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Summary of Senegal Investment Climate Assessment

Since 1994, Senegal has experienced a steady average gross domestic product growth of 4.7 percent, a performance superior to the overall growth in Sub-Saharan Africa (which averaged 3.2 percent between 1994 and 2003). As of 2003/2004, this growth occurred within a stable macroeconomic framework, limited inflation, and contained budget deficits. Senegal's general business environment in Senegal is correct, and it leads many eastern African countries in terms of growth, productivity, and recent improvements in easing regulations.

Yet, several investment climate issues continue to curb Senegal's current and potential growth, including the low qualification the overall workforce, various difficulties in accessing finance, problematic regulation enforcement, and infrastructure inefficiencies.

This note summarizes the Investment Climate Assessment (ICA) undertaken in Senegal in 2004. The objective of the ICA was to analyze the current business climate in Senegal using a survey of a representative sample of 350 manufacturing and services firms.

Macroeconomic Environment and Productivity

Despite Senegal's record of sustained growth and major improvements in its business environment (several privatizations, improvements in the labor code, and a major tariff reform), structural deficiencies still remain that hinder its current and potential growth, including a significant trade deficit, irregular manufactured exports, and low foreign direct investment (FDI). FDI levels in Senegal are among the lowest in Africa at 1.46 percent of GDP compared with 2.3 percent for Sub-Saharan Africa as a whole in the 1994 to 2003 period. In effect, foreign investors have mixed views about the country. According to data from the World Economic Forum and Institutional Investor, Senegal remains in the last quarter of the rankings in 2003 (Table 1). However, as recognized by other rankings (such as Invest in Franc Zone), Senegal is well perceived as a moderate risk in terms of direct investment, financial risk, and political instability.

Such mixed perceptions among investors can partially be explained by the fact that productivity levels in Senegal, while still higher than in eastern Africa, have declined since the 1970s. Research suggests that in the mid-1970s, labor productivity was twice as high in Senegal as it was in South Korea and about 30 percent higher than in Thailand. Since the late 1970s, however, labor productivity has increased rapidly in the two Asian countries, while decreasing in Senegal. As a result, by the late 1990s, labor productivity was about five times higher in Korea and 10 percent higher in Thailand than it was in Senegal.

Nevertheless, as of 2002/2003 and in spite of such a decline, firms in Senegal remain among the most productive in Africa, with a relatively high labor and capital pro-

Figure 1. Unit Labor Costs in Senegal and Other Countries

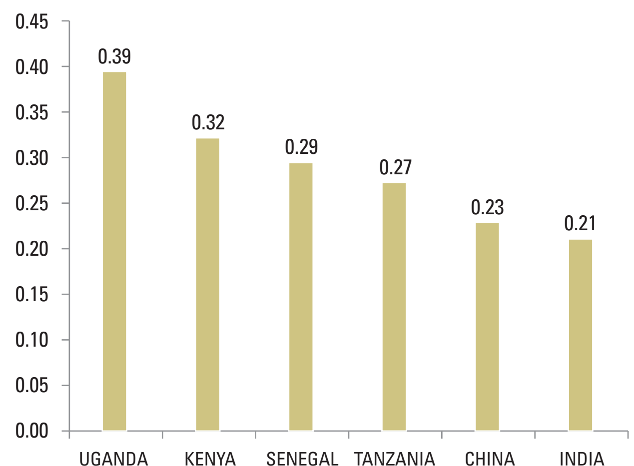


Table 1. Country Ratings.

	World Economic Forum 2003		Institutional Investor 2003		
	Growth Competitiveness Index	Business Competitiveness Index		Rank	Note Credit Rating
Best Performance			***Best Performance***		
Finland	*1*	*1*	*Swiss*	*1*	*95.3*
USA	*2*	*2*	*Luxemburg*	*2*	*94.3*
South Africa	*42*	*27*	*South Africa*	*40*	*52.4*
China	*44*	*32*	*China*	*34*	*60*
India	*56*	*37*	*India*	*48*	*49.4*
Senegal	***79***	***87***	***Senegal***	***76***	***27.6***
Uganda	*80*	*74*	*Uganda*	*85*	*21,4*
Kenya	*83*	*67*	*Kenya*	*82*	*22.1*
Worst performance			***Worst performance***		
Haiti	*102*		*Argentina*	*99*	*14.5*
Angola		*101*	*Zimbabwe*	*100*	*10.8*

Source: Global Competitiveness Report 2003–2004 and Institutional Investor, March 2003.

ductivity. Yet, this high productivity is offset by high wages, which reduce the competitiveness of Senegal as indicated by the relatively high level of the unit labor cost indicator (that is, wages adjusted for productivity levels). So, as shown in Figure 1, although Senegal is in a better position than countries like Kenya and Uganda, it still faces difficulties with respect to countries like China and India that are more productive and whose labor costs are lower.

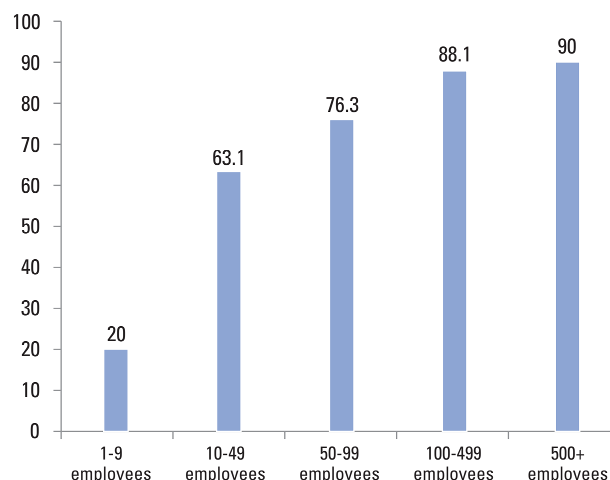
Key Investment Climate Constraints

Another element that sheds light on investor confidence in Senegal is the importance of the remaining investment climate constraints. Investment climate constraints in Senegal, by order of intensity, are related to factor markets, corruption, regulations, and infrastructure.

Constraints in the factor market include issues related to the financial and labor markets. The cost of financing and the difficulties in accessing it are the two most important individual constraints quoted by investors (64.5 percent and 55.2 percent of the surveyed firms, respectively). Access to finance (defined as the use of loans and overdraft) largely depends on the size of the firms. Smaller firms have less access to bank's finance, whether or not they export (Figure 2).

The formal labor market in Senegal suffers from several weaknesses as well. The workforce has a relatively low level of education (partly because only about a third of the firms

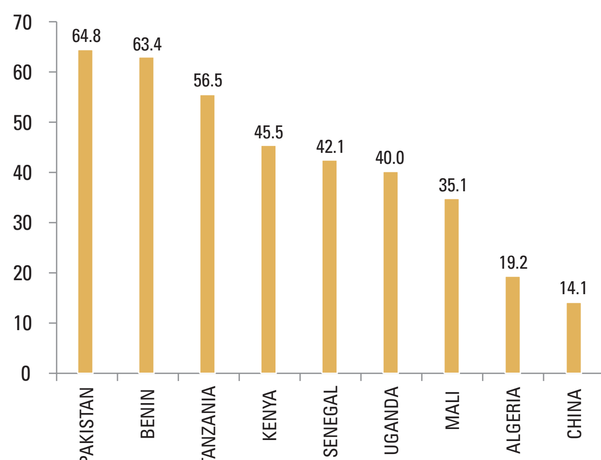
Figure 2. Access to Credit by Size.



provide training to their employees). In addition, the training provided does not always match the needs. Absenteeism resulting from health issues (malaria) remains non-negligible, and the average nominal wage level remains high for a developing economy, largely because of the wage-setting mechanism and regulations.

Corruption remains a major concern for almost 40 percent of the surveyed firms in Senegal. Senegal's performance is about average with respect to corruption when compared with other countries where surveys were con-

Figure 3. Percentage of Firms Identifying Application of Regulations as Inconsistent.



ducted—better than some (Kenya, Benin, or Mali) but worse than others (China or Turkey).

Regulations and their enforcement are yet another serious cause of concern and uncertainty for investors. Typically, entrepreneurs have a relatively low confidence in the enforcement of regulations and the ability of the judiciary. As shown in Figure 3, about 42 percent of the manufacturers consider that the enforcement of regulations by officials remains inconsistent, and 40 percent of them do not trust the judiciary to enforce their property rights. Here again, Senegal's performance is about average compared with other countries.

And, finally, infrastructure is a cause of concern for 30 to 36 percent of the companies. The road network, the waste disposal system, and the railroad network to sub regions and to Mali constitute a real handicap for firms in Senegal. Electricity supply remains irregular, further hampering efficiency. However, the intensity of the infrastructure constraints, though critical, remains lower than in many other African countries.

Policy Options

Despite numerous important reforms carried out during the last ten years, the investment climate in Senegal still suffers from several weaknesses that hinder private investment, productivity, and growth. Further reforms and measures are therefore necessary to enable a more competitive business environment. These reforms should aim at improving the working of factor markets, fighting corruption, further reducing the regulatory burden, and improving infrastructure. Priority should be given to reforms in the following areas:

Labor Market

- Improve dissemination of labor market–related information;
- Step up the fight against malaria to reduce absenteeism;
- Increase the output of the education system and professional training organizations to improve the overall level of qualification of the workforce; and
- Review and improve selected regulations of the labor code.

Financial Market

- Promote the use of better accounting procedures, especially for small and medium enterprises (SMEs);
- Review the regulations dealing with the accounting/auditing field to improve the quality of the audits; and
- Develop information on available financial products, especially export financing as firms often simply ignore their existence.

Corruption

- Strengthen the administration's internal and external control mechanisms;
- Revisit and improve the ancient legislative and regulatory framework dealing with these matters; and
- Implement microeconomic measures such as limiting employment duration for selected sensitive positions and reinforcing and effectively enforcing a corruption punishment system with high penalties.

Tax System

- Simplify the fiscal system and continue to reduce corporate and local taxes; and
- Improve capacity of the tax administration through additional training for staff and provision of new equipment, which will help to improve revenue collection and reduce the bureaucratic burden for firms.

Judicial System

- Strengthen the capacity of the Ministry of Justice;
- Increase the number of judges specialized in business and fiscal issues and promote the development of business courts;
- Upgrade computer equipment in courts; and
- Improve creditors' rights.

Infrastructure

- Finalize the development of a realistic and effective transport strategy for the country and, more specifically, for Dakar, to move firm output more efficiently; and
- Implement the Electricity Supply Efficiency Enhancement Project (ESEEP) to improve electricity supply.

This note is part of a series of summaries of analytical work of the Africa Private Sector Development Unit. This note is authored by Nadia Sandi based on a report entitled ***Senegal: Une evaluation du climat des investissements*** (March 2005). The report was written by a team in the Africa Private Sector Unit led by Jean-Michel N. Marchat, and including Jean-Paul Azam, George Clarke, Magueye Dia, and Mouhssine Affifi. For more information, contact Melanie S. Mbuyi via email at mmbuyi@worldbank.org or via telephone on 202 473 9574. A copy of the report is also available from www.worldbank.org/rped