finance data, including the public sector's borrowing requirement for the currency union.

STAFF APPRAISAL

28. **Economic activity remained strong in 2017 but vulnerabilities persist.** Real GDP growth exceeded 6 percent for a sixth year in a row but continued to be driven mainly by public spending, notably to address infrastructure gaps, contributing to widening fiscal and external current deficits. The recovery in reserves in 2017 masks continued underlying pressures, and reserves would have sustained their slide that started in 2016 were it not for the extraordinary level of Eurobond issues in 2017.

29. **The medium-term outlook remains positive but subject to significant downside risks.** The current growth momentum could be sustained over the medium term but hinges crucially on planned fiscal consolidation and the decisive implementation of structural reforms. Further delays on these two fronts would jeopardize debt sustainability and external viability. Other downside risks to the outlook relate to terms of trade and weather shocks, a global growth slowdown, tighter international financing conditions and worsening of the security situation. Timely and well-coordinated national and regional policy responses are needed to build policy buffers to mitigate the impact of the materialization of these risks.

30. **Fiscal consolidation is essential to lower public debt and lift pressures on monetary policy and reserves.** Governments should bolster revenues and prioritize spending to meet the WAEMU fiscal deficit criterion of 3 percent of GDP by 2019 and beyond while creating fiscal space for priority infrastructure and social spending. Effective fiscal consolidation must also be supported by an assessment of risks to fiscal and debt sustainability related to below-the-line operations or contingent liabilities, more effective regional surveillance efforts, and improved debt management.

31. **While national fiscal policies must deliver the necessary deficit reductions, monetary conditions should be tightened if the external position weakens.** The BCEAO should stand ready to further tighten monetary policy if pressures persist on the money market and on foreign exchange reserves. Meanwhile, it should steer liquidity based on autonomous factors while gradually reducing the banking system's dependence on central bank refinancing.

32. **Developing the interbank and the debt securities markets is important to improve monetary policy transmission.** The BCEAO could further promote the development of interbank transactions by continuing to gradually mop up liquidity and promote banks' balance sheet repair. The interbank market would be stimulated by the availability of more information on counterparty risks and the development of repo transactions, based on public debt securities. Such transactions would in turn be facilitated by the development of secondary trading of debt

securities, including by eliminating market segmentation between the auction and syndication modes of issuance.

33. Improving financial stability remains essential, including to create more room for monetary policy actions. The appropriate phasing and effective enforcement of the new prudential rules aligned with Basle II/III principles should help consolidated banks' balance sheets and address vulnerabilities. The authorities should bring all undercapitalized banks to meet capital requirements by June 2018, and are encouraged to use their new bank resolution powers as needed after that deadline.

34. The promotion of financial inclusion remains a priority. Staff encourages the authorities to implement the regional strategy adopted to this end, while paying due consideration to financial stability and money-laundering and terrorism financing risks.

35. Sustaining the growth momentum will also require addressing structural impediments to private investment, competitiveness and diversification. Efforts will be needed to raise public investment efficiency and improve the business environment.

36. Efforts to improve the quality, coverage and timeliness of regional data should be sustained. Senegal's adherence to the SDDS in late 2017 illustrates the progress recently achieved in this area. More needs to be done however, in particular regarding external sector and public finance statistics.

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

Table 1. WAEMU: Selected Economic and Social Indicators, 2014–22

Social Indicators

GDP		**Poverty**	
Nominal GDP (2017, millions of US Dollars)	108,285	Headcount ratio at $2 a day (2011 PPP, percent of pop	39.56
GDP per capita (2017, US Dollars)	917	Undernourishment (2012, percent of population)	12.26
Populations charateristics		**Inequality**	
Total (2017. millions)	118	Income share held by highest 10 percent of populatior	32.10
Urban Population (2016, percent of total)	41	Income share held by lowest 20 percent of population	6.34
Life expectancy at birth (2015, years)	59.3	Gini index (2011)	40.74

Economic Indicators

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est.			Proj.		
	(Annual percentage change)								
National income and prices									
GDP at constant prices	6.7	6.2	6.6	6.5	6.4	6.3	6.3	6.4	6.2
GDP per capita at constant prices	3.7	3.3	3.8	3.6	3.5	3.4	3.4	3.5	3.3
Broad money to GDP	4.7	5.8	0.9	3.3	2.8	1.5	0.7	0.9	3.6
Consumer prices (average)	-0.1	1.0	0.3	0.8	1.7	1.9	2.0	2.2	2.0
Terms of trade	0.7	7.8	13.6	-1.8	-4.3	0.4	0.2	-0.7	-1.0
Nominal effective exchange rates	3.8	-3.8	2.0	3.0	…	…	…	…	…
Real effective exchange rates	1.0	-5.5	-0.5	-0.2	…	…	…	…	…
	(Percent GDP)								
National accounts									
Gross national savings	18.4	16.6	17.1	17.4	17.8	18.8	19.6	20.3	20.2
Gross domestic investment	23.5	22.5	22.6	23.4	24.2	24.6	25.3	25.4	25.2
Of which: public investment	7.5	7.8	7.5	8.3	8.5	8.4	8.4	8.2	8.1
	(Annual changes in percent of beginning-of-period broad money)								
Money and credit [1]									
Net foreign assets	0.1	0.0	-5.4	1.7	1.8	2.8	1.9	2.6	2.7
Net domestic assets	0.1	14.8	16.1	5.8	9.1	7.9	8.7	8.0	8.0
Broad money	12.6	14.8	10.7	7.5	10.9	10.6	10.6	10.6	10.6
Credit to the private sector	12.9	16.2	12.3	13.2	12.5	11.7	12.2	12.7	12.6
	(Percent GDP, unless otherwise indicated)								
Government financial operations									
Government total revenue, excl. grants	17.5	18.4	18.2	18.7	19.3	19.3	19.7	19.9	20.1
Government expenditure	23.5	25.0	24.8	25.8	25.4	24.8	24.8	24.7	24.6
Official grants	2.7	2.4	2.2	2.3	2.1	2.5	2.4	2.3	2.2
Overall fiscal balance, incl. grants (commitment basis)	-3.3	-4.1	-4.5	-4.7	-4.0	-2.9	-2.7	-2.5	-2.4
Basic fiscal balance, incl. grants & HIPC	-1.6	-1.5	-2.0	-1.5	-0.5	0.3	0.5	0.6	0.8
External sector									
Exports of goods and services [2]	25.0	25.4	22.7	22.6	21.5	21.5	21.4	21.9	22.1
Imports of goods and services [2]	35.2	33.5	30.8	30.8	30.0	29.5	29.3	28.9	28.9
Current account, excl. grants	-7.6	-7.5	-7.8	-8.2	-8.4	-8.0	-7.7	-6.9	-6.7
Current account, incl. grants	-5.1	-5.5	-5.6	-6.0	-6.3	-5.7	-5.6	-5.0	-4.9
External public debt	24.1	28.0	27.7	29.8	29.3	29.1	28.6	28.2	27.9
Total public debt	40.7	45.5	48.2	48.2	48.9	48.2	47.4	46.6	45.8
Broad money	30.1	31.9	32.1	33.2	34.1	34.7	34.9	35.2	36.5
Memorandum items:									
Nominal GDP (billions of CFA francs)	49,911	53,816	58,176	62,906	68,030	73,618	79,693	86,418	93,530
Nominal GDP per capita (US dollars)	931	815	855	917	1,034	1,092	1,153	1,214	1,275
CFA franc per US dollars, average	494	591	593	581	…	…	…	…	…
Foreign exchange cover ratio [3]	91.7	84.4	71.5	72.1 ..	…	…	…	…	…
Gross international reserves									
In months of imports of goods and services [2]	4.7	5.0	4.0	4.2	4.2	4.3	4.4	4.5	4.6
In millions of US dollars	7,033	7,487	6,466	7,184	7,629	8,376	9,094	10,035	11,053
In percent of broad money	39.7	36.8	28.7	29.7	28.4	28.2	27.6	27.6	27.4

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

[1] Year on year change, end December.

[2] Excluding intraregional trade.

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

Table 2. WAEMU: Selected National Accounts and Inflation Statistics, 2014-22

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est.			Proj.		
				(Annual percentage change)					
Real GDP									
Benin	6.4	2.1	4.0	5.6	6.0	6.3	6.7	7.1	6.1
Burkina Faso	4.3	3.9	5.9	6.4	6.0	6.0	6.0	6.0	6.1
Côte d'Ivoire	8.8	8.8	8.3	7.8	7.4	7.1	6.9	6.7	6.5
Guinea-Bissau	1.0	6.1	5.8	5.5	5.0	5.0	5.0	5.0	5.0
Mali	7.0	6.0	5.8	5.3	5.0	4.7	4.7	4.7	4.7
Niger	7.5	4.0	5.0	5.2	5.2	5.4	5.6	7.2	6.1
Senegal	4.1	6.5	6.7	6.8	7.0	7.0	7.0	7.0	7.0
Togo	5.9	5.3	5.0	4.8	5.0	5.2	5.3	5.4	5.6
WAEMU	6.7	6.2	6.6	6.5	6.4	6.3	6.3	6.4	6.2
Real GDP per capita									
Benin	3.5	-0.6	1.2	2.8	3.3	3.6	4.0	4.4	3.5
Burkina Faso	1.3	0.9	4.1	3.5	3.2	3.2	3.2	3.2	3.3
Côte d'Ivoire	6.0	6.1	5.6	5.0	4.6	4.3	4.2	3.9	3.8
Guinea-Bissau	-1.2	3.8	3.5	3.2	2.7	2.7	2.7	2.7	2.7
Mali	3.6	2.6	2.4	1.9	1.6	1.4	1.4	1.4	1.4
Niger	4.3	0.8	1.9	2.0	2.0	2.2	2.4	4.0	2.9
Senegal	1.1	3.4	3.7	3.8	4.0	4.0	4.0	4.0	4.0
Togo	3.2	2.6	2.4	2.2	2.4	2.6	2.7	2.8	3.0
WAEMU	3.7	3.3	3.8	3.6	3.5	3.4	3.4	3.5	3.3
Inflation									
Benin	-1.1	0.3	-0.8	0.1	2.9	2.9	2.8	2.8	2.8
Burkina Faso	-0.3	0.9	-0.2	0.4	2.0	2.0	2.0	2.0	2.0
Côte d'Ivoire	0.4	1.2	0.7	0.8	1.7	2.0	2.0	2.0	2.0
Guinea-Bissau	-1.0	1.5	1.5	1.1	2.0	2.2	2.3	2.5	2.6
Mali	0.9	1.4	-1.8	1.8	1.4	1.7	1.9	2.1	2.2
Niger	-0.9	1.0	0.2	2.4	2.5	2.0	2.0	2.0	2.0
Senegal	-1.1	0.1	0.9	1.4	1.5	1.5	1.5	1.5	1.5
Togo	0.2	1.8	0.9	-0.7	-1.6	1.4	2.0	5.6	2.0
WAEMU	-0.1	1.0	0.3	0.8	1.7	1.9	2.0	2.2	2.0
				(Percent of GDP)					
Gross national savings									
Benin	20.0	16.7	15.2	19.2	19.8	18.9	20.0	20.8	18.1
Burkina Faso	13.4	5.3	8.5	9.3	8.7	10.1	10.4	11.0	11.3
Côte d'Ivoire	21.2	19.5	19.6	20.6	21.0	22.7	23.6	24.8	24.8
Guinea-Bissau	12.0	10.5	9.3	8.1	7.2	6.8	7.0	7.3	7.5
Mali	15.7	13.0	11.4	10.4	12.5	13.9	14.1	14.4	14.2
Niger	23.7	22.0	21.6	22.7	22.1	22.3	22.2	22.1	22.2
Senegal	15.5	18.2	21.2	18.5	18.4	19.3	20.0	20.4	20.7
Togo	17.9	19.6	20.8	20.4	21.0	19.6	22.3	24.4	24.8
WAEMU	18.4	16.6	17.1	17.4	17.8	18.8	19.6	20.3	20.2
Gross domestic investment									
Benin	28.6	25.6	24.6	28.6	28.3	26.3	26.9	27.5	24.2
Burkina Faso	21.5	13.8	15.8	17.7	16.7	17.0	17.5	17.9	18.2
Côte d'Ivoire	19.7	20.1	20.7	21.5	22.9	24.1	25.1	26.2	26.3
Guinea-Bissau	11.4	8.2	8.0	8.1	10.4	9.4	9.4	9.4	9.3
Mali	20.4	18.4	18.6	18.5	19.6	19.9	20.0	20.1	20.2
Niger	39.3	42.5	37.0	36.1	38.2	39.1	40.5	34.1	34.0
Senegal	24.5	25.2	26.9	27.2	27.7	28.0	28.1	28.3	28.4
Togo	27.9	30.7	30.5	29.1	29.6	27.5	29.0	29.9	29.8
WAEMU	23.5	22.5	22.6	23.4	24.2	24.6	25.3	25.4	25.2

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

Table 3. Sub-Saharan Africa: Cross-Group Comparison, 2014-22

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est.			Proj.		
	(Annual percentage change)								
Real GDP									
WAEMU	6.7	6.2	6.6	6.5	6.4	6.3	6.3	6.4	6.2
CEMAC [1]	4.7	1.9	-0.6	0.3	2.1	2.7	3.3	3.9	3.8
Sub-Saharan Africa [2]	5.1	3.4	1.4	2.7	3.4	3.5	3.7	3.8	3.8
Inflation (annual averages)									
WAEMU	-0.1	1.0	0.3	0.8	1.7	1.9	2.0	2.2	2.0
CEMAC [1]	2.7	2.7	1.3	1.0	1.3	1.6	2.1	2.2	2.3
Sub-Saharan Africa [2]	6.4	7.1	11.4	11.3	9.5	8.9	8.6	7.9	7.7
Terms of trade									
WAEMU	0.7	7.8	13.6	-1.8	-4.3	0.4	0.2	-0.7	-1.0
CEMAC [1]	-10.0	-38.8	-13.0	10.2	-3.9	-0.4	-1.0	0.5	-0.6
Sub-Saharan Africa [2]	-2.5	-13.0	0.3	4.1	-0.5	-2.0	-1.6	-1.3	-0.7
	(Percent GDP, unless otherwise indicated)								
Gross national investment									
WAEMU	23.5	22.5	22.6	23.4	24.2	24.6	25.3	25.4	25.2
CEMAC [1]	29.8	27.2	23.9	21.9	22.0	23.0	23.5	23.7	24.2
Sub-Saharan Africa [2]	21.9	21.7	19.8	19.8	20.3	20.8	21.2	21.7	21.6
Overall fiscal balance, incl. grants									
WAEMU	-3.3	-4.1	-4.5	-4.7	-4.0	-2.9	-2.7	-2.5	-2.4
CEMAC [1]	-3.8	-8.4	-6.3	-3.0	-1.5	-0.7	-0.2	0.2	0.2
Sub-Saharan Africa [2]	-3.7	-4.4	-4.6	-4.6	-4.3	-4.0	-3.7	-3.6	-3.5
External current account, incl. grants									
WAEMU	-5.1	-5.5	-5.6	-6.0	-6.3	-5.7	-5.6	-5.0	-4.9
CEMAC [1]	-3.9	-12.2	-13.9	-6.5	-4.0	-3.6	-2.8	-1.7	-2.0
Sub-Saharan Africa [2]	-3.8	-6.0	-4.1	-3.3	-4.1	-4.1	-4.0	-3.9	-3.7
External public debt									
WAEMU	24.1	28.0	27.7	29.8	29.3	29.1	28.6	28.2	27.9
CEMAC [1]	19.6	28.3	30.3	35.6	37.6	38.2	36.5	34.4	32.8
Sub-Saharan Africa [2]	14.7	17.2	20.8	21.9	22.1	21.6	20.9	20.1	19.2

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

[1] Central African Economic and Monetary Community (CEMAC).

[2] Including Nigeria and South Africa.

Table 4. WAEMU: Selected Fiscal Indicators, 2014–22

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est.			Projections		
					(Percent GDP)				
Primary fiscal balance									
Benin	-1.5	-7.3	-4.8	-4.1	-2.2	0.6	1.5	1.9	2.5
Burkina Faso	-1.1	-1.5	-2.4	-7.2	-3.7	-1.8	-1.7	-1.7	-1.6
Côte d'Ivoire	-0.9	-1.3	-2.2	-2.7	-1.9	-1.2	-1.1	-1.1	-1.0
Guinea-Bissau	-2.6	-3.0	-3.6	-1.2	-2.0	-1.6	-1.2	-1.1	-1.0
Mali	-2.3	-1.2	-3.3	-2.1	-2.7	-2.1	-2.0	-2.0	-2.0
Niger	-7.7	-8.4	-5.2	-5.1	-5.1	-4.5	-2.9	-1.2	-0.5
Senegal	-3.3	-2.8	-2.1	-1.3	-1.4	-0.9	-1.0	-1.1	-1.1
Togo	-5.4	-6.6	-7.2	-0.2	-0.1	3.4	1.9	1.8	1.9
WAEMU	-2.3	-2.9	-3.1	-3.1	-2.3	-1.2	-1.0	-0.9	-0.7
Overall fiscal balance, commitment basis (including grants)									
Benin	-1.9	-8.0	-6.0	-6.2	-4.5	-1.7	-0.6	0.0	0.9
Burkina Faso	-1.9	-2.2	-3.4	-8.2	-5.0	-3.0	-3.0	-3.0	-3.0
Côte d'Ivoire	-2.2	-2.8	-3.9	-4.5	-3.7	-3.0	-2.9	-2.9	-2.8
Guinea-Bissau	-3.1	-3.7	-4.3	-1.7	-2.8	-2.2	-1.6	-1.5	-1.4
Mali	-2.9	-1.8	-3.9	-3.0	-3.5	-3.0	-3.0	-3.0	-3.0
Niger	-8.0	-9.1	-6.1	-6.0	-6.2	-5.7	-4.1	-2.3	-1.5
Senegal	-5.0	-4.8	-4.2	-3.7	-3.5	-3.0	-3.0	-3.0	-3.0
Togo	-6.9	-9.0	-9.6	-2.3	-2.4	0.2	-0.9	-1.4	-1.2
WAEMU	-3.3	-4.1	-4.5	-4.7	-4.0	-2.9	-2.7	-2.5	-2.4
Government revenue (excluding grants)									
Benin	16.3	16.7	14.7	16.9	17.5	17.4	18.0	18.5	18.9
Burkina Faso	17.4	17.0	18.4	19.0	19.7	20.3	20.8	20.9	21.2
Côte d'Ivoire	17.1	18.5	18.0	18.0	18.3	18.5	18.7	19.0	19.2
Guinea-Bissau	12.6	13.8	12.2	12.6	14.5	14.9	15.6	16.1	16.9
Mali	14.9	16.4	16.7	18.5	19.2	18.6	18.9	19.3	19.7
Niger	17.6	18.0	14.4	15.2	15.6	15.9	17.2	18.3	18.9
Senegal	21.5	22.2	24.0	23.4	24.0	23.9	24.0	23.2	23.2
Togo	18.3	19.7	18.9	20.0	21.7	21.3	21.3	21.2	21.2
WAEMU	17.5	18.4	18.2	18.7	19.3	19.3	19.7	19.9	20.1
Government expenditure									
Benin	19.1	25.3	21.4	24.5	23.6	21.0	20.2	19.5	19.0
Burkina Faso	23.4	22.9	24.4	29.9	28.1	27.0	27.2	27.4	27.5
Côte d'Ivoire	21.0	22.8	23.3	24.0	23.3	23.1	23.1	23.2	23.0
Guinea-Bissau	24.7	23.4	20.9	18.9	21.3	21.3	21.6	22.0	22.8
Mali	20.0	20.9	22.2	22.9	23.9	23.5	23.8	24.0	24.4
Niger	31.1	32.5	26.6	28.5	28.7	29.3	28.7	26.4	26.0
Senegal	29.8	29.9	31.0	29.0	29.2	28.7	28.7	28.7	28.7
Togo	27.5	31.1	31.4	27.6	28.0	25.1	26.2	26.7	26.5
WAEMU	23.5	25.0	24.8	25.8	25.4	24.8	24.8	24.7	24.6
Government current expenditure									
Benin	14.2	17.2	15.4	15.1	15.0	14.7	14.3	14.0	13.7
Burkina Faso	14.5	15.0	16.7	17.3	17.4	16.1	15.8	15.9	15.9
Côte d'Ivoire	15.3	16.4	16.7	17.1	16.2	15.8	15.9	16.1	16.2
Guinea-Bissau	17.1	15.3	14.8	12.5	12.7	13.7	14.0	14.5	15.3
Mali	11.9	11.9	12.2	12.7	13.2	12.4	12.6	12.7	12.9
Niger	14.6	15.5	14.1	14.2	14.0	13.8	13.2	12.7	12.5
Senegal	18.5	18.6	18.5	16.4	16.1	15.4	15.5	15.5	15.5
Togo	16.2	17.9	17.4	16.6	17.4	18.1	17.7	18.2	18.1
WAEMU	15.1	16.0	16.0	15.9	15.7	15.1	15.1	15.2	15.2
Government capital expenditure [1]									
Benin	5.2	7.7	5.9	9.3	8.6	6.3	5.9	5.5	5.3
Burkina Faso	9.1	8.1	7.9	12.6	10.7	10.8	11.4	11.5	11.6
Côte d'Ivoire	5.7	6.4	6.5	6.9	7.0	7.3	7.2	7.1	6.8
Guinea-Bissau	7.6	8.1	6.2	6.4	8.7	7.6	7.6	7.6	7.4
Mali	6.5	7.3	8.9	8.5	9.5	9.8	9.9	10.0	10.1
Niger	16.4	17.0	12.5	14.3	14.7	15.4	15.5	13.7	13.6
Senegal	11.3	11.2	12.5	12.6	13.1	13.3	13.2	13.3	13.2
Togo	11.3	13.1	14.0	11.0	10.6	7.1	8.5	8.5	8.4
WAEMU	8.2	8.7	8.6	9.6	9.6	9.5	9.5	9.4	9.3

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

[1] Excludes net lending.

Table 5. WAEMU: Balance of Payments, 2014-22

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
				Est.			Proj.			
					(Percent of GDP)					
Balance on current account	-5.1	-5.5	-5.6	-6.0	-6.3	-5.7	-5.6	-5.0	-4.9	-4.9
excluding official transfers:	-7.6	-7.5	-7.8	-8.2	-8.4	-8.0	-7.7	-6.9	-6.7	-6.0
Balance on goods and services	-8.3	-8.1	-8.1	-8.2	-8.4	-8.0	-7.8	-7.0	-6.7	-6.1
Exports of goods	25.1	25.4	22.7	22.7	21.7	21.7	21.7	22.3	22.6	23.0
Exports of services	4.4	4.2	3.9	3.8	3.6	3.6	3.5	3.5	3.4	3.3
Imports of goods	-27.5	-27.9	-24.6	-24.6	-24.3	-24.0	-23.9	-23.8	-23.9	-23.9
Imports of services	-10.3	-9.8	-10.0	-10.0	-9.5	-9.3	-9.2	-9.0	-8.8	-8.5
Income, net	-2.1	-2.2	-2.2	-2.4	-2.3	-2.3	-2.2	-2.1	-2.1	-2.0
Income credits	1.4	1.4	1.3	1.4	1.4	1.3	1.3	1.3	1.3	1.3
Income debits	-3.5	-3.6	-3.5	-3.9	-3.7	-3.6	-3.5	-3.4	-3.4	-3.3
Of which										
Investment income, debit: interest	-0.7	-0.7	-0.7	-0.8	-0.8	-0.8	-0.8	-0.7	-0.7	-0.7
Current transfers, net	5.4	4.9	4.7	4.6	4.4	4.6	4.4	4.2	3.9	3.3
Private current transfers, net	2.9	2.9	2.5	2.4	2.3	2.3	1.9	1.8	1.8	1.7
Official current transfers, net	2.5	2.0	2.2	2.2	2.1	2.3	2.1	2.0	1.8	1.1
Balance on capital and financial account	5.3	7.3	2.6	7.1	7.0	6.7	6.5	6.1	6.0	6.1
Balance on capital account	2.1	2.0	1.8	1.9	1.8	1.9	1.8	1.7	1.6	1.5
Balance on financial account	3.2	5.3	0.8	5.2	5.1	4.8	4.7	4.4	4.4	4.6
Direct investment, net	2.0	2.0	1.7	2.2	2.5	2.7	2.7	2.5	2.6	2.7
Portfolio investment, net	1.8	2.0	1.3	3.1	2.9	0.8	0.8	0.7	0.6	0.6
Other investment, net	-0.6	1.4	-2.2	-0.2	-0.2	1.3	1.2	1.2	1.2	1.3
Errors and omissions, net	1.2	0.5	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	1.4	2.3	-3.3	1.1	0.7	1.0	0.9	1.1	1.1	1.2
Change in official NFA ("-" increase)	-0.5	-2.3	3.3	-1.1	-0.7	-1.0	-0.9	-1.1	-1.1	-1.2

Source: IMF, African Department database

Table 6. WAEMU: Government Debt and Debt Service, 2014–22

	2014	2015	2016	2017	2018	2019	2020	2021	2022
				Est.			Proj.		
					(Percent GDP)				
External Debt									
Benin	19.8	21.3	22.5	22.2	23.4	24.6	24.9	24.5	24.8
Burkina Faso	23.5	26.5	27.4	24.2	24.6	24.3	23.9	23.5	23.3
Côte d'Ivoire	26.8	29.5	28.2	28.9	29.8	28.9	27.4	26.5	25.9
Guinea-Bissau	15.0	15.2	14.4	12.2	11.1	11.6	11.8	12.0	12.1
Mali	21.0	22.6	24.9	21.7	21.4	21.6	22.1	22.4	23.0
Niger	25.1	30.3	33.0	35.0	37.1	38.9	41.7	42.7	43.7
Senegal	40.4	41.1	42.3	46.3	45.1	44.0	43.3	42.3	41.7
Togo	17.3	21.2	20.4	20.9	22.9	25.5	26.0	26.2	26.1
WAEMU	26.3	28.7	29.1	29.3	29.8	29.7	29.3	28.9	28.8
Total Debt									
Benin	30.5	42.4	49.5	55.7	56.1	53.2	48.6	44.3	40.3
Burkina Faso	30.4	35.8	38.3	38.3	41.0	41.3	41.8	41.6	41.5
Côte d'Ivoire	44.8	47.3	47.0	46.4	48.1	47.0	46.2	45.6	45.0
Guinea-Bissau	55.0	52.3	53.6	51.2	44.8	43.6	41.9	39.9	38.0
Mali	27.3	30.7	35.9	32.8	33.9	35.0	36.3	37.5	38.6
Niger	33.8	41.6	46.7	49.5	51.8	53.5	54.5	54.0	53.8
Senegal	54.5	56.9	60.4	60.7	58.6	56.9	55.5	54.4	53.3
Togo	65.1	75.6	81.5	77.2	73.8	69.6	66.2	62.7	58.8
WAEMU	40.7	45.5	48.2	48.2	48.9	48.2	47.4	46.6	45.8
					(Percent of Government revenue excluding grants)				
Total debt service									
Benin	12.3	14.9	19.0	40.0	46.7	46.9	40.3	33.6	28.2
Burkina Faso	14.1	16.4	30.8	27.1	33.0	40.4	41.3	40.2	40.2
Côte d'Ivoire	14.7	18.6	30.5	20.1	20.2	18.0	17.0	16.4	15.1
Guinea-Bissau[1]	5.7	11.2	12.1	37.2	9.9	9.1	7.4	7.3	6.7
Mali	10.1	13.1	10.5	11.6	12.2	12.4	13.1	13.2	13.1
Niger	23.2	39.7	32.1	43.2	48.4	44.1	42.6	34.9	30.2
Senegal	34.5	29.7	32.8	31.6	33.6	31.2	23.7	32.0	21.8
Togo	54.6	65.2	39.4	52.6	55.3	54.9	58.6	53.5	48.0
WAEMU	20.1	23.2	27.9	26.5	28.6	28.1	26.1	26.0	22.7
Debt service, interest									
Benin	2.3	4.4	8.5	12.1	13.0	13.7	11.8	10.2	8.7
Burkina Faso	4.0	3.9	5.2	4.7	4.7	5.5	5.5	5.7	5.6
Côte d'Ivoire	7.2	8.3	9.3	9.6	10.6	9.4	8.8	8.3	7.9
Guinea-Bissau	4.1	5.4	6.0	3.7	5.4	4.0	2.9	2.5	2.1
Mali	3.9	3.6	4.0	4.5	4.3	4.8	5.0	5.2	5.2
Niger	2.2	3.5	6.5	6.4	6.7	7.7	6.8	5.8	5.4
Senegal	7.0	7.3	7.6	8.4	8.9	8.2	7.9	8.0	7.4
Togo	7.6	11.2	13.5	9.9	10.8	12.3	11.2	10.5	9.1
WAEMU	5.5	6.5	7.8	8.1	8.6	8.4	7.9	7.6	7.1

Source: IMF, African Department database.

[1] Debt service payments for 2017 reflect debt relief on Guinea-Bissau's arrears with Taiwan.

Table 7. WAEMU: Monetary Survey, 2013–19

	2013	2014	2015	2016	2017	2018	2019
					Est.	Proj.	
	(Billions of CFA francs)						
Net foreign assets	**4,732**	**4,747**	**4,754**	**3,656**	**4,030**	**4,475**	**5,222**
of which:							
BCEAO	4,995	5,236	5,480	4,527	5,169	5,613	6,360
Commercial Banks	-263	-488	-726	-871	-1,138	-1,138	-1,138
Net domestic assets	**11,019**	**12,984**	**15,604**	**18,880**	**20,194**	**22,400**	**24,514**
Domestic credit	14,200	16,689	19,482	22,983	25,138	27,343	29,458
Net credit to government	3,159	3,926	4,506	6,475	6,926	7,977	8,287
Net credit to the economy	11,040	12,763	14,977	16,508	18,211	19,366	21,171
Other items, net	-3,180	-3,705	-3,878	-4,103	-4,944	-4,944	-4,944
Broad Money	**15,752**	**17,731**	**20,358**	**22,536**	**24,224**	**26,875**	**29,736**
Money	10,607	11,808	13,542	14,997	16,105	...	...
of which: Currency in circulation	4,265	4,692	5,254	5,542	5,813	...	...
Quasi-money	5,145	5,923	6,816	7,539	8,119	...	...
	(Annual changes in beginning of period broad money)						
Net foreign assets	**-5.9**	**0.1**	**0.0**	**-5.4**	**1.7**	**1.8**	**2.8**
Net domestic assets	**16.9**	**12.5**	**14.8**	**16.1**	**5.8**	**9.1**	**7.9**
Domestic credit	16.1	15.8	15.8	17.2	9.6	9.1	7.9
Net credit to government	5.9	4.9	3.3	9.7	2.0	4.3	1.2
Net credit to the economy	10.2	10.9	12.5	7.5	7.6	4.8	6.7
Other items, net	0.8	-3.3	-1.0	-1.1	-3.7	0.0	0.0
Broad Money	**11.0**	**12.6**	**14.8**	**10.7**	**7.5**	**10.9**	**10.6**
	(Year on year percent change)						
Net foreign assets	**-15.0**	**0.3**	**0.1**	**-23.1**	**10.3**	**11.0**	**16.7**
Net domestic assets	**27.8**	**17.8**	**20.2**	**21.0**	**7.0**	**10.9**	**9.4**
Domestic credit	19.1	17.5	16.7	18.0	9.4	8.8	7.7
Net credit to government	35.9	24.3	14.8	43.7	7.0	15.2	3.9
Net credit to the economy	15.1	15.6	17.3	10.2	10.3	6.3	9.3
Other items, net	-3.6	16.5	4.7	5.8	20.5	0.0	0.0
Broad Money	**11.0**	**12.6**	**14.8**	**10.7**	**7.5**	**10.9**	**10.6**
New credit to government							
In CFAF bln	382	767	580	1,969	451	1,051	309
In percentage of GDP	0.8	1.5	1.1	3.4	0.7	1.5	0.4

Source: BCEAO and IMF staff calculations.

Table 8. WAEMU: Financial Soundness Indicators, December 2011–June 2017[1]

	2011	2012	2013	2014	2015	2016	2016	2017
	December					Jun.	Dec.	Jun.
	(percent, unless otherwise indicated)							
Solvency ratios								
Regulatory capital to risk weighted assets	12.5	12.8	12.9	12.7	12.6	11.4	11.3	11.4
Tier I capital to risk-weighted assets	11.7	12.0	11.8	11.2	10.5	10.3	10.3	10.6
Provisions to risk-weighted assets	10.7	10.8	10.3	10.7	11.7	10.6	10.1	9.9
Capital to total assets	7.3	7.3	7.2	6.7	5.7	6.1	5.8	6.2
Composition and quality of assets								
Total loans to total assets	55.2	55.0	55.9	54.6	53.1	52.5	52.2	52.9
Concentration: loans to 5 largest borrowers to capital[1]	92.9	92.3	75.1	88.6	113.1	100.9	101.9	89.6
Sectoral distribution of loans								
Agriculture	2.9	2.6	2.8	3.1	3.2	2.6	3.2	4.7
Extractive industries	2.2	1.6	1.8	2.0	1.9	1.8	1.6	1.3
Manufacturing	18.8	18.2	17.0	17.9	17.2	16.7	15.5	12.7
Electricity, water and gas	3.2	3.2	3.7	3.9	4.2	4.1	4.9	5.6
Construction	6.7	6.7	7.8	8.6	9.4	10.0	10.8	11.7
Retail and wholesale trade, restaurants and hotels	32.3	34.7	33.5	31.1	31.5	30.6	26.7	31.4
Transportation and communication	11.2	10.1	11.2	9.8	9.5	10.9	9.9	11.9
Insurance, real estate and services	5.5	6.1	5.9	6.5	6.6	7.1	7.2	7.3
Other services	17.1	16.8	16.2	17.0	16.4	16.2	20.1	13.3
Gross NPLs to total loans	15.9	16.0	15.3	14.9	14.4	15.2	13.8	14.6
Provisioning rate	64.2	63.4	61.0	62.8	62.7	63.9	65.5	63.4
Net NPLs to total loans	6.3	6.5	6.6	6.1	5.9	6.1	5.2	5.9
Net NPLs to capital	47.8	48.8	51.1	50.1	54.9	52.7	47.2	49.7
Earnings and profitability								
Average cost of borrowed funds	2.4	2.5	2.8	2.4	2.4	…	2.9	…
Average interest rate on loans	9.7	9.8	10.7	9.1	8.8	…	9.8	…
Average interest margin[2]	7.3	7.3	7.9	6.7	6.4	…	6.9	…
After-tax return on average assets (ROA)	1.2	0.9	0.9	1.1	1.2	…	1.3	…
After-tax return on average equity (ROE)	13.7	10.1	11.5	15.5	16.4	…	20.2	…
Noninterest expenses/net banking income	61.6	61.0	60.6	58.6	58.6	…	58.5	…
Salaries and wages/net banking income	26.4	25.7	26.5	25.4	25.4	…	25.6	…
Liquidity								
Liquid assets to total assets	33.6	32.5	32.2	30.9	29.4	27.6	27.1	26.7
Liquid assets to total deposits	46.1	45.8	47.1	45.9	43.8	41.0	42.3	40.8
Total loans to total deposits	84.3	86.2	90.0	89.5	87.0	86.4	89.5	89.1
Total deposits to total liabilities	72.9	71.1	68.5	67.3	67.1	67.3	64.1	65.3
Sight deposits to total liabilities[3]	37.8	36.5	35.5	34.5	35.4	35.2	34.4	34.8
Term deposits to total liabilities	35.1	34.6	32.9	32.8	31.7	32.1	29.7	30.6

Source: BCEAO.

[1] Indicators do not account for the additional provisions required by the WAEMU Baking Commission.

[2] Excluding tax on bank operations.

[3] Including saving accounts.

Annex I. Authorities' Responses to 2017 Policy Recommendations

(Scale: fully consistent, broadly consistent, partially consistent, and inconsistent)

	2017 Article IV Recommendations	Authorities' Response
Policy Mix	- While fiscal policy should be the first line of defense, the BCEAO should stand ready to tighten monetary conditions if pressures on external reserves persist or re-emerge.	**Broadly consistent** - Bank refinancing has slowed down and reserves have recovered from their fall in 2016, but mainl due to the temporary impact of Eurobond issues Côte d'Ivoire and Senegal.
Fiscal Policy Coordination	- Governments need to adhere to their budget deficit reduction plans while maintaining public investment efforts, which will require increasing tax revenue and improving quality of spending.	**Partially consistent** - Deficits have widened in many countries in 2017 but 2018 budgets are consistent with convergence towards the 3 percent of GDP deficit target for 2019.
Monetary/ Financial sector Development	- Enhance monetary policy effectiveness - Continue financial sector reforms - Accelerate the development of the interbank and government debt markets.	**Partially consistent** - The regional debt agency is coordinating bond issuance but the regional market remains under-developed - Reforms to debt and interbank market still ongoing.
Financial Regulation and Supervision	- Speed up implement existing prudential regulations, and including capital standards consistent with Base II/III. - Strengthen risk based supervision, avoid regulatory forbearance.	**Partially consistent** - The requirement of CFAF 10 billion minimum capital has become effective in July 2017. - New regulations, including bank capital standard consistent with Basel II/III and consolidated supervision became effective in January 2018. - Some prudential limits and compliance need strengthening. - The Banking Commission's Charter has been amended to give it resolution authority.
Structural Reforms/Competitiveness	- Further improve the quality of public infrastructure and ease constraints on the business environment.	**Partially consistent** - Some WAEMU countries have kept the pace of reforms and made progress in areas such as starting a business, construction permits processing, property registrations, and insolvency resolutions but overall progress remains slow. Data from the 2018 World Bank's Report indicates that the regional Doing Business climate has improved less than in other comparator countries.

Annex II. External Sector Assessment

WAEMU's external current account deficit increased in 2017 relative to 2016 owing to the larger fiscal deficits and terms of trade decline. International reserves' import coverage in 2017 increased somewhat to 4.2 months. Under the baseline which assumes implementation of fiscal consolidations plans and improved external competitiveness, the reserve import cover is projected to improve steadily to reach 4.6 months of imports by 2022. An EBA-based assessment shows that WAEMU's external position remains broadly consistent with regional medium-term fundamentals and desirable policy settings. Survey based indicators of external competitiveness show some improvements, but further progress on structural reforms is needed to address the bottlenecks to private sector development.

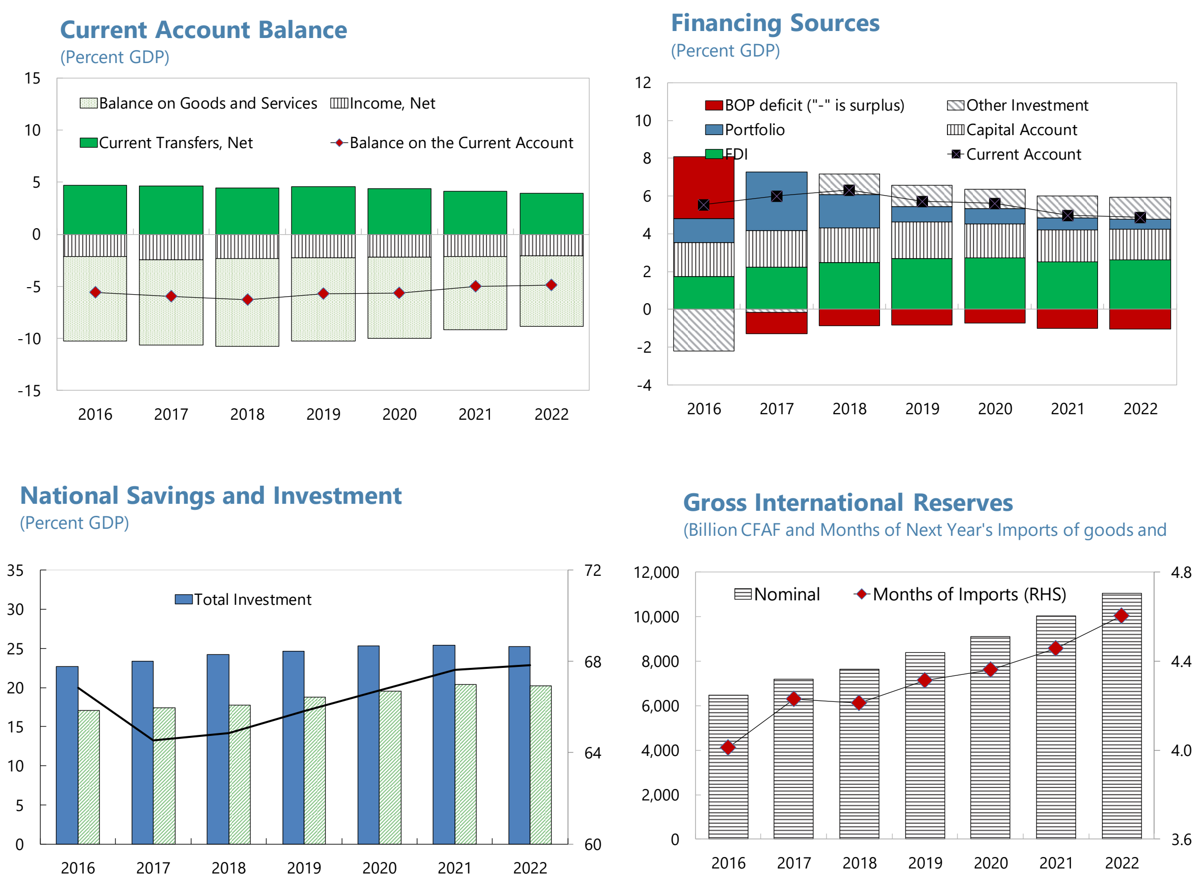
1. External current account developments. WAEMU's current account deficit (including grants) is estimated to have reached 6 percent of GDP in 2017, an increase of 0.4 percentage point of GDP compared to 2016, owing partially to the increased fiscal deficit. After widening in 2018 due to a deterioration in the terms of trade (driven by an increase in petroleum prices and the differed impact of the 2017 drop of world cocoa prices), the current account deficit is projected to gradually decline over the medium term, reaching 4.9 percent of GDP by 2022, assuming successful implementation of fiscal consolidations plans and improved external competitiveness.

2. External financing. After a slight decline in 2016, capital transfers increased slightly in 2017. FDI and portfolio inflows also increased. FDI is projected to increase over the medium term as commodity prices recover and structural reforms to promote the private sector take hold.

3. International reserves developments and prospects. After having fallen by CFAF 993 billion (US$1.7 billion) in 2016, external reserves increased by CFAF 655 billion (US$1.2 billion) in 2017 to reach CFAF 7,184 billion (US$13.1 billion) at end-2017. This increase made up about two thirds of the loss incurred during 2016, as the bulk of net capital inflows, including the US$3.1 billion net proceeds from the Eurobonds issued by Côte d'Ivoire, Senegal and the BOAD in 2017. External reserves' cover of prospective extra-regional imports of goods and services is estimated to have increased from 4.0 months at end 2016 to 4.2 months at end 2017. Under the baseline which assumes effective implementation of fiscal consolidation plans and improved external competitiveness, the reserve import cover is projected to improve to 4.6 months by 2022, somewhat below the adequate reserve import cover for the WAEMU estimated at 5 months (see Annex III). A lack of fiscal adjustment, a prolonged slowdown in global growth or a sustained terms-of-trade deterioration could result in significantly lower external buffers. Staff estimates show that in the absence of fiscal consolidation (i.e., if the regional fiscal deficit remains at its 2017 level in relation to GDP), international reserves' import cover would fall below two months of imports by 2022.

4. Assessment of external position. The EBA-based assessment ("EBA-lite") does not indicate significant misalignment of the real effective exchange rate (REER) for the WAEMU. Three approaches[1] have been used to assess the external stability of the WAEMU. The assessments point to a negligible REER overvaluation between 0.4 percent and 1.8 percent. The WAEMU's external position is broadly consistent with fundamentals and desirable policy settings, notwithstanding the recent strengthening of the euro (to which the WAEMU's CFA franc is pegged) against the U.S. dollar.

WAEMU: Current Account Balance and Financing Sources, and International Reserves



Sources: BCEAO; and IMF staff calculations.

[1] The first approach is the EBA's Current Account (CA), which compares the actual current account balance with the estimated current account norm. The second approach is the EBA's Index Real Effective Exchange Rate (IREER), for which the comparison is based on the fitted REER and the REER norm. The last approach is the EBA's External Stability (ES) which compares the current account balance that is expected to prevail in the medium-term to the one that would stabilize the external stock position.

WAEMU: External Stability Assessment

	EBA-Lite- 2017*		
	Current Account (CA)	Index Real Effective Exchange Rate (IREER)	External Stability
Adjusted actual current account	-5.5		0
Current account norm	-4.7		0.6
Log REER - actual		3.05	
Log REER - norm		2.65	
Current account gap (Percent)	-0.8		-0.6
REER gap (Percent)	1.8	0.4	1.3

*Assuming the average trade elasticity used in WAEMU countries

5. **Structural Competitiveness**. The WAEMU's competitiveness remains hampered by significant structural constraints, including inadequate infrastructure, high costs of inputs such as communication, transport and electricity, and weak business and legal environments.[2]

- The 2018 World Bank's Doing Business Report indicates that the regional business climate has improved though it remains less favorable relative to peers in Africa and Asia. The average WAEMU rank is 150 out of 190 ranked countries. However, some WAEMU countries (Benin, Niger, and Senegal) have kept the pace of reforms and made steady progress in areas such as starting a business, construction permits processing, property registrations, and insolvency resolutions.

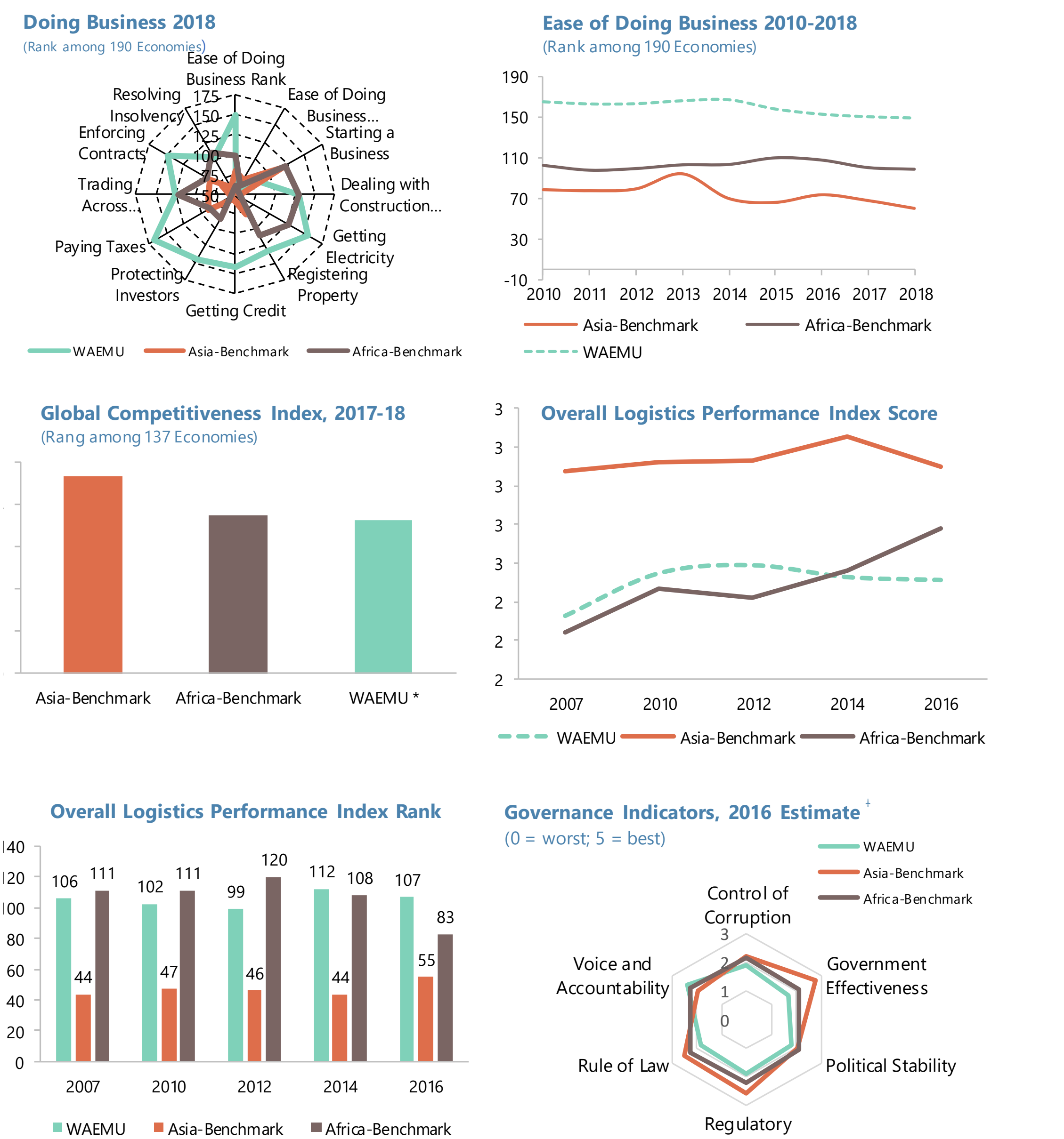
- The logistics performance index (LPI) also indicates lagging performance of the WAEMU. The LPI, which ranks 160 countries on six dimensions of trade including customs

[2] Structural competitiveness is captured by Doing Business, Global Competitiveness, Logistics Performance, and Governance Indicators, which are measures of perceptions of the investment climate and governance. Doing Business is based on the average of individual country's distance to frontier scores for 10 topics (as reported in the top left chart) included in the aggregate ranking. Global Competitiveness defines competitiveness as the set of factors that determine the level of productivity of a country based on 12 pillars including infrastructure, health and primary education, technological readiness, and business sophistication. Logistics Performance combines data on six cores of logistics performance including the efficiency of customs and border clearance, and the quality of trade and transport infrastructure into a single aggregate indicator of logistics sector performance. Governance Indicators are measured by Voice and Accountability, Political Stability and Absence of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, Control of Corruption. Voice and Accountability captures perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media. Political Stability and Absence of Violence measures perceptions of the likelihood of political instability and/or politically-motivated violence. Government Effectiveness assesses perceptions of the quality of public services. Regulatory Quality evaluates perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. Rule of Law measures perceptions of the extent to which agents have confidence in and abide by the rules of society. Control of Corruption captures perceptions of the extent to which public power is exercised for private gain. Caution is needed when interpreting the results as they may be affected by sample size, questionnaire wording and design, nonresponse bias, and availability of information.

performance, infrastructure quality, and timeliness of shipments, shows that the regional LPI score and ranking have lagged, compared to peers in Africa and Asia.

- Governance indicators also demonstrate some structural weaknesses. According to the World Bank's Governance Indicators, the region's scores for government effectiveness, political stability, regulatory quality and rule of law remain weak, compared to peers.

WAEMU: Doing Business, Competitiveness, Logistics, and Governance Indicators



Source: World Bank Doing Business; Global Competitiveness; Logistics Performance Index Dataset; World Governance Indicators; and IMF staff calculations. Notes: * Based on available data for the member countries of the WAEMU. ⸸ Similar perceptions are obtained using data from Transparency International and International Country Risk Guide (ICRG). Asia benchmark includes Indonesia, Malaysia, Philippines, Thailand, and Vietnam. Africa benchmark includes Ghana, Kenya, Lesotho, Rwanda, Tanzania, Uganda, and Zambia.

Annex III. Assessment of External Reserve Adequacy

External reserve adequacy in the WAEMU is examined by balancing the benefits from holding reserves—for both crisis prevention and mitigation—against the opportunity costs of holding reserves. Based on data calibrated for the WAEMU, including on marginal product of capital and Eurobond yields used as proxies for the opportunity cost of holding reserves, the Fund's ARA-CC model estimates that WAEMU's external reserves should be within a range of 5 months to 7 months of prospective extra-regional imports of goods and services. A level of reserves closer to the lower-bound of this range would seem adequate given the additional external buffers implied by the convertibility guarantee of WAEMU's currency to the euro, by the French Treasury.

1. International reserve adequacy assessments focus on the precautionary motives, whereby reserves are held to meet external liquidity needs in the event of shocks which are temporary and exogeneous. Thus, international reserve buffers act as an insurance mechanism against the risk of temporary and exogeneous external liquidity shortfalls, and are not meant to be used to maintain domestic demand at levels inconsistent with medium and long term external sustainability (due to inadequate policies, including when facing likely permanent shocks).

2. WAEMU's reserves are a common pool from which all residents of the currency union, regardless of nationality, can obtain foreign exchange at a fixed parity with the Euro for legitimate external current transactions, provided they have corresponding local currency holdings. Accordingly, the BCEAO stopped publishing "imputed reserves" data for each member country, and the data for the common pool of reserves are now reported for each WAEMU member country, in internal and external Fund documents.[1] External reserve adequacy must therefore be assessed for the WAEMU and the results of such assessments apply equally to each of the eight countries of the currency union.

3. All eight countries of the WAEMU are PRGT eligible with relatively shallow and underdeveloped financial markets. The WAEMU can therefore be considered as a "credit constrained" economy, although it has gained some access to international markets in recent years, through the Eurobond issuances of Côte d'Ivoire and Senegal. Contrary to current account transactions, capital and financial transactions between WAEMU residents and nonresidents, including from France and other parts of the Zone Franc, are subject to controls that limit the risk of capital flight.[2]

[1] Note that it is the data for the common pool of reserves that shall be submitted to the Fund for Senegal, following its recent adherence to SDDS.

[2] Controls and restrictions on capital transactions with non-WAEMU residents apply to the acquisitions of real or physical assets outside the currency union. Capital leakages may however occur through under-invoicing exports or over-invoicing imports, or through non-observance of the obligation to repatriate and surrender 80 percent of foreign exchange from export proceeds within one month.

4. Against this background, an appropriate reserve adequacy metric for the WAEMU is the coverage of prospective imports of goods and services which focuses on shocks emanating from the external current account, rather than the ratio of reserves to broad money (typically M2) generally used to assess capital flight risks and the ratio of reserves to short-term debt used as an indicator of roll-over risk for countries with large short-term cross-border financial transactions.

5. Based on the Fund's ARA-CC approach,[3] an estimate for the adequate level of import cover for international reserves may first be derived through an algorithm that balances the benefits from holding reserves in terms of both crisis prevention and mitigation against the opportunity costs of holding additional reserves. To this end, the ARA-CC model must be calibrated with relevant parameters for the WAEMU related to its exchange rate regime and economic specificities.

6. The results of the ARA-CC model depend on the degree of dependence of the economic entity's exports and public finances on a narrow commodity base, because resource-rich (RR) countries generally face higher external current account volatility than non-resource-rich (NRR) economies, which would argue in favor of a higher level of external reserves adequacy for RR than for NRR economies. Within WAEMU, Burkina Faso, Mali and Niger may be classified as RR as commodities represent a large share of total exports (20 percent or more) or fiscal revenues (15 percent or more).[4] These three countries account for 33 percent of WAEMU's GDP. Accordingly, the estimate for the adequate level of external reserves for the WAEMU can be calculated as a weighted average of the model's results under the two alternative assumptions of RR and NRR.

7. Regarding the opportunity cost of holding reserves, the ARA-CC approach suggests three possible proxies: (i) the sterilization cost, adjusted for an exchange rate risk premium, for LICs with liquid government securities markets; (ii) the yield on sovereign borrowing for LICs that have access to international capital markets; and (iii) the marginal productivity of capital (MPK), in cases where financial markets are thin and underdeveloped. The first proxy seems less appropriate for the WAEMU given the lack of a significant secondary market for government securities. The other two proxies appear more relevant for the WAEMU given the recent Eurobonds issuances by the sovereigns of its two larger member-countries and the under-development of financial markets respectively.

[3] See IMF: "Assessing Reserve Adequacy in Credit-Constrained-Economies," 2013, based on Dabla-Norris (2011).

[4] See Regional Economic Outlook—Sub-Saharan Africa, October 2017.

8. Côte d'Ivoire and Senegal issued in June 2017 Eurobonds amounting to US$1.2 billion and US$1.1 billion respectively, with yield of 6.25 percent. Côte d'Ivoire also issued in June 2017 a Euro-denominated Eurobond with a yield of 5.125 percent for an amount of EUR625 million.[5] The average yield for these three operations is 6 percent. To obtain the corresponding proxy for the opportunity cost of holding reserves, one should deduct from this average yield the return on BCEAO's reserves. The latter may be estimated at 0.5 percent, taking into account the minimum return of 0.75 percent guaranteed on half of the BCEAO's reserves held on the BCEAO's "operations account" at the French Treasury and the negative yield on a significant portion of these reserves held outside the "operations account" in the form of euro-denominated T-bills.[6] The opportunity cost of holding additional reserves for the BCEAO as proxied through Eurobond yields net of the return on reserves may be thus estimated at about 5.5 percent.

9. Alternatively, the opportunity cost of holding external reserves may be proxied by the MPK in the WAEMU, which in turn may be derived as the average for the period 1960-2014 of the weighted averages of estimates available in the World Penn Tables for the share of capital compensation in nominal GDP for WAEMU countries. This alternative approach yields an MPK of 4.5 percent, implying an estimate of 4 percent for the opportunity cost of holding reserves, after deducting 0.50 percent for the return on BCEAO's reserves.

10. Depending on the proxy used (yield of Eurobonds vs. MPK), the opportunity cost of holding reserves for the WAEMU is estimated in the 4 percent and 5.5 percent range.[7] Based on this and other relevant WAEMU economic data, and assuming a 50 percent unconditional probability of a large shock event,[8] the adequate level of external reserve is estimated in the range of 5 months to 7 months of prospective extra-regional imports of goods and services. [9]

[5] With net proceeds of US$1.2 billion and US$1.1 billion respectively for Côte d'Ivoire and Senegal.

[6] The BCEAO's "operations account" at the French Treasury must hold at least 50 percent of the BCEAO's international reserves. The balance of this account earns interest equal to the marginal lending rate of the European Central Bank (ECB) of 0.75 percent. This balance may be negative without limit subject to an interest rate equal to the ECB's marginal lending rate beyond an overdraft greater than EUR 1.5 million. The unlimited overdraft facility is, however, intended to be used in exceptional circumstances.

[7] This fits within the 4 percent to 6 percent range estimated for all LICs in Fund ARA policy documents (see IMF: "Assessing Reserve Adequacy-Further consideration," November 2013).

[8] As has been customarily done for ARA estimates in previous consultations with the WAEMU and the CEMAC regions.

[9] The estimated range of 5 months to 7 months of imports is narrower than the estimated range of 5 months to 12 months presented in the Staff Report for the 2017 consultations with WAEMU, which was based on the same ARA-CC model but also on alternative values between 2 percent and 6 percent for the opportunity cost of holding reserves.

WAEMU: Estimation of Adequate Import Cover for External Reserves[1]

		Opportunity cost of holding reserves 2/	
		MPK	Eurobond yield
		4.0 3/	5.5 4/
Economic classification	Resource-Rich (RR) 5/	8.4	6.3
	Non Resource-Rich (NRR)	6.1	4.4
	Weighted Average (RR - NRR)	6.9	5.0

Source: Fund staff estimates

1/ Using the Fund's ARA-CC model, based on Dabla-Norris (2011).

2/ Estimated as the difference between a proxy based on the MPK or Eurobond yields for WAEMU countries and the rate of return on BCEAO's reserves.

3/ Estimated from data for WAEMU countries on the share of capital compensation in nominal GDP, available in the Penn World Table.

4/ Using Eurobond issued by Côte d'Ivoire and Senegal in 2017.

5/Within WAEMU, Burkina Faso, Mali and Niger may be classified as RR, according to the Regional Economic Outlook on Sub-Saharan Africa (October 2017). These three countries account for 33 percent of WAEMU's GDP and of extra-WAEMU's trade in 2016.

11. Based on the mid-point of the above range estimate the adequate import coverage of reserves for the WAEMU is lower than the adequate import cover of about 8 months estimated for the CEMAC by Fund staff in the context of its 2017 consultation. Such a difference in estimation results between the WAEMU and the CEMAC appears reasonable, given differences in resource dependency, level of economic diversification and balance of payment volatility between these two currency unions.

12. In practice, a reserve import coverage at the lower bound of the range of 5 months to 7 months estimated above could be adequate for the WAEMU, because the ARA-CC model does not account for the value of the convertibility guarantee of the XOF into the euro at a fixed parity by the French Treasury. This guarantee amounts, in principle, to an unlimited overdraft facility through the BCEAO's "operations account" and enshrined in the current monetary cooperation agreement between France and WAEMU countries, which was first signed in 1973 and later amended to reflect the adhesion of Guinea Bissau to the WAEMU in 1997 and the replacement of the French Franc by the Euro in 1999.[10] Such an overdraft facility thus possesses a degree of permanency and has therefore greater reserve-like features than other reserve credit lines made

[10] See: European Union Council: Decision 98/863/CE of 11/23/1998 concerning exchange rate matters relating to the CFA and Comorian Francs", which notes that "*the convertibility of the CFAF Franc is guaranteed by a budgetary commitment of the French authorities*" and recognizes the right of France to "*negotiate and conclude modifications to the present agreements to the extent that the nature or scope of these agreements is not changed.*"

available for only limited periods at a time by some international institutions to some of their members.

13. Much like external reserves, the French convertibility guarantee of the WAEMU's currency at a fixed parity to the euro acts as an insurance mechanism against the risk of temporary and exogeneous external liquidity shortfalls. It is not meant to be used to help sustain inadequate economic policies that maintain domestic demand at levels inconsistent with medium and long term external sustainability, including in response to likely permanent exogeneous shocks. Although difficult to quantify, the value of the French convertibility guarantee in reinforcing WAEMU's external buffers may be appreciated from a qualitative standpoint, including through the references made to it by rating agencies as a mitigating factor to the risk of balance of payment crisis.

Annex IV. Risk Assessment Matrix[1]

	Source of Risk	Relative Likelihood	Potential Impact
	Spillover Risks		
ST-MT	**Tighter global financial conditions:** Fed normalization and tapering by ECB increase global rates and term premia, strengthen the U.S. dollar and the euro vis-à-vis the other currencies, and correct market valuations. Adjustments could be disruptive if there are policy surprises	High	**Low to medium.** The region's exposure to global financial markets remains limited, but increased financing costs could adversely affect the region through higher regional risk premium and WAEMU countries which plan to tap international financial markets. A strengthening of US dollar relative to the Euro could increase sovereign debt burden of countries with un-hedged dollar exposures and increase costs of certain imports. On the upside, stronger USD could increase export receipts of certain exports (e.g., cocoa, oil)
ST MT	**Retreat from cross-border integration.**	Medium	**Medium to high.** The realization of this risk could lower foreign aid, trade, and foreign investment in the region.
ST- MT	**Weaker-than-expected global growth:** **Significant China slowdown and its spillover.**	Low/ Medium	**Medium to high**. Sharper-than-expected downturn in China could significantly lower trade and investment and affect WAEMU region through cross-border spillover effects from the Euro area and emerging markets.
MT	• **Structurally weak growth in key advanced economies.**	High	**Medium.** • Slower growth in advanced markets could lower trade, remittances, foreign aid and FDI. It could also dampen commodity prices and thus exports in some countries (e.g. gold, cocoa); a positive impact is expected for the region's current account deficit if mainly oil prices are affected. •
ST -MT	**Heightened risk of fragmentation/security dislocation in part of the Middle East, Africa, and Europe**, leading to socio-economic disruptions.	High	**Low.** Overall, the WAEMU region is a net oil importer. An increase in oil prices would adversely impact the current account balance.
	Regional Risks		
ST	Political and security risks, including regional spillovers.	Medium	**Medium to high.** Security risks in the Sahel include adverse impacts on capital and growth, delays in reforms, and increased fiscal cost and liquidity risks for the affected sovereign.
MT	Delay in reforms at country and regional level related to (i) fiscal consolidation (ii) infrastructure investment, (iii) the energy sector, (iii) PFM, (iv) the financial sector and (iv) regional integration.	Medium	**Medium to high.** Fiscal consolidation and key reforms are crucial. Weak implementation capacity poses risks to efficient reform implementation. With many countries targeting large infrastructure investments, a delay in PFM reforms and inefficient investment could raise debt, weaken fiscal and external sustainability, with negative implications for growth and poverty reduction. Delays in supervisory reforms may pose financial stability risks.
ST	Adverse weather conditions.	Medium	**High.** Lower agricultural production could imply heightened food security risks, inflation hike, growth slowdown, and increased fiscal costs.
MT	Exchange rate pressure in the CEMAC.	Low	**High.** Given similarities between the two zones (e.g., CFAF peg agreement, economic and policy challenges) pressures on the XAF could have spillover effects on the XOF

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

Annex V. Debt Securities Market

1. The WAEMU sovereign debt securities market expanded significantly after it was launched and direct central bank funding to Governments stopped after 2001. Securities are issued as T-bills or bonds (short to medium-term). Issuance has occurred via auctions and syndications, with bills issued exclusively through auctions while bonds may be issued through both regimes.

2. The market is effectively clustered along the issuance regime (auctions and syndication). While new issues may be fungible with the outstanding stock of the same type, they are not fungible across the issuance regime. Auctions are organized by the Agence UMOA Titres (AUT) and regulated by the BCEAO[1], with securities cleared and deposited at the BCEAO. By contrast, syndicated issues are facilitated and supervised by the market regulator CREPMF[2], with securities listed on the regional stock exchange BRVM[3], cleared and deposited at DC/BR[4], the central securities depositor associated with the BRVM.

3. Both types of securities are eligible to BCEAO refinancing but, in practice, banks have essentially submitted auctioned securities as collateral for refinancing. Auctions expanded rapidly in recent years on the back of short-term refinancing from the BCEAO, but sovereigns have turned recently more to syndications after monetary tightening curbed bank demand. Auctions represented the bulk of issuance in recent years. Syndications have consisted of larger amounts but their process is quite long, as securities are listed about 5 months after the issuance launch. Although meant for wide distribution and listed on the BRVM, syndicated securities have not attracted retail investors.

4. Despite efforts at lengthening maturities in recent years, the average issuance maturity has remained rather short. The average time to maturity increased from 2.9 years in 2014 to 3.6 years in 2016 but dipped back below 3 years in 2017. T-bills extend out to 24 months while longer sovereign bonds may extend up to 10 years. Bullet bonds have been gradually replacing amortizing medium-term bonds, and smaller scale 7 and 10-year bullet bonds were first issued in 2017. Nevertheless, the market remains dominated by short-term securities.

5. Primary dealers have been banks and brokers[5], several of which are affiliated with banks. Their main role has been to provide a reliable level of participation in primary market issuance, and to advise sovereigns. In practice, banks have underwritten auctions because SGIs do not hold a settlement account with the BCEAO. By contrast, regulation authorizes only SGIs to underwrite syndications because these bonds are meant for public placement, although they have not attracted much retail interest.

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[1] Banque Centrale des Etats d'Afrique de l'Ouest.
[2] Conseil Régional de l'Epargne Publique et des Marchés Financiers.
[3] Bourse Régionale des Valeurs Mobilières.
[4] Dépositaire Central / Banque de Règlement.
[5] Sociétés de gestion et d'intermédiation (SGI).

6. Banks have been the primary buyers of the sovereign issues, holding the bulk of the total outstanding with the remainder held by mutual funds or institutional investors. Bank demand for sovereign debt securities was fueled by a profitable carry trade, reflecting a high net margin between the yield and central bank refinancing costs. The institutional investor base does not appear deep enough to stimulate stronger non-bank demand for the securities. Hence, banks have been holding sovereign securities to maturity. There is also some home bias in primary underwriting, with many banks buying in priority their national sovereign debt.

7. The secondary market has remained shallow lacking both depth and liquidity. The turnover ratio for securities issued through auctions, including some initial primary placements, remains low. Buy and hold remains the dominant strategy for banks in the context of the narrow investor base. Thus, the current market structure does not offer a stable long-term funding such as for infrastructure investments. In addition, suboptimal practices and the fragmented infrastructure impede market liquidity. A regional strategy with full support from sovereigns and regional institutions could help tackle those impediments.

8. Foreign participation in the regional market has been marginal. Investor concerns include the illiquid secondary market, and the lack of adequate market infrastructure. Sovereign risks, which translate into non-investment grade ratings, have also deterred some foreign investors.

9. Recently, increased recourse by governments to syndicated bonds and to bilateral loans has reflected tighter primary liquidity and its uneven distribution among banking groups. There is need to develop market depth by broadening the investor base, which would also stimulate active secondary trading.