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Seizing the Opportunity

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Acknowledgments

The Senegal Economic Update monitors significant recent economic developments in the country, highlighting the key structural challenges Senegal faces in its pursuit of inclusive and sustained growth, and analysing policy options.

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Executive Summary

Mounting international and regional uncertainties will require proactive actions to uphold hard-won socio-economic gains of the past decade. Political uncertainties linked to the presidential election affected economic activity during the second half of 2023 and in 2024Q1. Furthermore, international and regional financial markets have tightened, resulting in further deterioration of fiscal and external imbalances. There is an urgent need to build fiscal space and enhance Senegal's capacity to absorb shocks and address development challenges. Fiscal consolidation efforts will require an adjustment of 3.6 percent percentage points of GDP over 2024–25 to meet the West African Economic and Monetary Union (WAEMU) regional convergence criteria of a fiscal deficit ceiling of 3 percent of GDP. To achieve this, Senegal will have to accelerate the implementation of its Medium-Term Revenue Strategy (MTRS) to yield higher tax revenues and rationalize public expenditure while preserving essential investment and pro-poor spending. Pro-active efforts to address increasing macroeconomic imbalances, accelerate revenue mobilization, maintain a prudent borrowing strategy and proactive debt management, and ensure steadfast implementation of structural reforms will be crucial to help Senegal achieve its national development ambitions.

Raising tax revenues provides fiscal space to advance development objectives and plays a pivotal role in improving the living conditions of Senegalese. Senegal's poverty incidence stagnated over 2018/19–2021/22 while the absolute number of poor increased, reflecting the fact that growth has not necessarily reached the poor. Inequality has declined but only because consumption by poorer households fell less than the consumption of the better off, while middle-income households experienced an increase in consumption. Furthermore, the pace of poverty reduction is falling behind that of regional peers. Tightening financing conditions have led to higher public borrowing costs in the short and medium term, highlighting the urgent need to accelerate domestic revenue mobilization to finance Senegal's development ambitions. The Personal Income Tax (PIT) in Senegal has untapped potential to increase tax revenue – a stable source of revenue for macroeconomic stability and long-term development. This Senegal Development Update, therefore, focuses on (i) poverty and equity in a context of multiple crises, and (ii) options to boost tax revenue collection through the personal income tax.

Recent economic developments

Senegal's economy increased in 2023, driven by the resilience of the primary sector. Real GDP growth is estimated at 4.3 percent – 1.5 percent in per capita terms in 2023 – slightly above the 3.8 percent growth rate registered in 2022 and above initial projections of 4.1 percent. Political tensions, along with higher inflation and monetary tightening, disrupted the tertiary sectors and delayed some investments. On the demand side, investment growth decelerated, reflecting businesses delaying investments, while declining purchasing power associated with high led to a relatively contained private consumption. On the supply side, the tertiary sector decelerated due primarily to reduced commercial activities in restaurants and hospitality, information and communication technologies (ICT), and a downturn in financial and insurance services with the impacts of social unrest and political tensions. Despite challenges in the extractive sector, Senegal's secondary sector thrived with the positive contributions of cement production.

After reaching a record high of 9.7 percent in 2022, inflation declined to 5.9 percent. Declining international commodity prices and the normalization of supply chains drove the decline in headline inflation as external factors, such as the depreciation of the FCFA against the US dollar in 2022 and its pass-through via imported and local prices, eased. Most administrative measures to cap prices on certain food items, including rice and sugar, remain in place to combat inflation and ease the cost of

living. Pressures from energy prices, including electricity, gas, and other fuels (which increased by an average 10 percent in 2023) weighed heavily on inflation.

Fiscal consolidation envisaged in the 2023 budget law materialized, but fiscal deficit was higher-than-expected. The fiscal deficit narrowed to 5.1 percent of GDP in 2023 from 6.6 percent in 2022, remaining slightly above the 4.9 percent of GDP target set in the 2023 Budget Law. Tax revenue increased to 19.4 percent of GDP – about 1.2 percentage point above its 2022 level, owed primarily to higher revenue collection on taxes on goods and services and higher personal and corporate income tax. Public expenditure remained similar to its 2022 level at 26.6 percent of GDP. Measures to support purchasing power[1] (0.6 percent of GDP) and energy sector subsidies encompassing outstanding arrears (4.2 percent of GDP at end-September 2023) continue to weigh on fiscal consolidation efforts. As a result, public and publicly guaranteed debt increased from 75.6 percent of GDP in 2022 to 80.8 percent of GDP, in 2023 – equivalent to 17.2 percentage points of GDP above pre-pandemic (2019) levels. Senegal remains at moderate risk of public debt distress, with limited margins to absorb potential future shocks. Per its medium-term debt management strategy, Senegal intends to increasingly reorient market financing towards the regional market due to tighter financing conditions on the international bond market with decade high monetary interest rates in advanced economies.[2]

The current account deficit (CAD) improved significantly, increasing international reserves. The CAD is estimated to have improved from 19.9 percent of GDP in 2022 to 14.5 percent of GDP in 2023, primarily driven by the resumption of trade with Mali and a gradual reduction in service imports in the hydrocarbon sector. The CAD was financed from foreign investments, remittances, and partner support, with reserve withdrawals also covering the gap, which strained the BCEAO's reserves.

To counter inflation, the Central Bank of West African States *(Banque Centrale des États de l'Afrique de l'Ouest,* BCEAO) has raised its policy interest rates by a cumulative 150 basis points since mid-2022 to 3.5 percent for liquidity calls and 5.5 percent for the marginal lending facility. Still, the monetary policy stance remains broadly accommodative. Inflation in the region (average of 3.7 percent in 2023) is still above target, and foreign exchange reserves have been on a downward trend, estimated at 3.5 months of imports at end-2023, down from 4.3 months at end-2022. Credit growth accelerated from 29.3 percent in 2022 to 32.3 percent of GDP in 2023. The financial sector has shown resilience despite multiple crises, and domestic, regional and global uncertainties, posting declining non-performing loans.

Outlook, risks and challenges

The outlook remains broadly positive, but it hinges on a solid commitment to macroeconomic stability. The growth outlook relies on the implementation of Senegal's development agenda focused on improving economic opportunities and social inclusion. The outlook also relies on the tapering of current domestic and global geopolitical tensions, resumption of the global economic recovery and trade in the medium run, and improved regional stability. The government will have to commit to restoring macroeconomic stability and build buffers to enhance debt sustainability by implementing a revenue-based policy and rationalization of public spending. This will demonstrate a strong commitment to fiscal consolidation starting in 2024, aiming to achieve WAEMU's fiscal target of 3 percent by 2025. Short-term growth is expected to accelerate to 7.1 percent in 2024 and average 7.7 percent in 2025–26. Poverty (the international extreme poverty line, defined as $2,15 per day in 2017 PPP) is expected to fall to 8.7 percent in 2024 (1.1 percentage points lower than in 2023) driven by real per capita growth in agriculture, where 57 percent of the poor are employed, and a reduction in inflation,

[1] The measures include the payment of compensation of FCFA 15 billion (US$22 million) due to millers, payment of subsidy to paddy rice importers (FCFA 30 per kilogram; US$0.046 per kilogram), a subsidy of 32 FCFA (16.5 percent of the price) on the kilogram of paddy rice aimed at supporting local producers, and tax exemptions on fatty substances applied to importers.

[2] Senegal Medium-term debt management strategy https://www.sentresor.org/publication/strategie-de-gestion-de-la-dette-a-moyen-terme-2023-2025/

especially among food items. Despite headwinds, poverty reduction should continue in the medium term, reflecting improved economic opportunities, especially for the youth.

Overall, domestic, regional, and global uncertainties are high, tilting the risks to the downside. The context of a poly-crisis and their negative effects on the national economy still prevail. Protracted global geopolitical tensions are leading to persistently higher-than-expected inflation and could result in higher poverty and an even more aggressive monetary stance, further constraining government financing, and exacerbating debt vulnerabilities. There are regional security and political uncertainties with severe socio-economic implications, including the risk of the Alliance of Sahel States (ASS)'s withdrawal from ECOWAS, which will impact exports to Mali, constituting 20 percent of Senegal's total exports. Social discontent, stemming potentially from the phasing out of energy subsidies could endanger the envisaged fiscal consolidation. At the same time, delays in effective fiscal consolidation could severely affect debt sustainability and growth.

Spotlight 1: Poverty and equity in a context of multiple crises

Senegal has coped relatively well in the context of multiple shocks, with the poverty incidence remaining relatively unchanged at 37.5 percent in 2021/22 from 37.8 percent in 2018/19 despite the Pandemic. Poverty incidence (using the national poverty line) is stable in urban and rural areas but with contrasting regional trends.[3] There has been a marked reduction in poverty in the Senegal River Valley (center) and in eastern Senegal bordering Mali, and a slight increase in the south in Casamance. While middle-income brackets experienced a gain in real consumption per capita, both the poorest and the better-off experienced declines in consumption, with the better-off experiencing greater declines in consumption. This trend resulted in a decline in inequality, with the Gini index dropping from 35.1 percent in 2018/19 to 33.4 percent in 2021/22, suggesting a slight improvement in inequality. The poverty gap and the squared poverty gap declined slightly in urban areas while rising slightly in rural areas, where poverty levels are already higher. As a result, the living standards of poor households have generally not deteriorated in urban areas, while they have been deteriorating somewhat in rural areas.

Poor Senegalese are still concentrated in rural areas with a relatively high concentration in the groundnut basin. Senegal had 17.4 million people in 2021/22, 6.5 million of whom living below the poverty line. Three quarters of poor people still live in rural areas, as it was the case in 2018. The regions of Diourbel, Kaolack and Thiès in the groundnut basin are home to almost one third of the country's poor, due to the combination of being regions with large population and high average poverty rates. On the other hand, Tambacounda and Kedougou in the east of the country have respectively 9 percent and 2 percent of poor people, despite the very high poverty rates that characterize these regions. In fact, each region, except for Kedougou (because of its small population), is home to at least 5 percent of the poor. Consequently, if the objective of policies is to reduce the number of poor, the targeting of anti-poverty programs must be directed to all regions, including Dakar.

The observed decline in consumption per capita was mostly felt by better-off households. Between 2018/19 and 2021/22, average per capita consumption fell by 1.6 percent per year, while it grew slightly for the poorest 40 percent of the population, with an annual growth rate of 0.11 percent. As a result, there was a gain in shared prosperity of almost 1.3 percent, i.e., which means that the average consumption of the poorest 40 percent of the population has moved closer to that of the population as a whole by an average of 1.3 percent per year. However, it is important to note that this increase in shared prosperity results from a decline in consumption of better-off households rather than from a real gain in consumption for the poorest. In fact, households in the bottom 10 percent of the distribution, including in rural areas, experienced losses in consumption.

[3] The national poverty line is 369,666 FCFA per person per year in 2021/22, rising from 333,441 FCFA in 2018/19. Data come from the EHCVM (*Enquête Harmonisée sur les Conditions de Vie des Ménages*).

The average growth rate of the poorest was less negative than that of the better-off, which led to a decline in inequality at the national level and also in urban and rural areas. At the national level, the Gini index, one of the best-known inequality indicators, fell by 1.7 Gini points, from 35.1 in 2018/19 to 33.4 in 2021/22. While the average per capita consumption of the richest 20 percent represented 5.5 times that of the poorest 20 percent in 2018/19, this ratio declined to 5.2 in 2021/22. However, this decline reflects a loss in consumption (in real terms) among better-off households, largely in urban areas, rather than the increase of consumption of the poorest. Inequality has declined in both urban and rural areas.

Spotlight 2: Options to raise tax revenue from personal Income Tax (PIT)

Improving domestic revenue mobilization (DRM) is critical for Senegal to achieve its development ambitions. Between 2014 and 2019, Senegal was one of the most dynamic economies in Sub-Saharan Africa (SSA). GDP growth averaged 6 percent over 2014–19, one of the highest in SSA, and real GDP per capita increased by 17.9 percent during the same period. To finance its development ambitions, it is imperative to sustain investments in human capital and infrastructure, and boost productivity. Insufficient revenue has often reduced Senegal's ability to improve and sustain growth and invest in people, and revenue shortfalls have meant resorting to debt accumulation, raising fiscal vulnerabilities and limiting fiscal space to absorb shocks.

Senegal's tax revenue growth and buoyancy steadily improved over the past decade, surpassing its peers, but revenues remain below their potential. Tax revenue was stagnant at around 15 percent of GDP over 2010–18 before increasing gradually to 16.8 percent in 2020 and 18.2 percent of GDP in 2022—its highest level ever. This compares with an average of 15.7 percent of GDP for SSA countries, 13.6 percent of GDP for Lower Income Countries (LICs), and about 34 percent of GDP for OECD countries).[4] However, this relatively good performance is insufficient to boost Senegal's ability to address the development needs of its population and fostering resilience against uncertainty. Limited and increasingly constrained fiscal space hinders productive investment and efforts to ensure resilience against future shocks. Like most low- and middle-income countries, Senegal relies heavily on indirect taxes, constituting 71 percent of total tax revenues in 2021, although reliance on trade taxes for revenue collection has declined. There is an opportunity to strategically leverage the direct tax system to enhance domestic resource mobilization.

The PIT yields little revenue, and its contribution to total tax revenue has stagnated over the past decade due to a narrow tax base and lack of reform momentum. The PIT has increased over the past 3 decades, but it yields little revenue at 2.8 percent of GDP in 2021, much lower than the Organization for Economic Co-operation and Development (OECD) average of 8.3 percent of GDP although better than the average of WAEMU (0.82 percent of GDP) and ECOWAS (1.38 percent of GDP). The contribution of PIT revenue to total tax revenue was stagnant at 15 percent between 2010 and 2021 despite several reform attempts, while aspirational peers successfully increased the contribution of PIT revenue to total tax revenue over the same period. The tax base remains narrow with a limited number of taxpayers filing tax returns and low levels of formality. The levels of formality for both jobs and businesses are particularly low, with worrying signals of deterioration in 2022, with only 12.5 percent of wage workers being formal as the post-COVID-19 recovery seems to have brought lower quality jobs. In fact, only one-third of workers in the top-income decile and less than one-fifth of businesses, are formal. The low and even decreasing levels of formality erode the tax base, weakening the capacity of PIT to contribute to tax revenues. The PIT system faces low compliance, in the absence of a strong data-driven approach.

Accelerating tax administration and policy reforms on PIT can help boost domestic revenue mobilization efforts. Informality, narrow tax base, and limited enforcement hinder the capacity of direct taxes to

[4] https://www.oecd.org/tax/tax-policy/revenue-statistics-highlights-brochure.pdf

increase revenues and redistributive pre-fiscal inequalities. Apart from PIT, other direct taxes on capital, property and rents are subject to low and non-progressive tax rates. Taxes on capital, property taxes, and taxes on profits for small firms—CGU are subject to low and non-progressive tax schedules, limiting the redistributive capacity of direct taxes. The MTRS 2020–25 implementation and ongoing revenue administration reforms have strengthened tax mobilization capacity, thanks to efforts toward digitalizing tax and customs processes and expanding the tax base. However, more can be done to enforce filing of personal income taxes. Microsimulations show that clarifying the legal framework for tax declaration on all sources of income and enforcing tax filing would increase revenues without increasing poverty and inequality. Digitalizing the tax administration to reduce the cost of compliance, improve taxpayer monitoring, strengthen enforcement, data, and an evidence-based approach could yield revenues closer to their potential.

Chapter 1:
The State of the Economy

1.1. Recent developments

Moderate global and regional economic growth in the face of ongoing monetary policy tightening and challenging financing terms

Global economic growth slowed for a second consecutive year in 2023 amid continued tightening of monetary stance and credit conditions. The global economy experienced its second consecutive year of slowdown, with growth dipping to an estimated 2.6 percent, down from 3 percent in 2022.[5] This growth deceleration was primarily driven by the extended impact of stringent monetary policies aimed at curbing high inflation, alongside tighter credit conditions and diminished trade and investment activities. Recovery trajectories varied significantly across regions, with advanced economies showing more resilience and stronger growth dynamics than emerging markets and developing economies (EMDEs). EMDEs faced ongoing challenges related to the pandemic's lingering effects and elevated debt burdens. Despite lessening, inflationary pressures persisted, particularly in terms of food and energy prices, which remained stubbornly high across many advanced economies. Even as monetary tightening began to ease, real policy interest rates continued to be elevated, slowing the pace at which inflation could return to target levels. The year also marked a significant downturn in global trade growth, reaching its lowest point in five decades, in part due to a contraction in goods trade and a slower-than-anticipated recovery of services trade. Moreover, geopolitical tensions and recent conflicts added layers of complexity, disrupting essential shipping routes and amplifying the risk of further inflationary bottlenecks.

Economic growth in Sub-Saharan Africa (SSA) slowed from 3.7 percent in 2022, to an estimated 2.9 percent in 2023. This moderation in growth was driven by a mix of country-specific challenges, including increased business input costs in Nigeria and an acute energy crisis in South Africa. The region's overall economic momentum was dampened, with the combined growth of its three largest economies—Nigeria, South Africa, and Angola—averaging just 1.8 percent, influenced by decreased growth among metal-exporting countries and falling global metal prices. The region's economic landscape was further strained by sustained conflicts, particularly in Sudan, and new outbreaks of violence in Chad and Niger, leading to heightened regional instability. These conflicts, coupled with a slower post-pandemic recovery affected by reduced external demand and stringent domestic policies to curb inflation, significantly impacted economic activity. Despite a slight moderation, inflation in SSA remained high, influenced by the prior year's surge in food and energy prices, underlining the ongoing challenge of balancing growth with inflation control amid persistent poverty and external vulnerabilities.

The Senegalese economy remained resilient in 2023 despite heightened domestic, global, and regional turmoil, coupled with high inflation

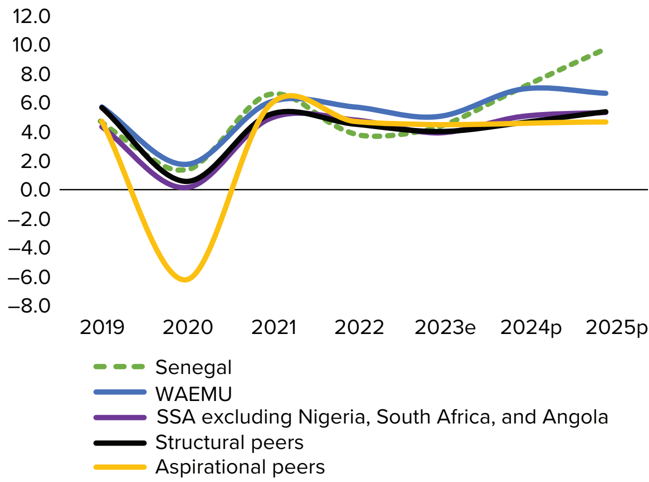
Economic activity accelerated in 2023 owing to a dynamism of the primary sector. Real GDP growth is estimated at 4.3 percent (1.5 percent in per capita terms) in 2023 from 3.8 percent in 2022[6] and above the initially projected level of 4.1 percent (1.4 percent in per capita terms) and below Senegal's aspirational peers (Figure 1.1.a). Political tensions coupled with higher inflation and monetary tightening, disrupted the tertiary sectors and led to reductions in growth in investment. On the demand side, private investment growth fell to 7.1 percent from 20.8 percent reflecting businesses delaying investments due to

[5] World Bank (2024). Global Economic Prospects, January 2024. Washington, DC: World Bank. doi:10.1596/978-1-4648-2017-5

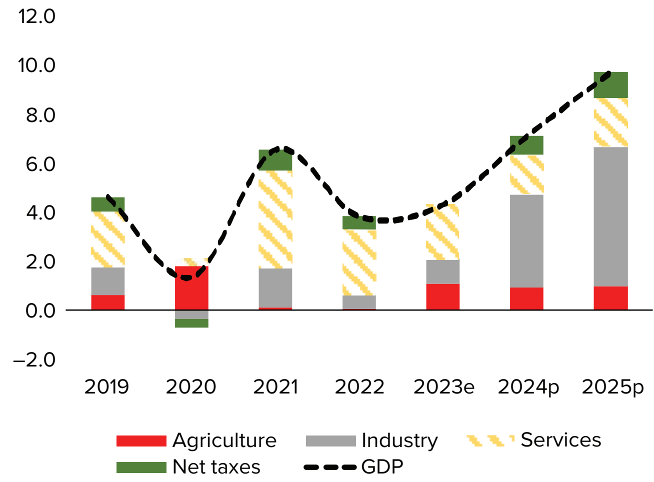
[6] The Senegalese authorities have revised down the 2022 growth data to 3.8 percent (1.2 percent in per capita terms) from 4.2 percent (1.4 percent per capita), revealing a less robust economy than initially estimated. This adjustment is primarily attributed to growth rate revisions in exports. Per the revisions, exports growth underperformed at 3.5 percent – more than 2 times lower than previous estimates of 8.1 percent. The latter was attributed to the decline in gold production (–7.6 percent year-on-year) and a slowdown in agricultural production (0.3 percent year-on-year).

Figure 1.1. Recent economic developments

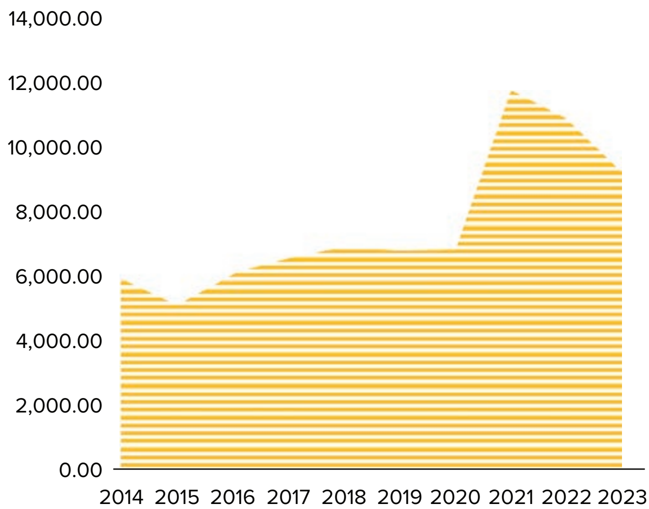
a. Senegal real growth remained below peers in 2023 . . .



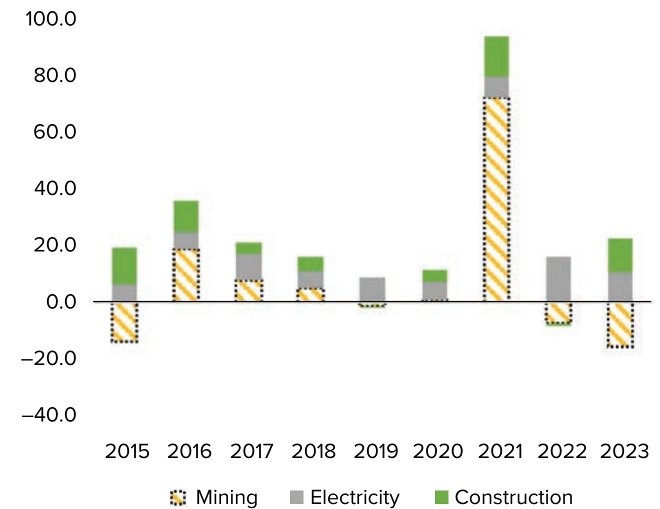
b. . . . due to adverse shocks that affected the services sector . . .



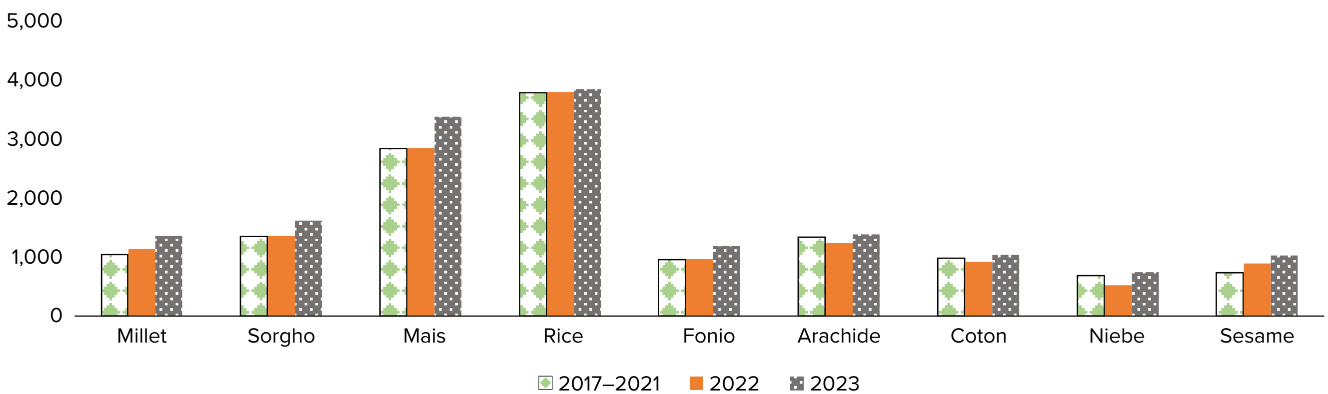
c. . . . and a sharp decline in annual gold production.



d. However, despite a contraction in mining, the industry sector thrived with the positive contributions of cement . . .



e. . . . while the agriculture production rebounded and emerged as a positive driver of growth.



Source: World Bank staff calculation, ANSD, Ministry of Economy.

political uncertainty and persistent inflation. Private consumption growth also increased marginally to 4.1 percent in 2023 from a growth rate of 3.5 percent in 2022 as consumers contained spending due to declining purchasing power associated with high levels of inflation and concerns about the future direction of government policy and the overall economic environment.

On the supply side, the tertiary sector is estimated to have experienced a slowdown in 2023. The tertiary sector decelerated from 5.1 percent in 2022 to 4.2 percent in 2023, due primarily to decreased commercial activities, reduced performance in information and communication, restauration, and a downturn in financial and insurance services. Following social tensions, the authorities imposed restrictive measures on the internet, urban, and maritime transport during the first nine months of 2023, impacting trade, telecommunications, and transportation sectors. The general activity index in the ICT sector declined by –6.5 percent (year-on-year) in 2023 compared to 2022, grappling with the aftermath of social unrest in June 2023 that led to the suspension of access to mobile internet and restricted television signals. The restaurant and hospitality service sectors experienced a significant downturn, with activity declining by 19.8 percent between the first and second quarters of 2023. This is primarily due to a pronounced underperformance in the hotel industry, which saw a sharp of 28.3 percent decline, affected by the adverse impact of the social unrest. On an annual basis, the sector recorded a 3.4 percent decrease in activity in the second quarter of 2023, with both the hotel and restaurant segments contributing to this downturn, registering declines of –3.4 percent and –3.3 percent respectively. Furthermore, in the second quarter of 2023, the financial and insurance activities sector experienced a quarterly decrease of 1.1 percent, primarily driven by a sharp decline of 39.4 percent in auxiliary financial and insurance services. Meanwhile, in the transportation sector, port and auxiliary activities fell by 6.7 percent, and road transport declined by 6.8 percent over the same period.

The secondary sector thrived with the positive contributions of cement production, despite challenges in the extractive subsector. Gold production, which accounts for 50 percent of the extractive production, witnessed a significant downturn, registering a 15.5 percent (year-on-year) decrease in 2023 compared to 2022 (Figure 1.1.b and c), attributed to lower global demand and depleted reserves. Additionally, labour strikes against changes in regulations for recruitment processes at the region's mining companies further hampered production. This decline follows a preceding year of contraction, with gold production experiencing a –7.6 percent (year-on-year) decline in 2022 compared to 2021, primarily due to lower market demand.[7] Similarly, phosphate production faced contraction in 2023, declining significantly by 20.4 percent compared to 2022.[8] This fluctuation in phosphate production reflects industry-specific challenges and fluctuations in market demand. Cement sales rose by 8.7 percent in the first nine months of 2023, compared to the same period in 2022, boosted by strong domestic demand with the implementation of major public infrastructure projects, notably the Bus Rapid Transit, the program to build auto-bridges to alleviate traffic congestion on major arteries, the continued development of the Diamniadio urban hub, as well as social housing programs.

The buoyancy of the primary sector played a positive role in overall economic growth in 2023. Total cereal production increased by 16 percent increase (year-on-year), reaching 4,255,352 tonnes,[9] reflecting a strategic shift towards more intensive farming practices. Millet production rose by 23.3 percent, while sorghum and rice also reported gains of 22 percent and 8 percent, respectively. The agricultural sector also benefitted from the performance of groundnut production, expected to rise by

[7] This negative trend emerged after a remarkable upswing in gold production in 2021, boasting a substantial +72 percent year-on-year increase relative to 2020.

[8] This decline followed a modest 0.8 percent year-on-year increase in 2022 compared to 2021 and a more robust 3.7 percent year-on-year increase in 2021 compared to 2020.

[9] The National Agency of Statistics' report on the 2022/2023 agricultural campaign.

15 percent year-on-year, as well as from the dynamism of seed cotton (+7 percent increase year-on-year). These positive developments could be attributed to a combination of factors including a favourable weather conditions and supportive government policies as part of the Agricultural Program for Sustainable Food Sovereignty (PASAD) through improved irrigation systems and the increase in the budget envelope. The latter enables—among others—the provision of subsidies for high-quality seeds and fertilizers, which may contribute to improved agricultural productivity, although the exact impact on yields can vary based on several factors. The impact of these policies was further amplified by the introduction of Community Agricultural Domains, improvements in agricultural infrastructure and the adoption of advanced technologies, which together have significantly enhanced horticultural production and the sector's overall productivity.

The fisheries and breeding sector demonstrated a substantial recovery. Production in the fisheries sector increased by 4.5 percent year-on-year in 2023, driven by a 6.3 percent year-on-year upswing in artisanal fishery, coupled with a 1.3 percent year-on-year rise in industrial production during the same period. This positive trajectory stands in stark contrast to the sector's struggles in 2022, which was marked by an overall growth contraction of −5.8 percent year-on-year, and a contraction of −13.9 percent year-on-year,in fish production. Artisanal sector benefited from more favourable weather conditions, which led to substantial fishing efforts. Similarly, the breeding production sector recorded an improvement in its growth rate, at 3 percent year-on-year in 2023, contrasting with the modest 0.3 percent year-on-year growth in 2022 compared to 2021. This positive momentum follows a contraction of −3.8 percent year-on-year in 2021 compared to 2020. The noteworthy upturn in 2023 indicates a promising shift towards increased productivity within the breeding production industry, which could indicate that the subdued growth in 2022 appears to have been surpassed, reflecting potential adjustments in the sector's practices attributable to efforts under the National Livestock Development Plan (PNDE).

Amid declining inflation, the monetary stance remains accommodative, while the financial sector has so far remained resilient

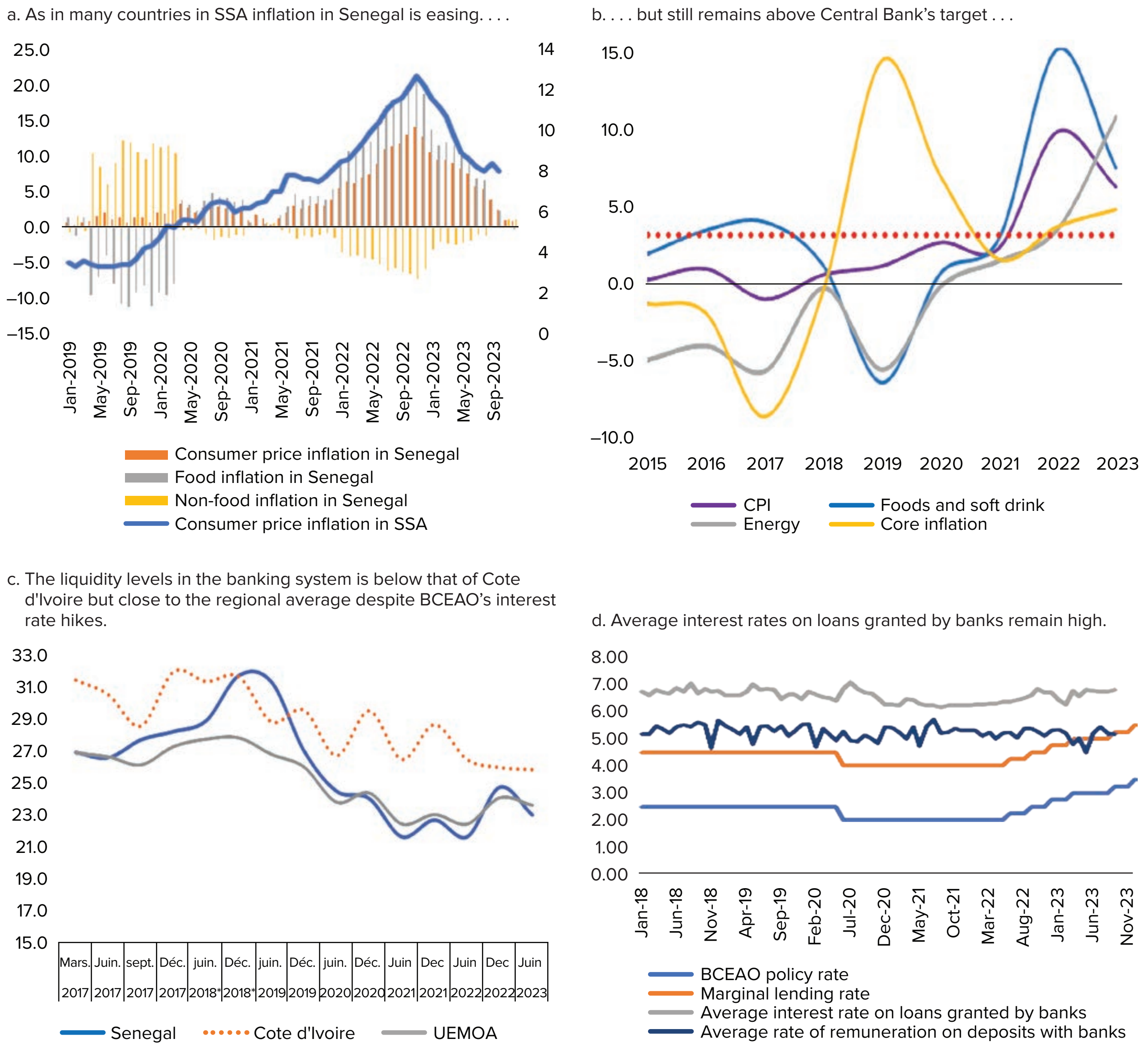
Annual inflation eased at 5.9 percent in 2023, from 9.7 percent in 2022 – but remains above the 3 percent regional target. As in many SSA countries, headline inflation in Senegal eased in 2023 compared to 2022 (Figure 1.2.a). Declining international commodity prices and the normalization of supply chains contributed to the reduction in inflation, with food prices having a declining contribution to inflation by 3.8 percentage points. Electricity, gas, and other fuels were the main drivers of inflation, with a 10.6 percent increase in the prices of these products (Figure 1.2.b). Price caps on essential food staples and fuel subsidies constrained further upward pressure. The inflation rate in Senegal remains more than twice the 3 percent upper bound of the BCEAO's 1–3 percent target and above the 3.7 percent average of the WAEMU region[10] in 2023 (Figure 1.2.b) – it is lower than regional non-WAEMU peers, including The Gambia and Ghana.

High inflation has cast a shadow on poverty reduction, affecting disproportionately the poorest. Poverty measured at the international extreme poverty line[11] is estimated to have remained stable at 9.9 percent in 2023 from 10 percent in 2022. While the expansion of agriculture, which employs a significant part of the labor force, likely improved household welfare in rural areas, the lower-than-expected economic recovery coupled with higher prices eroded households' purchasing power, counteracting this effect. The national poverty trend results from increased poverty in urban areas (0.03 percentage points), while the poverty rate slightly decreased in rural areas (−0.3 percentage points). Spotlight 1 provides an update on Senegal's progress in reducing poverty and improving shared prosperity in the context of multiple crises.

[10] The West African Economic and Monetary Union (WAEMU) aims to maintain regional stability and convergence through various monetary policies, including a central bank inflation target of less than 3 percent. This target is crucial for ensuring price stability across member states, which is a key factor for economic harmony and regional integration.

[11] $2.15 per capita per day in 2017 PPP.

Figure 1.2. Inflation, its drivers and liquidity levels in the banking system



Source: World Bank staff calculation, UEMOA-Titres, 2024, BCEAO.

Monetary policy reforms remain accommodative, but the tightening of financing conditions hold potential for accelerating growth. Senegal's monetary policy, guided by the Central Bank of West African States (BCEAO), prioritizes reducing inflation and maintaining the stable peg of the FCFA to the Euro. Although, the policy interest rates rose by a cumulative 150 basis points since the start of 2022 to 3.5 percent for liquidity calls and 5.5 percent for the marginal lending facility, the monetary stance remains broadly accommodative with rates remaining low enough to spur strong economic growth. In the context of regional and global turmoil, the monetary stance was

necessary to contain the impact of several macroeconomic risks, including regional uncertainties, continued inflationary pressures, and constrained external financial conditions. In response to financial stability risks stemming from budgetary constraints among the Union's member states and liquidity challenges in the government securities market, BCEAO conducted two buyback operations on the secondary market in 2023. These operations amounted to about FCFA 2 billion for all member states of the Union, with FCFA 437.1 billion allocated to the State of Senegal.

Senegal's financial system has so far proved resilient, despite multiple crises, domestic, regional and global uncertainties. NPLs[12] continued their downtrend and have stabilized 10.1 percent in June 2023 (compared to 9.3 as of December 2022 and 11.5 percent in December 2021) – remaining slightly higher than the WAEMU region average of 8.7 percent. The provisioning ratio in Senegal, which indicates the percentage of NPLs covered by funds set aside to absorb potential losses, has been steady at 64.5 percent as of June 2023.[13] This suggests that banks are consistently prepared to cover a significant portion of potential losses from non-performing loans. The liquidity levels in the banking system are still relatively high, although below that of Cote d'Ivoire (Figure 1.2.c). Liquid assets make up 23 percent of total assets as of June 2023, which is close to the regional average of 23.6 percent. However, there may be liquidity challenges at individual banks, and banks continue to depend heavily on central bank funding to maintain their large securities portfolios, which accounted for 22 percent of their assets in 2022 according to the WAEMU Financial Sector Assessment Program.

Credit to the private sector maintains a strong recovery pace. After credit to the economy grew by 6.9 percent in 2021 and by a substantial 26.1 percent in 2022, the proportion of credit to the private sector relative to the country's GDP also increased, rising from 29.3 percent in 2020 to 32.3 percent in 2023. The total credit to total deposit ratio, which measures how much banks are lending out compared to the deposits they receive, was 82.16 percent in June 2023, which is relatively stable compared to 2022's ratio of 80 percent. However, despite the recent stability, there has been a steady decline in the credit to deposit ratio since 2019, when it was 97.4 percent before the pandemic. This downward trend could suggest that banks have become more conservative in their lending practices or increasing deposit taking.

Fiscal and debt vulnerabilities have increased in the context of tightening financing conditions, high energy subsidies and improved revenue performance

The fiscal deficit narrowed to 5.1 percent of GDP in 2023 – slightly above the target of 4.9 percent, due to higher-than-expected domestic revenue. In its effort to align with the WEAMU target of a 3 percent fiscal deficit by 2025, the government revised its ambition for its fiscal deficit goal for 2023 to 4.9 percent of GDP from 5.5 percent of GDP in the initial Budget Law. These fiscal consolidation efforts were expected to be driven by higher tax revenue collection with the implementation of the MTRS and streamlined public expenses and energy subsidies. However, high-frequency monthly fiscal data reported a fiscal deficit of 5.1 percent of GDP at end-2023 thanks to higher-than-expected domestic revenue. With efforts made in containing expenses, total expenditures stagnated at 26.6 percent of GDP in 2023 while total revenue and grants are estimated to reach 21.6 percent of GDP in 2023, from 21.6 percent of GDP in 2022, thanks to higher tax revenue and grants.

Tax revenues, estimated at 19.4 percent of GDP in 2023 – 1 percentage point above the target in the 2023 initial budget law. Direct taxes are estimated at 6.9 percent of GDP in 2023, from 6.3 percent of GDP in 2022. During the first half of the year, there were increases in corporate tax payments from firms in the secondary sector. This was fuelled by a significant rise of +25.4 percent year-on-year

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[12] Gross NPLs are loans on which borrowers are failing to make payments.

[13] In addition, the NPL ratio for Microfinance Institutions in Senegal has also improved, reaching 7.3 percent as of June 2023, down from 9.5 percent in 2021. This improvement suggests that the microfinance sector is also experiencing a reduction in the proportion of loans that are not being repaid on time.

in corporate income tax in the construction sector (BTP). However, the performance of this sector was moderated by a contrasting trend in the second half of 2023, where there was a 3.1 percent year-on-year decline in corporate income tax paid by the telecommunication sector. Regarding indirect taxes, taxes on goods and services are estimated at 9.5 percent of GDP in 2023, a 0.6 pp increase from 2022, reflecting vigorous of domestic VAT and consumption tax collections. Tax on international trade also underperformed in 2023 at 2.6 percent of GDP from 2.8 percent of GDP in 2022, mainly due to poor agricultural season of the previous year and declining gold exports. Ambitious tax reforms are needed to improve domestic revenue mobilization to reach the non-oil tax revenue target of 20 percent of GDP by 2025. The tax system remains complex with a narrow tax base and high tax rates, encouraging avoidance and discouraging formalization. In addition, VAT suffers from multiple rates and exemptions that weaken its neutrality and efficiency. Moreover, auditing practices could be strengthened to broaden the tax base (cf. Chapter 2). Grants are estimated at 1.0 percent of GDP in 2023, relatively unchanged from 2022.

Public expenses remained stable reflecting higher wages and interest payments along with arrears in energy subsidies. Total expenditures are estimated at 26.6 percent GDP in 2023, similar to its level in 2022. The increase in wages, interest payments and arrears in energy subsidies was somehow offset by relative decline in goods and services and current transfers. Wages are estimated at 7.0 percent of GDP in 2023, from 6.6 percent of GDP in 2022, following an increase in the workforce and salary revaluation while interest payments are estimated at 3.1 percent of GDP in 2023, from 2.2 percent of GDP in 2022. Furthermore, direct subsidy compensations for the energy sector, including outstanding arrears, amounted to FCFA 792 billion (4.2 percent of GDP) as of September 2023, equal to the estimated amount of energy subsidies in 2023 if no energy reforms and roadmap were implemented (Box 1). With the adoption of that roadmap, energy subsidies should have been capped at 2.7 percent of GDP in 2023 and 1 percent of GDP in 2024. Energy subsidies are anticipated to be even higher in December 2023 following the revision of electricity tariffs in November 2023 to ease consumers' financial burdens from the January 2023 increase with the removal of the third consumption tranche.

Total public debt surged to 80.8 percent of GDP in 2023 – from 76.0 percent in 2022 – and Senegal remains at moderate risk of external and overall debt distress with very limited capacity to absorb shocks. This increase is primarily due to over-financing of the 2023 budget at 4.6 percent of GDP – positioned as a debt strategy to hedge against potential financing challenges in early 2024 particularly surrounding the presidential election to ensure the smooth functioning of the administration and ensure timely debt service payments throughout January–April 2024 – which contributed to higher debt level in 2023. With external debt estimated at 60.0 percent of GDP in 2023, the depreciation of the CFA franc against the US dollar led to the revaluation of the CFA value of outstanding external debt, contributing to higher external debt service (interest payment). According to the latest joint WB IMF Debt Sustainability Analysis (June 2023), the debt profile is vulnerable to a slowdown in economic growth and a deterioration of external conditions. External debt indicators mostly remain below their thresholds under the baseline scenario–except for a one-off marginal breach in 2026 for the debt-service-to-exports indicator. However, under sensitivity analyses, all four external debt risk indicators breach their threshold. The present value of public debt to GDP marginally breaches the risk threshold in 2023 under the baseline scenario while the present value of debt to revenues is also projected to gradually decline. Per its medium-term debt management strategy, Senegal intends to increasingly reorient market financing towards the regional market due to tighter financing conditions on the international bond market with decade high monetary interest rates in advanced economies.[14] Out of total

[14] Senegal Medium-term debt management strategy https://www.sentresor.org/publication/strategie-de-gestion-de-la-dette-a-moyen-terme-2023-2025/

Box 1.1. Impact of hydrocarbon in the economy

Noteworthy oil and gas discoveries in Senegal, spanning from 2014 to 2017, reveal reserves exceeding 400 million barrels of oil and more than 40,000 billion cubic feet of gas. Among these discoveries, the GTA field, poised to commence production in 2025, unveils reserves of approximately 1 billion barrels of oil and 40 trillion cubic feet (Tcf) of gas. Additionally, the Sangomar field, set to begin production in mid-2024, boasts recoverable oil reserves of 560 million barrels, along with 2.4 trillion cubic feet of natural gas. The Yakaar Teranga field is expected to contribute to the domestic market with 150 million cubic feet per day of natural gas.

These discoveries hold the potential to significantly boost the GDP growth of the Senegalese economy, playing a pivotal role in realizing the country's aspirational development objectives. Nominal GDP is expected to increase by 12.8 percent in 2024 as oil starts flowing from Sangomar. Real growth is projected to surge from 3.8 percent in 2023 to 7.1 percent in 2024 and further 9.7 percent in 2025. The fiscal revenues derived from oil and gas are expected to contribute an additional 1 percent of GDP, on average, over the production period from 2024 to 2045, significantly bolstering Senegal's fiscal resources. Public investment, financed by these revenues, is expected to substantially increase, allowing more investment in public infrastructures and human capital. Exports of hydrocarbons are anticipated to flourish, leading to a substantial improvement in the current account. On the supply side, in addition to the anticipated boom in the industry sector, the tertiary sector (including services, insurances, transportation) may experience positive spillover effects from hydrocarbon exploitation. Furthermore, the agriculture sector could benefit from increased fertilizer production.

Oil and gas fields discoveries could also contribute to the country's goal of achieving Universal Access to Energy. The gas from the Yakaar Teranga field is expected to serve the domestic market, strengthening the energy mix and allowing electrification extension networks in rural and peri-urban areas. It is expected to also fuel the implementation of the gas-to-power strategy, which ultimately should lead to cheaper electricity, increased competitiveness, and spurred growth. This can reduce energy subsidies (see Section 1.3 for a closer look at energy subsidy reforms) creating space for social policies, greater supply of reliable and cheaper energy can improve household living conditions and reduction of inequalities in rural areas, improve education and health outcomes. However, the discovery of oil reserves can present risks and lead to over-optimism regarding the potential for economic growth, as stakeholders may anticipate substantial revenue inflows and increased foreign investment. This exuberance must be tempered by the reality of the 'resource curse,' where countries like Ghana have experienced fiscal challenges, including budget mismanagement and increased debt due to premature spending and borrowing based on expected oil revenues. Moreover, economies like Nigeria have shown how reliance on oil can lead to broader economic volatility, with fluctuating oil prices causing instability in government revenues and exchange rates. Without a well-structured and transparent approach to managing these resources, their utilization may not result in a significant economic transformation. Effective management of hydrocarbon revenues is crucial for achieving Senegal's development objectives, given that managing oil and gas resources can present challenges and exacerbate governance issues. While hydrocarbon production may initially boost real GDP growth, it may not automatically translate into increased inclusivity and income for most vulnerable groups of population, whose productivity often remains low. The government must, therefore, strategically implement reforms to channel hydrocarbon resources into programs that create a new paradigm of benefits for factor productivity and economic diversification. Allocating these resources to investments in education, youth skills development, and technological advancement for Small and Medium Enterprises can enhance labor productivity gains, contributing to higher long-term inclusive growth.

Senegal's outstanding public debt in 2023, 20.8 percent of GDP is estimated for domestic debt (from 19.6 percent of domestic debt in 2022) and 60.0 percent external debt (from 56.5 percent of external debt in 2022). External debt of the central administration's predominantly consists of multilateral and commercial debt (Eurobonds and other commercial debt). As of September 2023, the y/y increase in external debt was primarily driven by commercial debt (24 percent), export credits (+20 percent), and multilateral debt (+13 percent). Domestic debt is largely comprised of Treasury bonds. In terms of maturity, long-term debt represents 99 percent of the central administration's total debt, compared to 1 percent for short-term debt. To reduce debt vulnerabilities, Senegal has undertaken debt management operations to mitigate risks associated with the external debt profile and does not plan to tap the international bond market in the near term.

Debt servicing has increased, representing one-third of total revenue. Interest payments on public debt increased to 3.1 percent in 2023, compared to 2.2 percent in 2022, driven by increased interest payments on both external (+52 percent) and domestic debt (+29 percent). To meet existing debt obligations, Senegal allocated an additional budget to interest payments on debt in 2023. Additionally, heightened borrowing by state-owned enterprises (SOEs) further contributed to the escalation of debt levels with SOEs' debt, driven by substantial debt-financed investments, including PETROSEN's expenditures to support Senegal's hydrocarbon industry. Finally, government measures to support both firms and household purchasing power[15] amounted to FCAF 113 billion in 2023 (0.6 percent of GDP) added to the fiscal deficit in 2023. Debt service is projected to remain substantial, averaging more than 30 percent of total revenues and grants over the next five years.

Tightening financial conditions resulted in an increase in T-bond and T-bill yields. The increase in BCEAO's policy rate since June 2022 has resulted in yields rising in most WAEMU countries. In the first half of 2023, overall conditions on the public debt market exhibited increased stringency compared to the corresponding period in the previous year. The average cost of resources raised by WAEMU's member states rose across various maturities, encompassing both Treasury bills and bonds. For instance, Senegal's 3-year bond yields increased by almost 200 bps between September 2022and September 2023 (Figure 1.3.d) while 5-year bond yields increased by 180 bps, over the same period, due to the sustained high demand in the market amid a backdrop of more constrained global financial conditions. Furthermore, since the end of October 2023, Senegal has been issuing 1-month Treasury bills on the regional market at elevated rates and conducted five auctions of 1-month Treasury bills (T-bills) on the regional market, amounting to a total of FCFA 135 billion (0.7 percent of GDP) – first short-term maturities since the COVID-19 shocks, which generated urgent financing needs. These recent operations were justified by the government's decision to overfinance the 2023 budget in anticipation of potential financial market constraints during the upcoming presidential elections. However, the yields on these bills have been notably high for such a short maturity, reaching 5.81 percent in December – a substantial increase, with yields surging by 350 basis points compared to the 1-month Treasury bill from 2020. The shift towards issuances at lower maturities, coupled with the resultant heightened yields, could significantly elevate the debt level, thereby escalating the risk of debt distress.

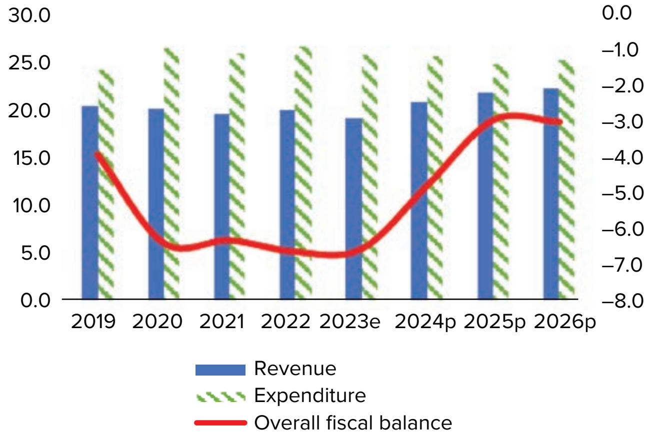
External accounts improved but vulnerabilities remain elevated due to lower exports

The external position is estimated to have improved. The current account deficit (CAD) is estimated to have narrowed to 14.5 percent of GDP from 19.9 percent of GDP in 2022 driven primarily by the resumption of trade with Mali in 2023 and a gradual reduction in service imports in the hydrocarbon sector. The CAD was financed through a combination of foreign direct investments (7.4 percent of GDP), portfolio investments (7.4 percent

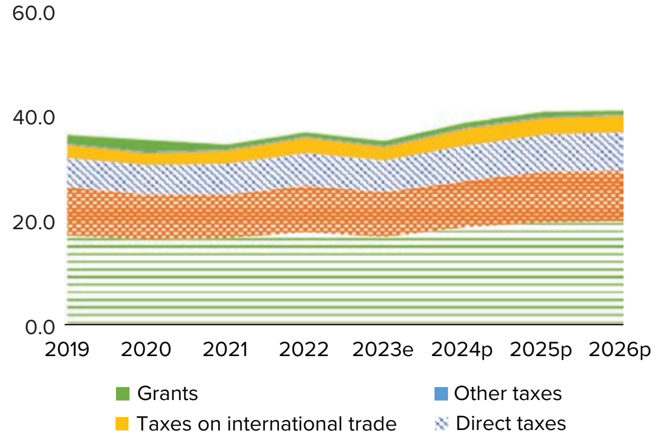
[15] The measures include the payment of compensation of FCFA 15 billion (US$22 million) due to millers, payment of subsidy to paddy rice importers (FCFA 30 per kilogram; US$0.046 per kilogram), a subsidy of 32 FCFA (16.5 percent of the price) on the kilogram of paddy rice aimed at supporting local producers, and tax exemptions on fatty substances applied to importers.

Figure 1.3. Fiscal and debt vulnerabilities have risen, but debt is deemed sustainable

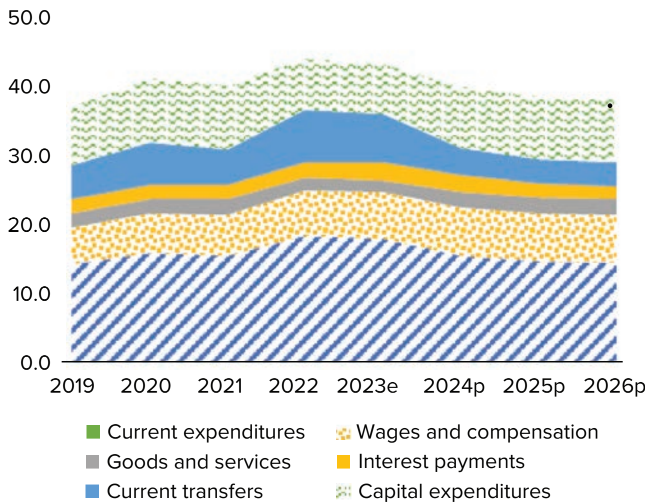
a. in 2023, Senegal's fiscal deficit remains high, above target . . .



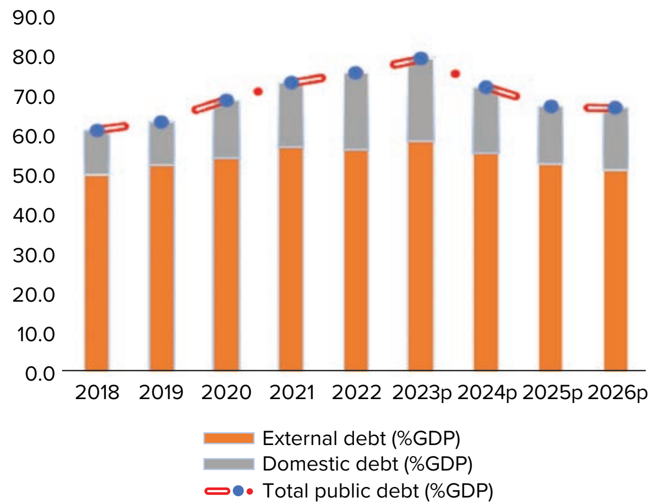
b. . . . due to lower taxes collection . . .



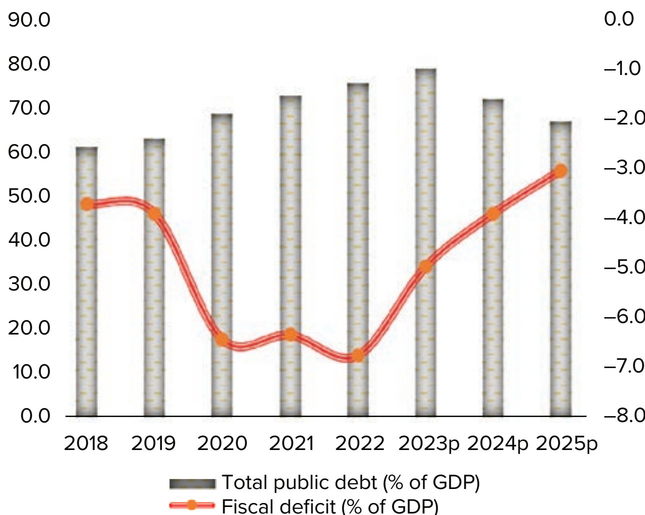
c. . . . high interest payment and high level of energy subsidies.



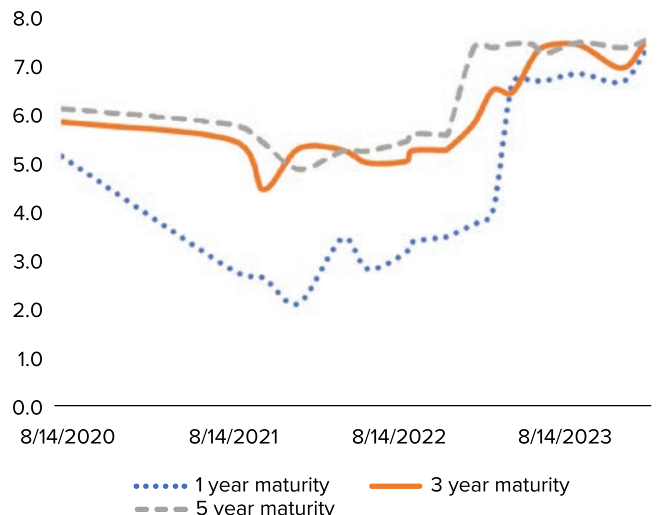
d. Public debt has been rising very fast driven by high external debt . . .



e. . . . following the trend of the fiscal deficit



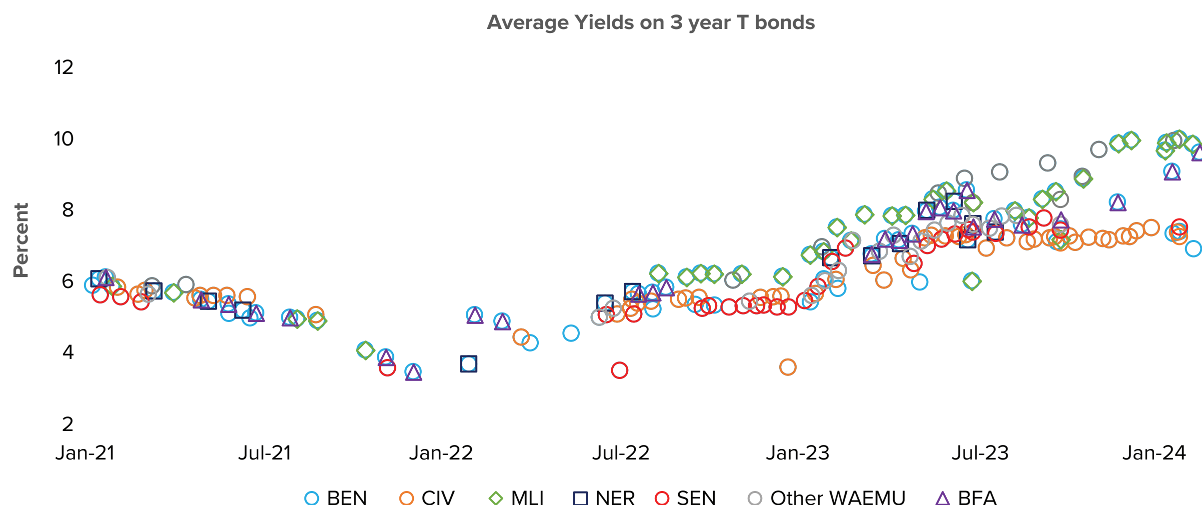
f. . . . while average yields of bonds issued by Senegal in the regional market have been rising.



(continues)

Figure 1.3. Fiscal and debt vulnerabilities have risen, but debt is deemed sustainable (*Continued*)

g. Financing conditions in CIV, Senegal, and Benin were the most favorable, albeit still above pre-pandemic levels.



Source: World Bank staff calculation, Ministry of Finance, UEMOA-Titres, 2024, BCEAO.

of GDP), remittances (10 percent of GDP in 2023), along with external credits, budget support, and financing from development partners.

The trade balance improved to 18 percent of GDP in 2023, from 26 percent of GDP in 2022, on the back of lower import bills. Imports of goods decreased from 38.8 percent in 2022 to 36.4 percent in 2023, along with service imports (from 14.1 to 7.3 percent of GDP), particularly related to hydrocarbon services. Senegal's main imports include food products, refined petroleum, rice, crude oil, equipment and cars. The main origins of the country's imports in 2023 were China, France, Russia, the Netherlands and India. Export value is expected to have fallen to 20.2 percent of GDP in 2023 from 22.2 percent of GDP in 2022, primarily due to declining global commodity prices. Senegal's exports are dominated by gold, zirconium, cement, frozen fish and petroleum oils, which together account for over 60 percent of total exports. Other marketable products include frozen fish, phosphoric acid, titanium, and ground nuts. The main destinations for Senegal's exports remain Mali, Switzerland, India, China, and Australia. Export value is expected to have fallen to 20.2 percent of GDP in 2023 from 22.2 percent of GDP in 2022, primarily due to declining global commodity prices. Export growth in 2023, particularly in key product categories such as gold, phosphoric acid and fish products, was weaker than expected. The downturn in exports is explained by the expected drop in foreign sales of phosphoric acid (43.9 percent decline year-on-year), titanium (26.5 percent decline year-on-year), zircon (a 30 percent decline year-on-year) and gold (8.6 percent decline year-on-year). These declines were mitigated by higher foreign sales of cement (40.57 percent increase year-on-year) along with the resumption of exports to Mali, as well as horticultural (25.2 percent increase year-on-year) products.

Terms of trade improved slightly in 2023 despite high volatility. Export price indices increase in the first quarter (+13.8 percent), driven by growth in machinery and horticulture prices. However, growth moderated to 4.2 percent in the second quarter, with a slowdown in horticultural and mineral products. This declining trend in export prices persisted into the second half of the year. Conversely, import price indices experienced volatility, with an 18.7 percent increase in the first quarter, but growth slowed significantly thereafter, reflecting decreases in mineral and food products' prices. A slight recovery was observed in the fourth quarter, particularly in transport

equipment prices, indicating some sectoral recovery and potential shifts in the global market. Towards the end of 2023, a slight uptick in the terms of trade reflected an improvement in export conditions and a favourable shift in import prices (Figure 1.4. c).

The capital and financial account, impacted by mixed trends, is estimated to have decelerated, with project grants rising, direct investment declining, and remittances showing a slight reduction. The capital and financial account are estimated to show a deterioration, with an expected decrease to 17.8 percent of GDP in 2023 compared to 19.6 percent of GDP in 2022, indicating a slight reduction in the total volume of capital flows into the country. This decline is primarily influenced by a decrease in the financial account to 16.5 percent of GDP in 2023, compared to 18.8 percent in 2022, pointing to a deceleration in direct investment, which is estimated to decline to 7.4 percent of GDP from 9.6 percent of GDP a year prior as a result of political instability and uncertainty. Conversely, grants are estimated to experience a positive shift, increasing to 1.2 percent of GDP in 2023 from 0.7 percent of GDP in 2022. Remittances are expected to stabilize at 10.1 percent of GDP, down slightly from 11.5 percent in 2022. This slight decline in remittances could be attributed to challenges in global economic conditions which might affect the disposable income of expatriates.

The BCEAO's external reserves fell to 3.5 months of imports at end-2023 from 4.3 months at end-2022. Foreign exchange reserves have been on a downward trend, estimated at 3.5 months of imports in 2023, down from 4.3 months at end-2022, suggesting that the BCEAO may need to continue tightening in 2024.

1.2. Outlook, risks and opportunities

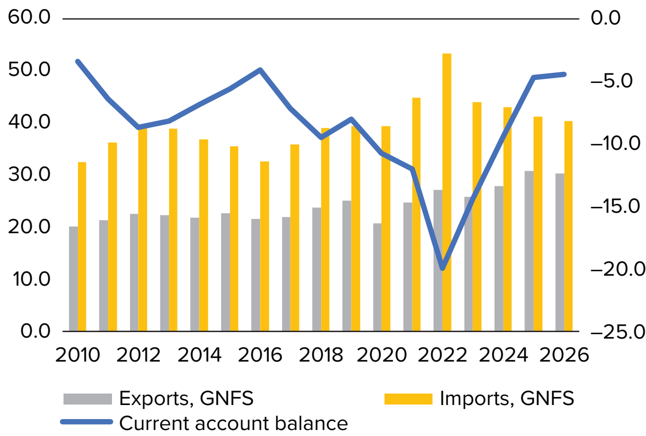
The medium-term outlook is positive with a solid recovery driven by the extractive industry, a commitment to macro-fiscal stability, and the implementation of key structural reforms

The macroeconomic outlook remains favourable, but uncertainty and risk are high. With heightened global and regional instability, the Senegalese economy is set to face significant challenges, which could be exacerbated by potential capital volatility related to FDI reallocation, and trade, as a consequence of a slowdown of economic recovery in key trading partners. Persistent political instability in the region and the risk of social discontent linked to the high cost of living with high inflation and phasing out of energy subsidies (see Section 1.3 for updated progress in phasing out energy subsidies), as well as delayed investment and further monetary tightening, could cloud the outlook. The decision by AES to exit the Economic Community of West African States (ECOWAS) adds another layer of uncertainty with potential impact on the financial and monetary sectors.

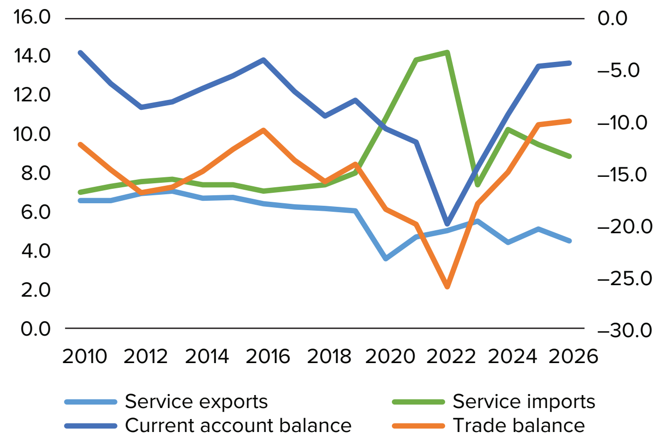
Assuming political stability, prudent macro-fiscal policies, steadfast implementation of key reforms and the beginning of hydrocarbon production, the economy should expand robustly in the medium term. Growth is anticipated to average 7.4 percent in 2024–2026, boosted by hydrocarbon production and exports (Box 2). The secondary sector is poised for robust growth, primarily driven by the significant contributions from the hydrocarbon sector, coupled with sustained positive spillover effects in other sectors. Several factors should contribute to this dynamic baseline outlook, including the government's commitment to improved transparency and transformative reforms. The extractive sector is also set to benefit substantially from the establishment of Senegal's regional mining hub. A refined regulatory framework is expected to expedite the execution of the sub-sector's revival strategy, emphasizing the acceleration of gold, zircon, and phosphate mining alongside the relaunch of the integrated Falémé iron ore mining project. Gold mining is expected to receive a considerable boost through the expansion of reserves at Sabodala Gold Operation (SGO), the initiation of production at Sored Mines, and the implementation of a project promoting artisanal and small-scale mining. Furthermore, the effective commencement of mining at the Niafarang zircon deposit, boasting an annual production capacity of 54,000 tonnes of heavy minerals, is poised to strengthen the extractive activities. Additionally, the manufacturing of agri-food products in 2024 is expected to exhibit increased vigor compared to the previous year, benefiting from the dynamism of agricultural production and the livestock sub-sector.

Figure 1.4. Developments in Senegal's external sector

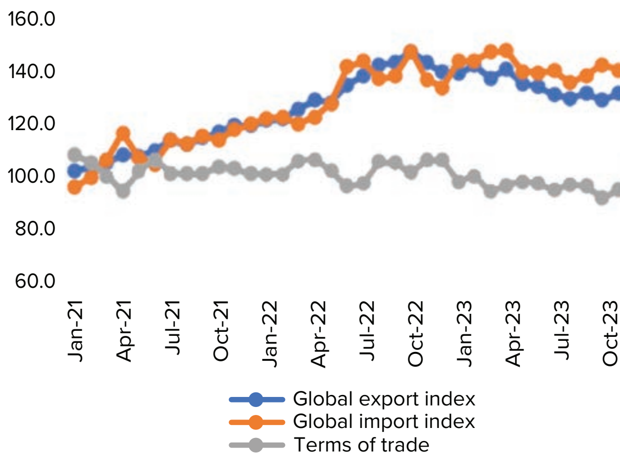
a. the current account deficit widen in recent years but should improve in the medium term . . .



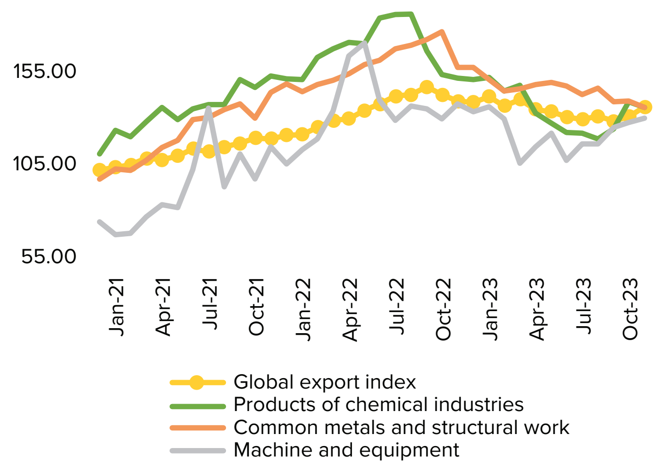
b. . . . on the back of a strong improvement of the Trade Balande thanks to hydrocarbons exports and declining services imports.



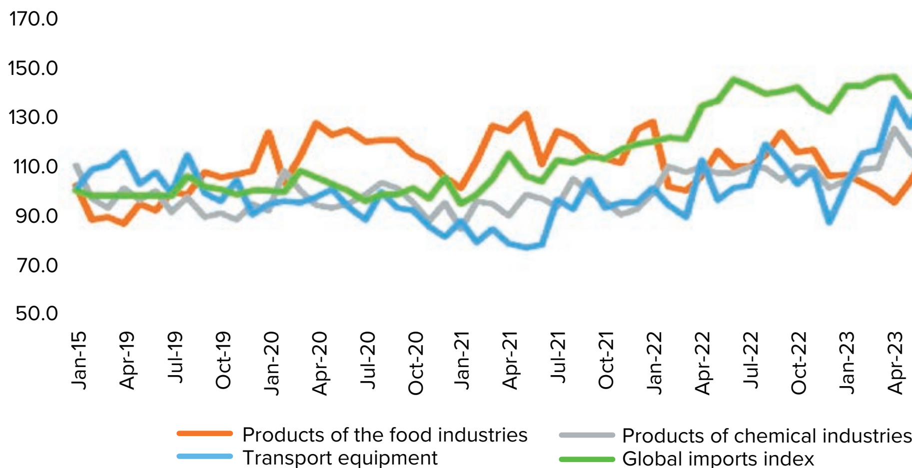
c. the terms of trade remains stable



d. Export Price Indices Experience a Year of Volatility Across Key Sectors in 2023 . . .



e. and sharp fluctuations in import price indices, culminating in sector-specific recoveries.



Source: World Bank staff calculation, ANSD, BCEAO.

Box 1.2. Progress as of December 2023 in Senegal's six-step plan for energy subsidies reform

Senegal started phasing out energy subsidies in mid-2022 with a 15 percent increase in the price of premium fuel in June 2022, and the removal of VAT exemptions for medium and high consumption tranches of electricity in the 2022 supplemental budget, while shielding lower-income households in the social tranche. In January 2023, the government announced a six-step roadmap to gradually eliminate energy subsidies by 2025, and increased prices for both fuel and electricity as a first step to implement the roadmap.

1. **Upward adjustment of selected energy prices and measures to be taken to mitigate the impact of these increases on vulnerable households** (starting January 1, 2023)

   The goal is to keep overall energy subsidies within the 2023 budget envelope of 2.7 percent of GDP. The readjustment of electricity prices should result in avoided subsidy of FCFA 99.7 billion (0.6 percent of GDP) for the government budget, while the increase in fuel prices is expected to reduce the fuel subsidy need by FCFA 158.5 billion (0.9 percent of GDP).

   Update: On January 1st, premium fuel and diesel prices rose by FCFA 100 per liter each, reaching FCFA 990 and FCFA 755, respectively. Despite remaining below international market prices, the reform coincided with a decline in global prices, reducing government spending on fuel subsidies. Regarding electricity, the government adjusted tariffs as of January 1, 2023, while preserving tariffs paid by those consuming less than 150 kWh per billing period, i.e., 1,159,146 households or 48 percent of Senelec's total customers. However, following consumer protests over high electricity prices, the Government abolished the third consumption block (households whose electricity consumption exceeds 250 kWh) of pre-paid electricity for residential customers. Subsidy rates for this block was close to zero and even negative for non-residential customers, suggesting that those customers were cross subsidizing some residential customers. This abolition, effective from December 1, 2023, allows customers exceeding 250 kWh to fall within the second consumption block, saving over 13 FCFA per kWh. Although the authorities did not disclose the fiscal burden of this measure, it is anticipated that government subsidies will increase to enable Senelec to recover some of its costs.

2. **Review the fuel pricing formula and electricity rate structure** (by end of 2023)

   Fuel: The government will review the current fuel pricing formula to ensure that prices at the pump reflect developments in international markets. The review will address (i) the different elements of the price structure; (ii) the reference price, a smoothing mechanism for adjusting prices to avoid large variations, and the frequency of price adjustments; and (iii) the composition and powers of the technical committee in charge of price setting.

   Electricity: To reduce the need for subsidies in the electricity sector, the government intends to (i) revise the electricity tariff structure gradually eliminating subsidies and (ii) complete a financial audit of Senelec by the end of 2023 to strengthen its financial situation.

   Update: A comprehensive review of the current pricing formula for petroleum products (gasoline and diesel) is underway to ensure that pump prices accurately reflect international market developments. The authorities have sought technical assistance from the IMF in this area. The government is committed to proposing and introducing a new electricity tariff structure that incorporates a social tariff specifically designed for vulnerable groups (IMF structural benchmark, September 2024). The authorities have also requested technical assistance from the World Bank to finalize an audit of the electricity company (SENELEC) (IMF structural benchmark, May 2024), which will help obtain an updated assessment of the sources and structure of both variable and fixed costs in the electricity sector.

(*continues*)

Box 1.2. Progress as of December 2023 in Senegal's six-step plan for energy subsidies reform (*Continued*)

3. **Strengthen the cash transfer system** (by end 2023)

   This reinforcement will focus on: (i) the re-certification of the Single National Register (RNU) data for the 558,000 households already registered; (ii) the addition of 412,000 vulnerable households identified for the most part through community-based targeting; and (iii) the migration to digital payment of cash transfers.

   Update: The government revalued the resources devoted to the National Family Security Grant Program (Programme national de bourse de sécurité familiale – PNBSF) and increased the number of beneficiaries in 2023. The quarterly transfers given to households through the PNBSF program increased from FCFA 25,000 to FCFA 35,000 per household, benefitting a total of 350,000 households. The management mechanism is also expected to be strengthened through the digitalization of payments to beneficiaries.

4. **Launch a communication campaign** (first half of 2024)

   The government will launch an effective communication campaign to increase public support. This campaign will inform the public of the disadvantages of the existing subsidies and the benefits of the reform.

5. **Reduce the subsidy envelope to no more than 1% of GDP (2024 budget)**

   Update: The 2024 budget law approved by the National Assembly, reflects a gradual phasing out of untargeted energy subsidies with a commitment to limit them to 1 percent of GDP in 2024. However, potential outstanding unpaid fuel subsidy obligations from 2023 may pose a risk to achieving this target. The IMF advised the authorities to stand ready to increase domestic prices if needed.

6. **Eliminate subsidies** (by 2025)

   Fuel: The price adjustment mechanism will be fully applied, ensuring that premium fuel and diesel prices follow international price trends. Vulnerable households will be partially compensated by cash transfers set up within the RNU.

   Electricity: Electricity subsidies will be removed, and vulnerable households will be protected either through cash transfers under the RNU or through cross-subsidization by other consumers.

The tertiary sector will benefit from the revival of commerce and a more favorable international economic situation. The sector is set to gain from the indirect effects of oil production in services, particularly in sub-sectors such as commerce, transportation, accommodation and food services, and financial services. The transportation sub-sector is expected to thrive due to the recovery of industries and commerce, as well as the commercial operation of the Bus Rapid Transit (BRT) and the introduction of the Regional Express Train (TER) on the Diamniadio – AIBD airport axis. Simultaneously, the reinforcement of Air Senegal SA routes and the rehabilitation and upgrading of regional airports would consolidate transportation activities. Financial and insurance services are expected to do better in 2024 than 2023, capitalizing on the vibrancy of the economy to meet the demand, especially for insurance products, notably in the oil sector, and with the expansion of the transportation sector.

Inflation pressures are expected to gradually abate as global headwinds subside. Improvements in supply chains are anticipated thanks to the good agricultural season, and the anticipated easing of commodity prices that would play a role in alleviating inflationary pressures. Annual inflation is projected to decline below 3 percent as global supply-side disruption subsides and inflationary pressures abate, with the fixed exchange rate anchored to the Euro.

Poverty is expected to decline amid solid economic rebound and lower inflation in near term, but efforts might be needed to make growth more equitable. With the stagnation of economic growth in 2023, poverty measured by the extreme international poverty line ($2.15 per capita per day in 2017 PPP)- is estimated to have remained stable (see Spotlight 1 for an update on poverty and equity in the context of multiple crises). In the near term, poverty is set to decline and reach 6.4 percent[16] in 2026 thanks to robust economic expansion with dynamic agriculture sector, the expansion of cash transfers, and declining food prices. The solid economic recovery is less likely to benefit poorest households without proactive actions to increase their participation in the growing sectors, enabling them to diversify their income and increased economic opportunity.

Fiscal consolidation is an upmost priority to lessen fiscal and debt vulnerabilities. Senegalese authorities are firmly committed to build fiscal buffers and consolidating public finances to meet the WAEMU convergence criteria of 3 percent of GDP by 2025. The MTRS includes a bold ambition of raising domestic revenue to 20 percent of GDP by 2025 – about 3 percentage points of GDP over the next 2 years. Although fiscal consolidation is likely to rely on accelerating revenue mobilization, efforts are also needed to streamline public spending by phasing out energy subsidies (see Section 1.3 for a closer look at energy subsidy reforms) and rationalizing public spending while protecting pro-poor and core capital expenditure. The fiscal deficit is expected to reach 4.8 percent in 2024 and 3 percent in 2025–2026. Energy subsidies are planned to be capped at 1 percent of GDP in 2024 (excluding arrears). Revenue collection should increase, thanks to measures that include, among others, the expansion of the tax base with 25,000 new taxpayers in 2024, the digitalization of all customs offices, the set- up an Intelligence, Risk and Value Analysis unit, and the identification of new taxpayers through information shared by Electricity and Water Companies with tax authorities, and reform options to raise tax revenue from PIT (Spotlight 2).

The CAD is projected to narrow in the near-term thanks hydrocarbon exports. A positive terms of trade shock is expected with the beginning of hydrocarbon production and exports leading to an improvement of the trade balance. The CAD is expected to gradually narrow and average -6.3 percent over 2024–26 with hydrocarbon exports and supported by fiscal consolidation and lower public investment, continued efforts to improve the investment climate and boost competitiveness. The CAD is expected to be mainly financed by remittances, foreign direct investments and external credit and debt inflows.

Rising risks cloud the outlook

The baseline outlook is uncertain, with risks tilted to the downside. The baseline outlook is subject to considerable uncertainty and risks are tilted to the downside. The context of poly-crisis and its negative effects on the Senegalese economy persist. Risks include additional delays in hydrocarbon production, regional and global geopolitical tensions, and lingering impacts of Russia's invasion of Ukraine with all its implications for trade and commodity prices. Regionally, uncertainties persist with widespread socioeconomic implications, including the risk of delayed investments, inflation, and uncertainties for the financial and monetary sectors. The January 28, 2024, announcement by Mali, Burkina Faso, and Niger to exit ECOWAS could significantly affect regional trade dynamics, particularly for Senegal. With approximately 20 percent of Senegal's total exports destined to Mali, this withdrawal has the potential to disrupt not only

[16] Using the international poverty rate of USD$2.15 in 2017 PPP.

trade flows but also the free movement of people, goods, services, and capital. The absence of alternative regional or bilateral agreements could compound these challenges. Additionally, there is growing speculation regarding the future intentions of these nations concerning their membership in the WAEMU and the possible repercussions for the shared currency.

Further delay in the commencement of oil production could undermine the economic rebound in the short term. The Senegalese Minister of Energy and Petroleum, in conjunction with the Mauritanian minister, has announced further delays to the Grand Tortue Ahmeyim (GTA) gas project, located along the maritime boundary between Senegal and Mauritania. The project, initially set for a 2022 start, has faced successive postponements—first to 2023, then to mid-2024, and now to the final quarter of 2024. This has led to a revision of expected revenue from hydrocarbon production, underscoring the urgent need for diversification and enhancement of revenue streams. Financial conditions are also tightening, raising alarms about future funding availability and potential financial constraints.

Climate-related risks are evident and could hold back Senegal development ambitions. The impacts of climate shocks are increasingly pertinent to the economic outlook. Senegal is grappling with the impacts of climate change, including higher temperatures, unpredictable rainfall patterns, and more frequent occurrences of floods, droughts, and locust invasions, compounded by the threat of rising sea levels. In response to these environmental challenges, the Bank is actively supporting Senegal in its efforts to build climate resilience and promote cost-effective, low-carbon development strategies. Current initiatives include projects focused on coastal adaptation, flood risk management, water security, climate-smart agriculture, waste management, and the sustainable management of natural resources within the fisheries and forestry sectors. Notably, progress is being made in urban mobility with the introduction of the Dakar Bus Rapid Transit (BRT) system in 2024.

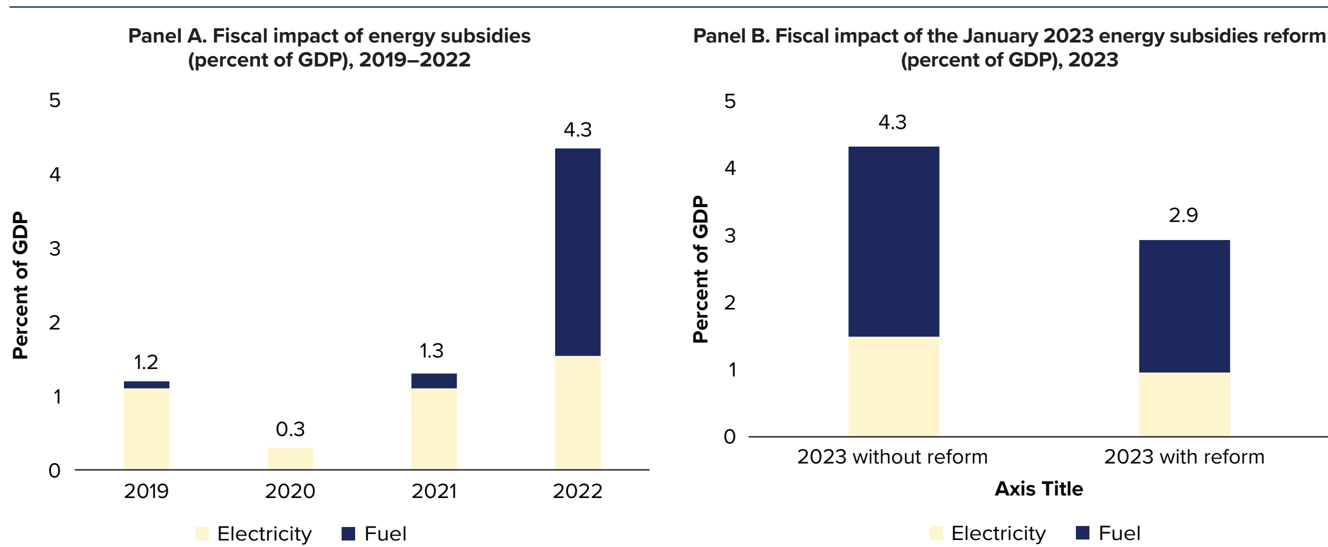
Persistent high inflation in advanced economies could drive further global and regional tightening monetary policy and exacerbate fiscal vulnerabilities. The BCEAO may need to continue tightening in 2024 to bring inflation under control and in the context of rising uncertainties over the withdrawal of Niger, Mali, and Burkina Faso from ECOWAS and potential spillovers to WAEMU. These uncertainties are likely to increase investors' risk perceptions leading to tighter financing conditions and putting additional strain on already low foreign exchange reserves.

1.3. Taking a closer look: Energy subsidy reform

The spending on energy subsidies in 2022 led to significant fiscal strain that set up the stage for a subdue energy reform that took place in January of 2023. Senegal subsidizes fuel and electricity cost through (i) fixed prices on petroleum products and gas and (ii) regulated electricity tariffs that are set below the cost-recovery price. The fiscal cost of energy subsidies went from less than 1.3 percent of GDP in the 2019–21 period to almost 4 percent of GDP in 2022. The sudden increase resulted from the soaring oil prices triggered by the war in Ukraine. The unsustainable debt gave the momentum needed to implement a comprehensive reform to both fuel and electricity subsidies. In January of 2023, the government of Senegal increases the price of premium gasoline, diesel, and electricity tariffs for high-consumption households. This reform aimed to generate 1.4 percent of GDP in fiscal savings—CFAF 258 billion), with 0.9 and 0.5 percent of those savings coming from lower fuel and electricity subsidies, respectively.

This energy reform includes a comprehensive set of complementary policies. In particular, the reform increases the price of premium gasoline, diesel, and electricity for high-consumption households. A wide range of compensatory measures accompanied these price hikes: First, the government aimed to protect the most vulnerable households by keeping fixed prices of other energy commodities such as LPG, boat gasoline, and electricity for low-consumption households. Second, the government planned to increase the coverage and benefits of the main cash transfer program—PNBSF. As

Figure 1.5. The energy reform is expected to bring substantial fiscal savings

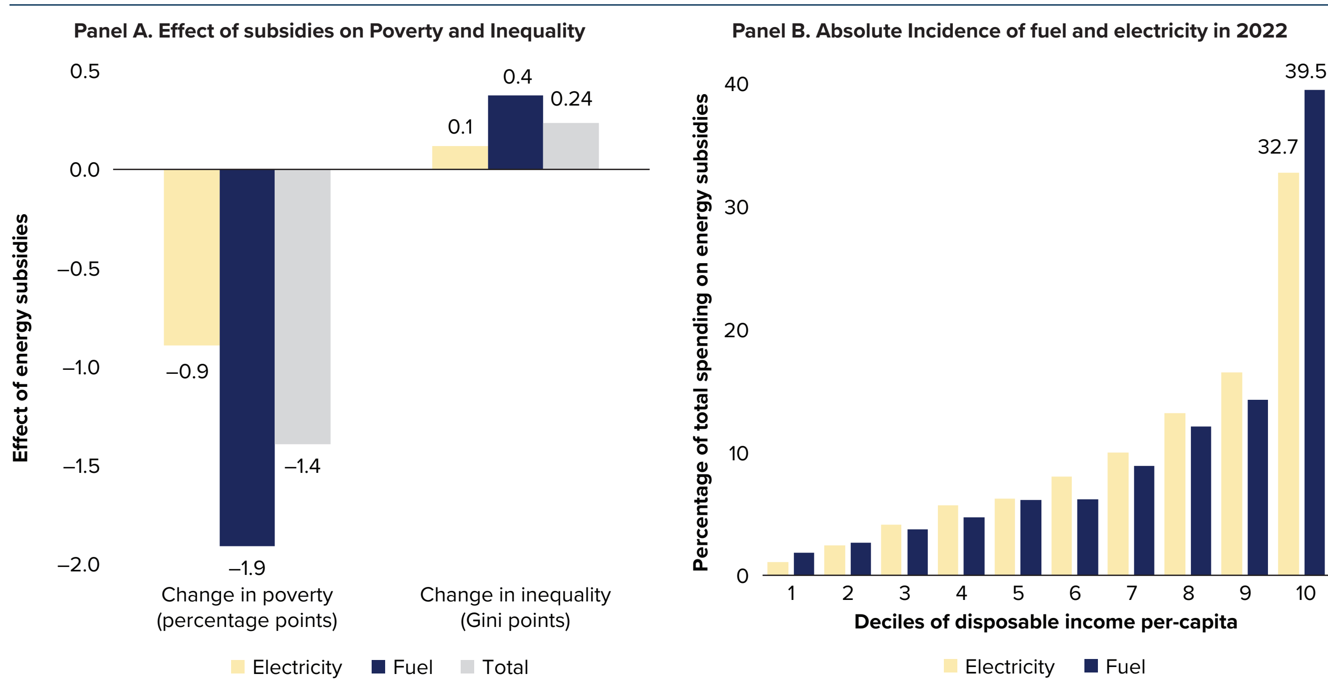


Source: Bank staff calculations based on government estimates.

Table 1.1. Policies defined by the energy subsidy reform in Senegal

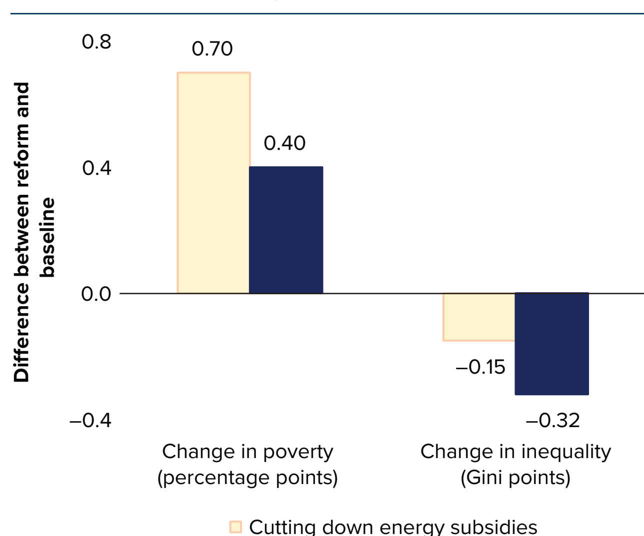
Sequential Reduction of Subsidies	*Compensation Measures*	*Communication*
• Upward adjustment of selected energy prices by January of 2023 • Review the pricing formula by end of 2023 • Complete elimination of energy subsidies by 2025	• Freezes prices for LPG, kerosene, boat gasoline gas and electricity for Kwh consumed under the first consumption block • Strengthen the cash transfer system (coverage and benefits) • Extension of the social registry to 1 million households, which is in progress, covering not only the entire poor population but also the vulnerable • Subsidizing transport sector	• Launch a communication campaign

Figure 1.6. The energy reform was needed as subsidies are inefficiently targeted



Source: Bank staff calculations based on EHCVM 2021–22 and policy parameters available in November of 2023.
Notes: The figure shows how disposable income inequality (poverty) changes after considering energy subsidies (i.e. fuel and electricity))and value added exemptions of electricity consumption. Change in poverty headcount use the national poverty line.

Figure 1.7. The energy reform requires stronger compensation measures to fully compensate its effects on poverty



Source: Bank staff calculations based on EHCVM 2021–22 and policy parameters available in November of 2023.
Notes: The figure shows the change in disposable income inequality and poverty (measure by the national poverty line) across different scenarios.

a consequence, the benefit of the cash transfer program increases by 40 percent, by FCFA 10,000. As the exact increase in coverage is unclear, we assume it will increase by one-third before 2025 (100,000 families). By October of 2023, the number of beneficiaries increased by 54,000. Third, to boost public support, the government plans to invest in a communication campaign that explains the reason for the increase in energy prices and how this policy aims to translate into a higher redistributive capacity of the fiscal system.

Energy subsidies have been an inefficient instrument to reduce poverty and exacerbate pre-existing inequalities. In 2018–19, energy subsidies reduced poverty by 0.6 percentage points in Senegal (World Bank 2024).[17] In 2022, this effect was even higher, with subsidies reducing poverty by 1.4 percentage points. The increase in the importance of subsidies being explained by the core role of subsidies in preventing the erosion of household's purchasing power due to a decline in oil prices. However, energy subsidies have been proven to be an inefficient way to protect low-income households. In 2022, between 32–39 cents of each dollar spent on energy subsidies (Electricity and Fuel) was being received by households in the top decile of income distribution. This inefficiency results in subsidies increasing the pre-existent levels of income inequality, with inequality increasing by 0.24 Gini points. The regressivity of energy subsidies is mainly explained by high-income households having higher access to the electricity grid and more energy-intensive assets (e.g., cars, tractors, air conditioning) than their low-income counterparts.

Additional compensation measures are needed and are financially feasible. The cost of the compensation measures simulated here is expected to be 35.6 billion FCFA,[18] most of it coming from increasing coverage of PNBSF by one third. This cost is less than 15 percent of the reform's expected fiscal gains—258.2 billion FCFA, suggesting that the stronger compensation measures are financially feasible.

[17] This figure corresponds to the impact of removing subsidies on consumable income. See World Bank (2024). Africa Poverty and Inequality Flagship.

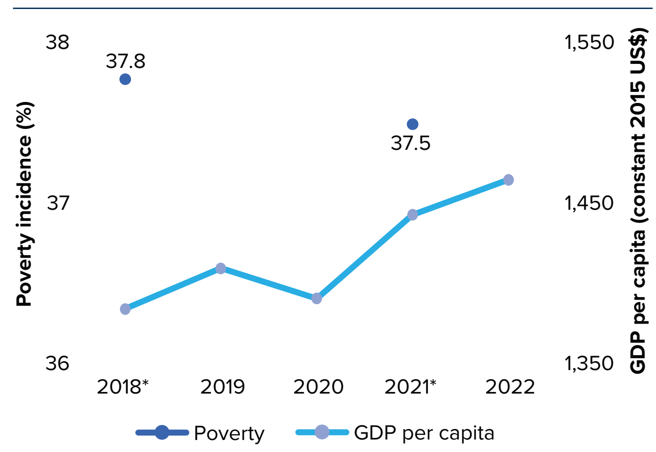
[18] This cost is explained by: i) increase in the amount of the PNBSF transfer from 100,000 to 140,000 (CFAF 12 billion), ii) increase of PNBSF beneficiaries by 100,000 families (CFAF 14 billion), and iii) Transport subsidies (CFAF 9.6 billion), which are computed by the share of fuel subsidies that goes into public transportation—1.8 percent of fuel subsidies. This estimate does not consider implementation costs of these policies.

Chapter 2: Spotlight on Senegal's Development Agenda: Poverty and Equity in a Context of Multiple Crises

Senegal's poverty incidence stagnated over 2018/19 to 2021/22 but the number of poor has increased, reflecting the fact that growth has not necessarily reached the poor

Poverty incidence stagnated over 2021/22 and 2018/19 in Senegal despite the context of multiple shocks. The country has coped well, with poverty incidence (using the national poverty line) remaining quasi-stable at 37.5 percent of the population in 2021/22 compared to 37.8 percent in 2018/19[19]. Poverty incidence is stable in both urban and rural areas, but with contrasting regional trends. There has been a marked fall in poverty in the Senegal River Valley (center) and in Eastern Senegal bordering Mali, and a slight increase in the south in Casamance. Real per capita consumption declined among the poorest and the better-off while middle income brackets experienced a gain in real per capita consumption. This trend resulted in a decline in inequality, with the Gini index dropping from 35.1 in 2018/19 to 33.4 in 2021/22.

Figure 2.1. Poverty incidence and GDP per capita, 2018–2021



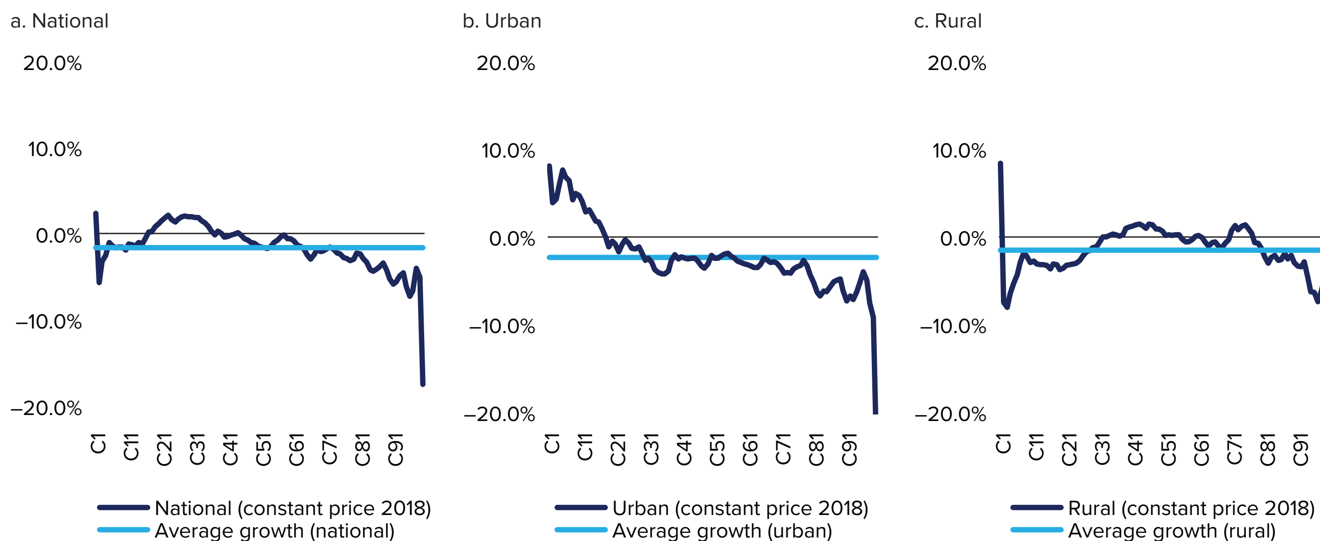
Source: World Bank calculations based on EHCVM 2018/19, EHCVM 2021/22 and data portal (https://data.worldbank.org/).
Note: Poverty rates in 2018 and 2021 are computed using EHCVM 2018/19 and EHCVM 2021/22.

Economic growth slowed down with the COVID-19 shocks after several years of above SSA average performance. The period 2018–2022 coincided with the implementation of the second phase (PAP-2) of the *Plan Senegal Emergent* (PSE), which aimed at accelerating structural transformation to help Senegal achieved the status of an emerging economy by 2035. Senegal's ambitions were hindered by multiple shocks over 2018–2022 including the COVID-19 pandemic, the spillover from Russia's invasion of Ukraine, rising political instability, and domestic political tensions. Average annual GDP per capita growth was around 1.4 percent between 2019–2022, compared with 3.7 percent in 2014–2018 (Figure 2.1). Moreover, GDP growth, driven by growth in services didn't translate into consumption per capita growth. The period was also marked by high inflation. From 2011 to 2019, average annual inflation was 1 per cent in Senegal; but consumer prices rose by 2.5 percent in 2020, 2.2 percent in 2021 and 9.7 percent in 2022. A combination of lower growth and high inflation had a negative impact on household living conditions.

Average households' consumption declined with significant differences between urban and rural areas. Nationwide per-capita consumption growth declined by 1.6 percent, with most of the decline felt by more affluent households. The growth incidence curve (GIC) at the national level (Figure 2.2, left panel) shows negative growth rates for all households that belong to the top quintile of the consumption distribution, with declines in consumption ranging between −1.6 and −5.1 percent between the 61 and the 99 percentile of the consumption distribution. The national average masks substantial

[19] Data used on this note comes from two rounds of the WAEMU Harmonized Household Survey known by its French acronym EHCVM (*Enquête Harmonisée sur les Conditions de Vie des Ménages*). The two rounds of the survey were fielded in October 2018–July 2029 for the first edition, and November 2021–August 2022 for the second one by the NSOs of the 8 WAEMU member states (Benin, Burkina Faso, Côte d'Ivoire, Guinea Bissau, Mali, Niger, Senegal, and Togo) as part of a World Bank regional project implemented by the WAEMU Commission and the NSOs of the WAEMU member states. The two rounds of the survey are comparable, changes in survey design, questionnaires and poverty measurement between the two rounds are small. For Senegal the sample size of each round is 7100 households, representative at the national level, urban/rural and at the regional level.

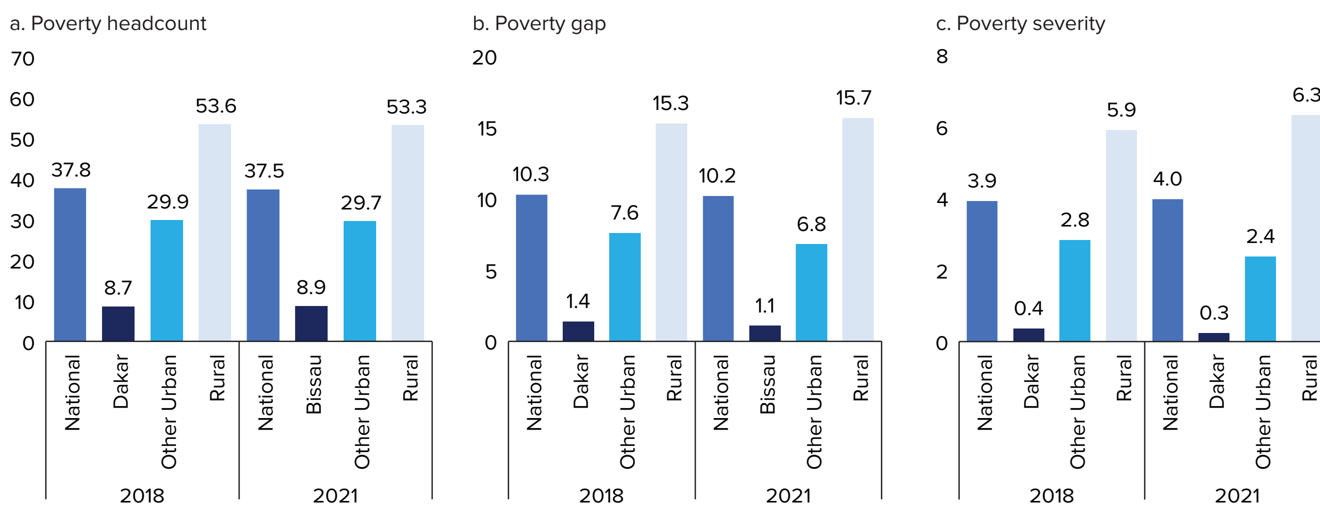
Figure 2.2. Growth incidence curves by geographical location



Source: World Bank staff calculation based on EHCVM 2018/19 and 2021/22.

heterogeneity across urban and rural areas. In urban areas (Figure 2.3, center panel), consumption growth was largely negative, with an average decline of 2.3 percent over the period, driven mainly by declines in consumption of the better-off. Poorest urban households experience a positive and strong consumption growth, which suggests that the targeted social assistance provided during the period may have helped these households to mitigate the effects of the negative urban consumption growth. In rural areas (Figure 2.3, right panel), on the other hand, consumption growth declined by 1.5 percent over the period, oscillating around this value for poor and

Figure 2.3. Monetary poverty indicators 2018–2021 by area of residence



Source: World Bank calculations based on EHCVM 2018/19 and EHCVM 2021/22.

non-poor households. This timid and slightly negative growth rate in rural areas sheds light on why poverty has not declined in Senegal. As most of the poor still live in rural areas, inclusive growth policies that boost household income of rural habitants is needed to effectively continue reducing poverty in Senegal.

However poverty indicators remained relatively stable despite the COVID-19 pandemic and other 2018–2022 crises, reflecting resilience among households. The national poverty line is 369,666 FCFA per person per year in 2021/22, rising from 333,441 FCFA in 2018/19. Nationally, the percentage of the population living below the poverty line is stable, at 37.5 per cent in 2021/22 compared to 37.8 per cent in 2018/19 (Figure 2.3). This trend of a stable poverty headcount is recorded in both rural and urban areas. The poverty gap, which measures the depth of poverty by looking at the average consumption deficit of individuals living below the poverty line, remained stable at around 10.2 percent. The relative stability of poverty headcount was accompanied by a 9 percent increase in the number of poor between 2018/19 and 2021/22, with the number of poor people increasing both in urban areas (12.1 percent) and in rural areas (7.5 percent). The squared poverty gap, which measures the severity of poverty by putting greater weight on those furthest below the poverty line, also remained stable around 4 percent. The squared poverty gap tend to decline slightly in urban areas, and to rise slightly in rural areas, where poverty levels are already higher, reflecting the fact that the situation of poor households has not deteriorated in urban areas, whereas it may be tending to deteriorate somewhat in rural areas. Among other factors, high demographic growth (around 2.9 per cent per year) due to persistently high fertility (4.1 children per woman on average, according to the 2018/19 DHS) contribute to the increased number of poor.

Although the incidence of poverty is high in areas far from Dakar, a high share of the poor lives in the groundnut basin. The incidence of poverty across regions is correlated with economic opportunities, which are strongly associated with the distance of each region to Dakar. Panel a of Figure 2.4 shows a poverty incidence of around 60 percent for the regions in the east (Tambacounda, Kedougou) and the south (Sedhiou, Kolda). In spite of the high incidence of poverty in the east and the south, about one-third of the poor population lives in the regions of Diourbel, Kaolack, and Thiès in the groundnut basin (Panel b of Figure 2.4). Moreover, poverty is still a rural phenomenon, as three-quarters of the 6.5 million of people who live below the poverty line reside in rural areas. This implies large social gains for anti-poverty programs that are localized around the groundnut basin. Also, it suggests that regions far from Dakar need more substantial investments to ignite a virtuous cycle of economic growth that tackle the high incidence of poverty in these regions.

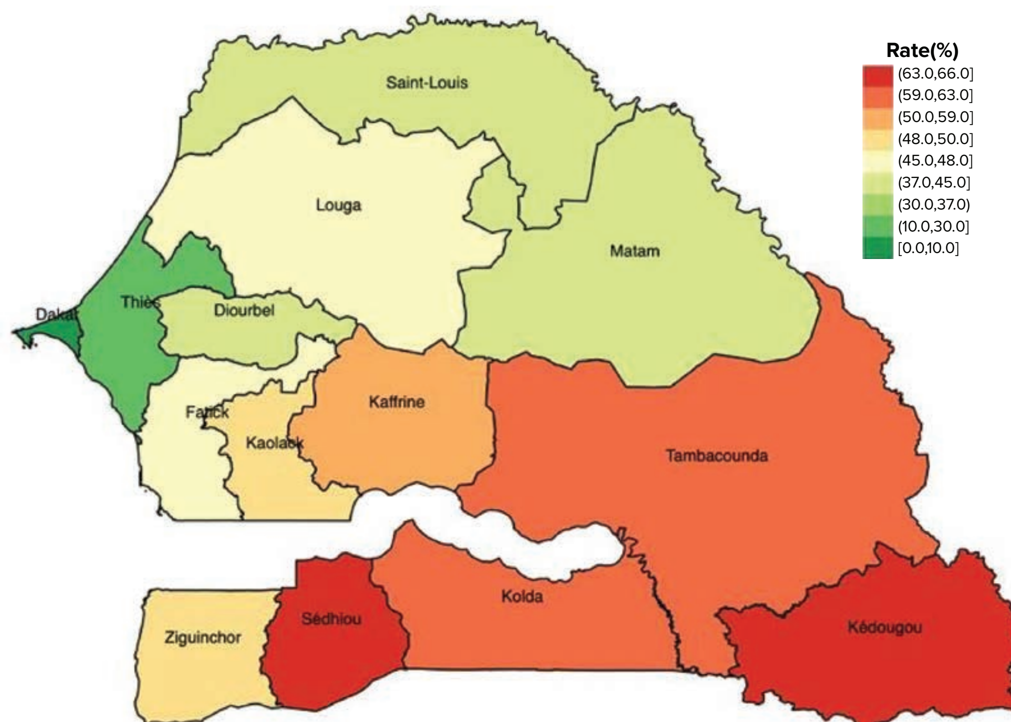
Inequality declined due to declining household consumption, while the pace of poverty reduction is falling behind that of regional peers

Inequality declined as a result of an overall declined welfare, not an increase in the livelihoods of the poorest households. As mentioned before, average consumption growth was negative, with middle-income households experiencing growth in consumption, while both high- and low-income households experiencing declines in consumption. High-income households experienced declines in consumption that were above the national average. This pro-poor decline in consumption resulted in a reduction of inequality across the board. At the national level, the Gini index fell by 1.7 Gini points, from 35.1 to 33.4 during the 2018–2022 period (Figure 2.5). Similarly, the average per capita consumption of the top 20 percent, which represented 5.5 times that of the bottom 40 percent in 2018/19 declined to 5.2 in 2021/22 (Table 2.1). Similarly, inequality declined in Dakar (1.6 Gini points), other urban areas (3.2 Gini points) and rural area (0.5 Gini points). However, these decline in inequality results from an erosion of purchasing power of the better-off household rather than from the increase in real consumption of the poorest households.

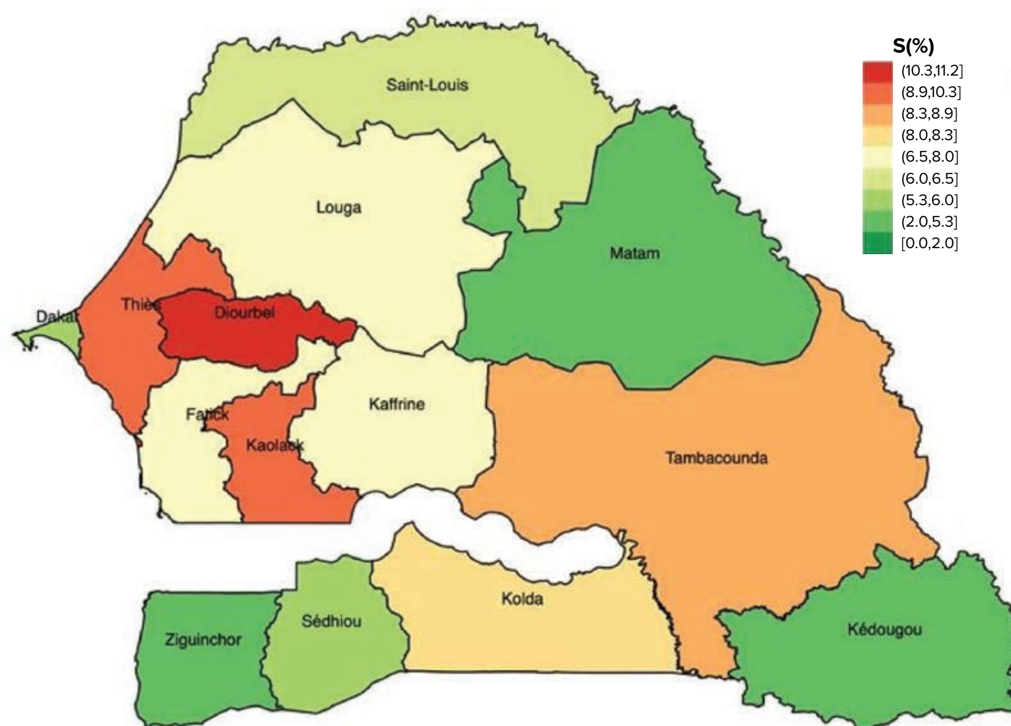
Despite a marginal decline in inequality between urban and rural areas, the disparities are still high in favor of urban areas. Dakar represented 22.2 percent of Senegal's population in 2018/19 and 22 percent in 2021/22, but Dakar's share in total consumption dropped from 33.2 percent to 30.8 percent over the same period.

Figure 2.4. Poverty indicators by region (EHCVM 2021)

a. Poverty rate

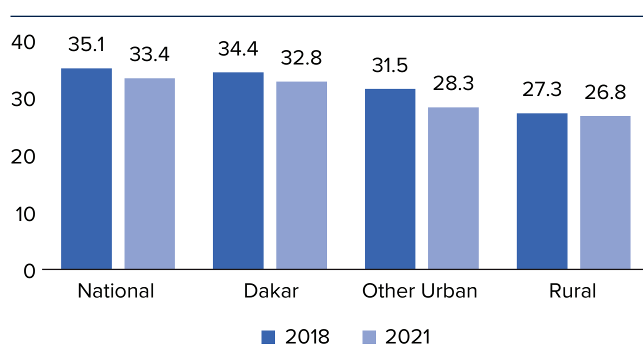


b. Share of poor population



Source: World Bank calculations based on EHCVM 2021/22 (poverty line of 369,516 CFAF per person per year).

Figure 2.5. Gini (consumption) inequality index, 2018–2021



Source: World Bank staff calculation based on EHCVM 2018/19 and 2021/22.

The gains have been in favor of both other urban areas (0.9 percentage points increase of population share and 1.1 percentage points increase in total consumption) and mostly rural areas (0.7 percentage points decrease of population share but 1.2 percentage points increase in total consumption). Despite these recent trends, disparities between urban and rural areas are still high. The average per capita consumption of overall urban areas was 80 percent higher than that of rural areas in 2018/19, compared to 70 percent in 2021/22.

Despite declining inequality and poverty, and improved shared prosperity, the pace of poverty reduction is falling behind that of regional peers. Compared to some of its peers in the WAEMU region[20] (Figure 2.6), Senegal's poverty rate is relatively low. As of 2018/19, Senegal had the lowest poverty incidence among the WAEMU countries, when using the $2.15 a day international poverty line. However, by 2021/22, the country has fallen behind Côte d'Ivoire, which had experienced a higher drop in poverty, although Senegal still has a lower poverty rate when using the lower-middle income poverty line of US$3.65 a day. Additionally, out of the eight countries in the region, Senegal is one of the three that saw an increase in poverty under the $US2.15 per person per day 2017 PPP international poverty line during the period, because of the drop in consumption of the poorest, as seen earlier in this note. This increase, albeit the lowest in the region, is just behind Mali (5.6 percentage points increase) and Guinea-Bissau (4.3 percentage points increase). Some of its peers experienced a moderate reduction in poverty. Compared to some of its structural peers,[21] Senegal's poverty rate (based on the US$3.65 international poverty line) is about 2 percentage points lower than Kenya's 2021 rate; and almost 33 percentage points higher when compared to Vietnam's 2020 rate. Senegal has room to decrease poverty (Figure 2.7).

Table 2.1. Consumption inequality indicators in Senegal 2018–2021

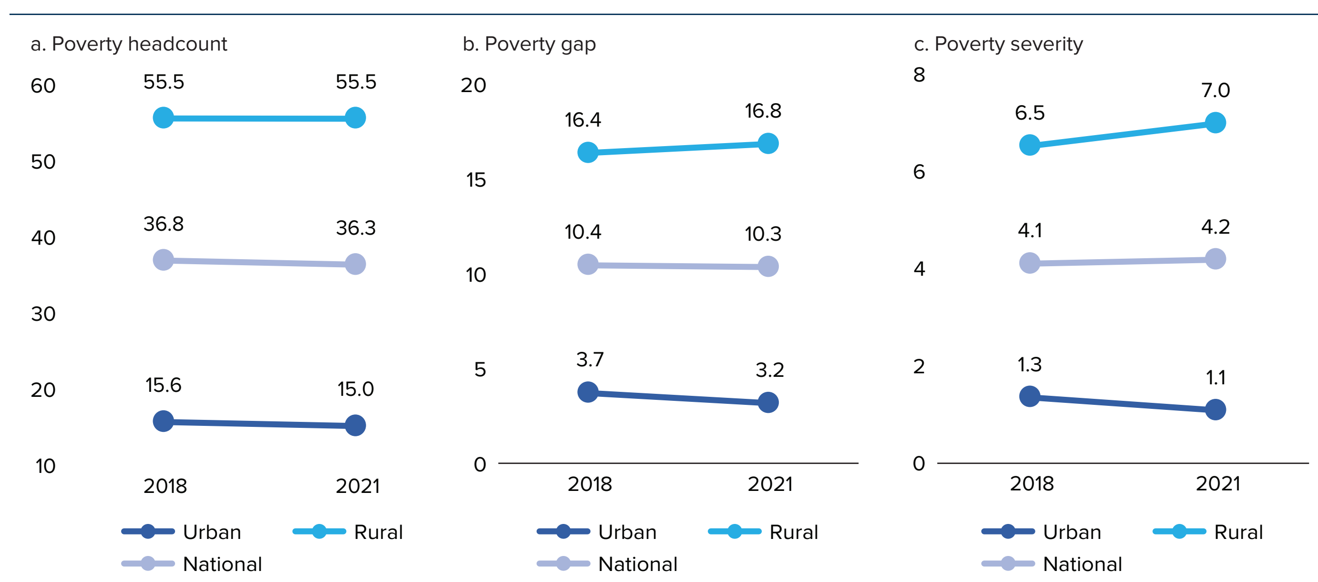
	Share of Total Population (Percentage)		*Share of Total Consumption (Percentage)*		*Gini Index*		*Consumption Ratios Between Top and Bottom Quintiles*	
	2018	*2021*	*2018*	*2021*	*2018*	*2021*	*2018*	*2021*
National	—	—	—	—	35.1	33.4	5.5	5.2
Dakar	22.2	22.0	33.2	30.8	34.4	32.8	5.2	4.8
Other Urban	24.6	25.5	25.6	26.7	31.5	28.3	4.8	4.1
Rural	53.2	52.5	41.3	42.5	27.3	26.8	3.8	3.8

Source: World Bank staff calculation based on EHCVM 2018/19 and 2021/22.

[20] As the two rounds of EHCVM were fielded in 8 WAEMU member states, it is possible to assess the evolution of poverty from 2018/19 to 2021/22 across these countries, leveraging that the two episodes of the harmonized survey are comparable. To compare the evolution of poverty across countries we rely on the international poverty lines of $2.15 and $3.65 per person per day in 2017 PPP.

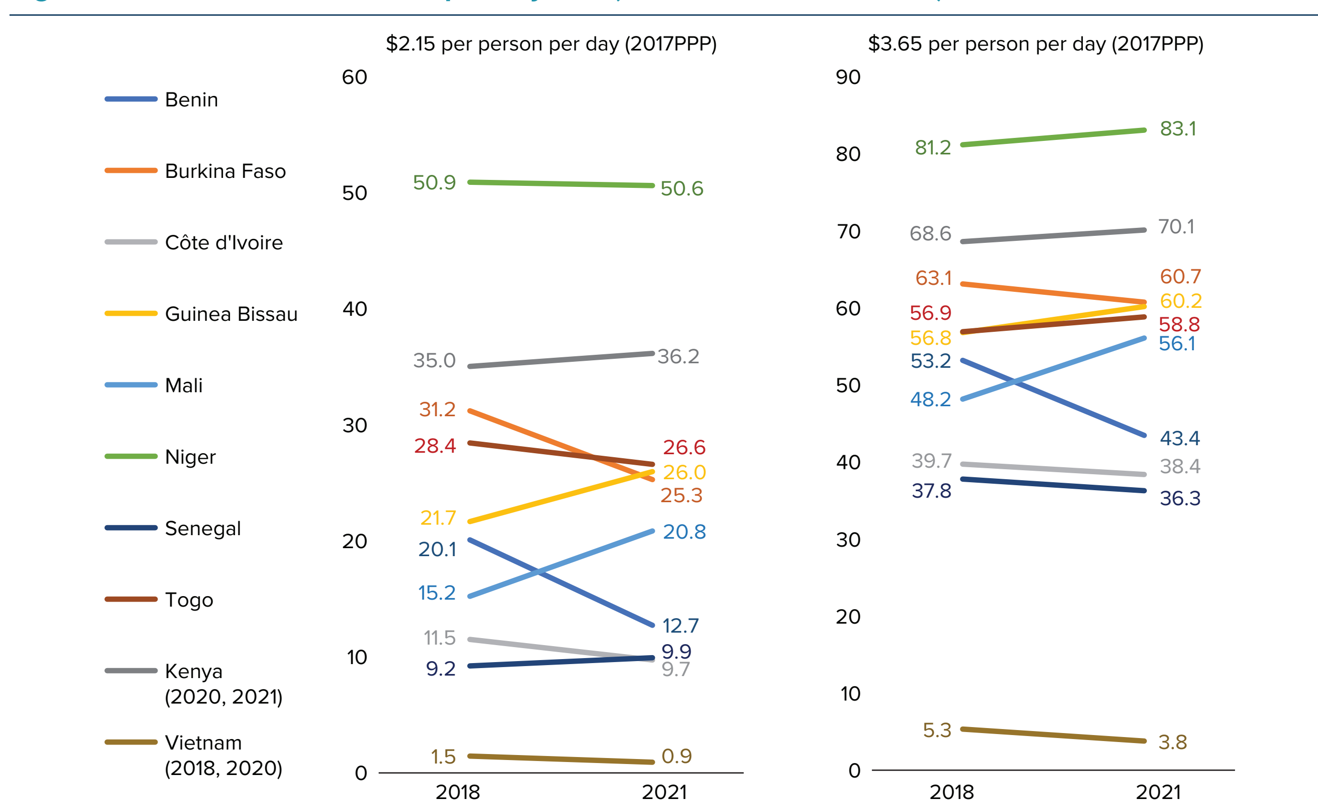
[21] Structural peers are defined as countries that have similar structural characteristics (population, GDP per capita, contribution of agriculture to economy, life expectancy, trade composition, and government revenue) to Senegal.

Figure 2.6. Trends in monetary poverty using the $3.65 (PPP2017) international poverty line by area of residence, 2018–2021



Source: World Bank staff calculation based on EHCVM 2018/19 and 2021/22 using the international poverty line of US $3.65 per person per day in 2017 PPPs.

Figure 2.7. International extreme poverty rate ($2.15 & $3.65, PPP2017), 2018–2021



Source: World Bank staff calculation based on EHCVM 2018/19 and 2021/22 using the international poverty line of US $2.15 per person per day in 2017 PPPs.
**Note:* Poverty estimates for Kenya (2020 and 2021), Morocco (2019, 2021) and Vietnam (2018, 2021) – some aspirational peers for Senegal – correspond to the recent Macro Poverty Outlook (MPO) from AM23.

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Chapter 3: Spotlight on Senegal's Development Agenda: Options to Raise Tax Revenue from Personal Income Tax (PIT)

Improving domestic revenue mobilization (DRM) is critical for Senegal to achieve its development ambition. Between 2014 and 2019, Senegal was one of the most dynamic economies in sub-Saharan Africa (SSA). GDP growth averaged 6 percent over 2014–19, one of the highest in SSA, and real GDP per capita levels increased by 17.9 percent during the same period. To finance its development ambitions, it is imperative to sustain investments in human capital and infrastructure. Additionally, there is a need to accelerate structural transformation, requiring a significant mobilization of both private and public resources.

Senegal's longstanding challenge of boosting domestic revenue collection has been amplified by short-term vulnerabilities in context of multiple crises. DRM is a longstanding challenge for countries in SSA with large informal economies, complex tax policy not always aligned with administrative capacity, and limited enforcement capacity. Insufficient revenue has often reduced countries' ability to invest in human and physical capital to support inclusive growth and revenue shortfalls have been compensated by debt accumulation, raising vulnerabilities, and limiting fiscal space to absorb shocks. The context of poly-crises with the COVID-19 pandemic, Russia's invasion of Ukraine, and conflicts in the Middle East have exacerbated challenges in sustaining public finances in SSA countries, including Senegal, underscoring an urgent need to accelerate domestic revenue mobilization efforts. Long-term pressures and development needs are also emerging as Senegal faces large gaps in adapting and mitigating the impacts of climate change, on top of addressing structural issues related to youth emigration in search of better economic opportunity, limited human and physical capital and low productivity. Global and regional financial tightening in the aftermath of these crises means Senegal, like other countries, will have to mobilize domestic revenue sources to finance its long-term development ambitions and sustain the capacity to borrow. In this context, establishing a fiscal path through a revenue-based fiscal consolidation process to ensure fiscal and debt sustainability in the medium term, alongside measures on the expenditure side, is the utmost priority for Senegal. As a member of the West African Economic and Monetary Union (WAEMU), Senegal adheres to the regional fiscal framework (Box 3.1), which highlights the imperative of sustaining macro-financial stability.

Box 3.1. The WAEMU regional fiscal framework

The West African Economic and Monetary Union (WAEMU) is one of four currency unions in the world, and consists of eight countries (Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal, and Togo). The Central Bank of West African States (BCEAO) issues a common currency, the CFA Franc, pegged to the euro, conducts a single regional monetary policy, pools members' foreign exchange reserves, and helps to supervise the WAEMU's financial system.

Achieving and maintaining fiscal convergence is essential for safeguarding macroeconomic stability and preserving the sustainability and credibility of the fixed exchange rate regime. To this end, a well-designed regional fiscal framework can foster fiscal discipline and improve coordination to prevent member states from running excessive budget deficits. The fiscal stance of one member of the union can impact other members' fiscal positions through various channels, including trade and contagion effects. These fiscal spillovers can be particularly problematic under a fixed exchange rate since lack of fiscal discipline can deplete international reserves and jeopardize the peg.

In this context, the WAEMU regional surveillance framework, adopted in 1996, aims at ensuring the sustainability of national fiscal policies and their consistency with the common monetary policy (including the fixed exchange rate regime). It also envisages a gradual convergence by member countries towards a number of criteria related to macro-fiscal aggregates,

Box 3.1. The WAEMU regional fiscal framework (*Continued*)

including the fiscal deficit, public debt, and inflation (Table B.3.1). Regional convergence was temporarily achieved at the aggregate level in 2019, but the fiscal framework was suspended in 2020 in the context of the COVID-19 crisis. Additional vulnerabilities have also compromised some of the convergence criteria. Debt has accumulated significantly over the past decade due to the accumulation of high fiscal deficits over time, as well as the prevalence of debt-creating operations that were not captured by the fiscal deficit. Sever and Laws (2023)[22] however suggests that repeated fiscal slippages and historically large stock flow adjustments contributed to the surge in the WAEMU public debt. The paper calls for an urgent need to reintroduce the fiscal rules and revamping them by introducing a correction mechanism contain surges in debt in the future and an escape clause, which would enhance fiscal discipline and predictability, as well as capturing the extensive extra-budgetary and below-the-line operations and strengthening the enforcement mechanism.

Reforms could be carried out to improve the coordination and enforcement mechanisms and enhance public financial management (PFM) to contain stock-flow adjustment, prevent a build-up in fiscal imbalance, and tighten the link between the evolution of fiscal and debt targets.

Table B.3.1. WAEMU convergence criteria (adopted in 2015)

First Order Criteria of the Convergence Phase	*Ceiling/Floor*
Overall fiscal balance (including grants) to nominal GDP	≥–3 percent
Average consumer price inflation per year	≤3 percent
Total public debt to nominal GDP	≤70 percent
Second Order Criteria of the Convergence Phase	*Ceiling/Floor*
Wages and salaries to tax revenue	≤35 percent
Tax revenue to nominal GDP	≥20 percent

Source: Compiled by staff based on information from the Additional Act no. 01/2015/CCEG/UEMOA.

Source: David, Nguyen-Duong and Selim (2022).

Tax revenue has increased steadily, but levels remain low and dominated by indirect taxes

To accelerate revenue collection, Senegal has set a target of mobilizing domestic taxes exceeding 20 percent of its GDP by 2025. In 2020, Senegal adopted a Medium-Term Revenue Strategy (MTRS) aiming at raising the tax-to-GDP ratio (excluding hydrocarbon) to 20 percent by 2025. The MTRS focuses on tax base expansion policies and equitable compliance, notably through the Yaatal project.[23] The implementation of the MTRS helped increase from 16.8 percent in 2020 to 18.2 percent of GDP in 2022 after stagnating around 15 percent of GDP over 2010–18. This performance was primarily

[22] Sever, Can and Laws, Athene. Revamping the West African Economic and Monetary Union (WAEMU) Fiscal Framework. IMF Selected Issues Paper (SIP/2023/028). Washington, D.C.: International Monetary Fund.

[23] The Yaatal Program is the operational planning of a series of actions launched by the Senegalese tax administration in 2020 to broaden the tax base for the period 2020–2023. The objective is to increase the number of taxpayers from 25,000 to 500,000 by end-2023.

driven by corporate income tax (CIT), personal income tax (PIT), and customs duties, with respective modest growth of 0.2 percent, 0.4 percent, and 0.1 percent of GDP. However, concerns remain about the sustainability of the current revenue levels as the trend is largely attributed to cyclical factors such as rising public-sector wages and inflation-driven increases in the value of imports. In 2023, the ratio of tax to GDP was estimated to have fallen to 17.3 percent, primarily attributed to lower direct tax collection. In 2022, PIT was reformed again with the introduction of a new marginal rate of 43 percent for annual income above 50 million CFA (around 82,000 USD).

Senegal's tax revenue growth and buoyancy steadily improved over the past decade, surpassing its peers, but revenues remain below their potential.[24] This relatively good performance, however, is not sufficient to boost Senegal's ability to address the development needs of its population, and fostering resilience against uncertainty. Limited, and increasingly constrained, fiscal space continues to hinder productive investment and resilience against future shocks. Like most low- and middle-income countries, Senegal relies heavily on indirect taxes, which constituted 71 percent of total tax revenues in 2021. Reliance on trade taxes for revenue collection has declined, as fiscal transition is underway.

There is an opportunity to strategically leverage the direct tax system to enhance domestic resource mobilization. Direct taxation plays a pivotal role in fostering a more equitable society, as it allocates the tax burden to citizens and businesses in accordance with their earned incomes. Leveraging direct taxes can therefore unlock additional revenue and increase the tax system's redistributive capacity. Direct taxes have the potential to reduce post-fiscal inequality by collecting more revenues for top-income individuals and empowering governments to invest on high-value policies that protect the poor from aggregate and idiosyncratic shocks while fostering their income generation capacity. Simplifying taxes and targeting high-net-worth individuals could be more effective than raising marginal tax rates (Basri et al 2021[25] and Bergeron et al. 2023[26]). Furthermore, exploring property taxes as an untapped revenue source could further improve fiscal system progressivity.

3.1. Collected PIT revenue has stagnated, while informality hindering its redistributive capacity

The PIT as a share of GDP has stagnated over the last decade with narrow tax base undermining its performance

PIT is imposed on labor income, rental income, income from capital assets and sale of capital, business profits and pension/annuities. As a direct tax, PIT in Senegal is primarily collected through withholding rather than income tax declarations. PIT is calculated based on six net income categories including (a) salary, pensions, and life annuities, (b) property income, (c) industrial and commercial benefits, (d) agricultural profits, (e) non-commercial activities profits, and (f) income from movable assets, including securities and withheld at the source (Box 3.2). Audits of personal income taxes are limited, and Senegal has not developed a strategy to enhance compliance by high-net worth individuals.

PIT yields little revenue, and its contribution to total tax revenue has stagnated over the past decade. PIT collections have increased over the past 3 decades but yield little revenue at 2.8 percent of GDP in 2021[27] compared to OECD countries (8.3 percent of GDP),[28] although it collects similar levels to other countries in the

[24] See for instance, Diagne and Ba. 2019. "How much more can the tax administration collect? Measuring tax potential for Senegal." MPRA Paper No. 114168 for estimates and discussion on Senegal tax gap.

[25] Basri, M. Chatib, Mayara Felix, Rema Hanna, and Benjamin A. Olken. 2021. "Tax Administration versus Tax Rates: Evidence from Corporate Taxation in Indonesia." *American Economic Review*, 111 (12): 3827–71.

[26] Bergeron, Augustin, Tourek, Gabriel, Weigel, Jonathan. 2023. The State Capacity Ceiling on Tax Rates: Evidence from Randomized Tax Abatements in the DRC. National Bureau of Economic Research Working Paper Series No. 31685.

[27] Author's calculations based on OECD Global Revenue Statistics Database.

[28] OECD Global Revenue Statistics Database.

Box 3.2. Personal income tax design in Senegal

PIT is supposed to be computed based on overall net income, which encompasses six categorical net incomes:

- salaries, wages, allowances, emoluments, benefits in kind, pensions and life annuities: income tax payable on salaries, wages, pensions and life annuities is collected by withholding tax. The declaration and payment are obligatorily made by the employer each year;
- property income: it covers income from property rental exceeding 30 million FCFA (approx 49,200 USD). It can be built properties such as factories or unbuilt properties of all kinds including mines and quarries. Property income below this threshold is subject to another property tax. Residents who receive this property income must declare each year the amount of their net taxable income for the previous year. In addition, partners of real estate companies are personally required to declare their share of net property income under the same conditions. However, the withholding tax regime is applied in the case where the tenant is a legal entity;
- industrial and commercial benefits: industrial and commercial profits are the profits made by "natural person" and coming from the exercise of an industrial, commercial, artisanal profession or an agricultural profession but also the profits made by mining concessionaires as well as title holders hydrocarbon mining, mining research or exploitation permits. The term "natural persons" refers not only individual operators but also members of partnerships and similar companies, de facto companies, joint ventures and economic interest groups liable to income tax and who do not opt for corporate tax;
- agricultural profits: the same provisions as those for industrial and commercial income are applied for agricultural income. However, farmers are exempt from income tax for the sale and handling of crops and hay from the land they own and for the livestock raised there;
- non-commercial activities profits: it concerns profits from liberal professions, margins made occasionally on real estate transactions by individuals, and any other income relating to this category apart from capital gains from transfers of transferable securities and social rights, operations stock market transactions carried out on a usual or speculative basis;
- income from movable assets: these are income from securities and income from debts, deposits, guarantees and current accounts. Income from movable assets is also withheld at source.

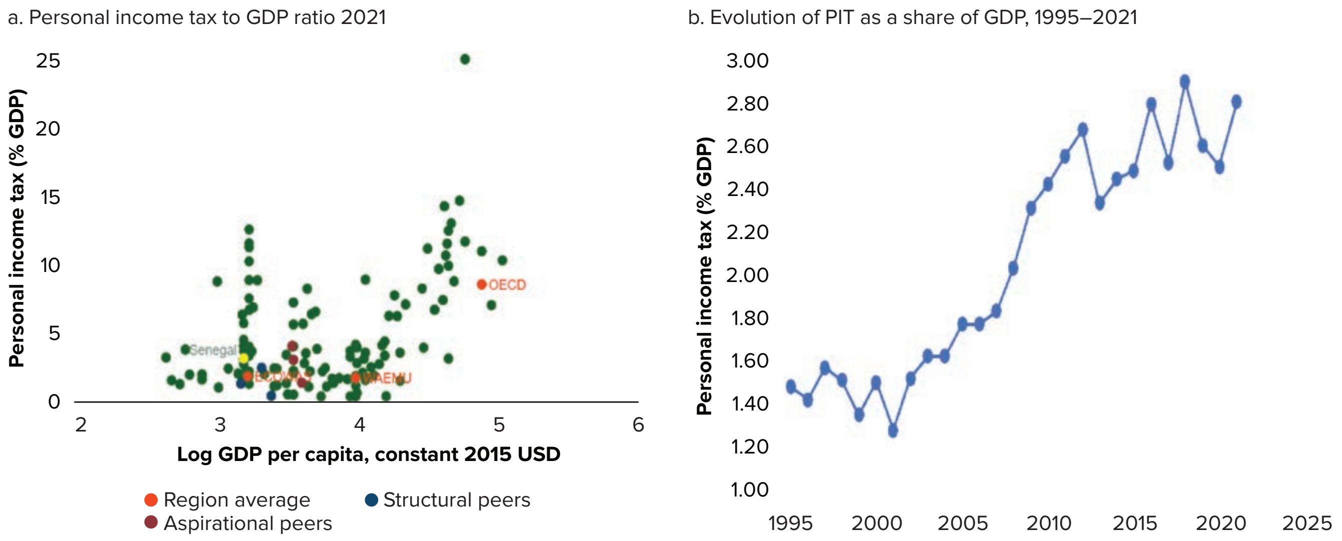
The annual net income is made up of all categorical income after deductions for actual expenses, legal allowances, and family composition. A progressive scale is applied to the net total income, excluding income from movable assets, with rates ranging from 20 percent to 43 percent with 7 brackets. All income types are withheld at source, except for rental income from properties, and mixed income from business activity (rents and mixed-income are subject to withholding when the paying source is an incorporated firm). Taxpayers benefit from a tax rebate ranging from XOF 100,000 CFA (160 USD) to 3,180,000 CFA (5,088 USD) depending on family composition.

region – WAEMU (0.82), ECOWAS (1.38) – Figure 3.1.[29] The contribution of PIT to total tax revenue has been stagnant at 15 percent between 2010 and 2021[30] despite several reform attempts. Senegal reformed PIT to shift it from proportional to progressive taxation with a capped marginal rate of 43 percent. The calculation system of tax incentives for family responsibilities was also redesigned to enhance tax justice. The family quotient approach was replaced by a progressive rate-based formula with minimum and maximum thresholds. However, the changes led to challenges in

[29] Author's calculations based on OECD Global Revenue Statistics Database. The ECOWAS and WAEMU average are unweighted and should be interpreted with cautious as data are not available for Benin, Bissau Guinea, Liberia and Sierra Leone.

[30] Author's calculations based on OECD Global Revenue Statistics Database.

Figure 3.1. PIT revenue collected in Senegal compared to peers



Source: Author's calculations based on OECD Global Revenue Statistics Database, World Development Indicators and UNU-WIDER Government Revenue Dataset, 2021.

Source: Author's calculations based on OECD Global Revenue Statistics Database and UNU-WIDER Government Revenue Dataset, 1995–2021.

capital gains taxation treatment. In fact, capital gains tax is paid in instalments, but the 2012 reform caused some confusion over those instalments' computation rules. Consequently, in 2016, the new tax code was revised to clarify those rules.

The tax base remains narrow as a limited number of taxpayers fill their tax returns. According to the tax code, all sources of income are pooled together to determine the applicable tax rate. This implies that the law imposes an integrated income tax de jure i.e., each individual should self-report his/her income each year by submitting an "Impôt sur le Revenu des Personnes Physiques" (IRPP) form. In practice this is not enforced, and PIT relies heavily on withholding rather than income tax declarations. There is legal uncertainty surrounding the reporting obligation for individuals with multiple sources of income, whether subject to withholding or not. The Tax Code lacks clarity regarding the legal requirement for residents to submit an annual personal income tax form that consolidates global income. Withholding tax stands as a discharge from an income tax return. Notably, only 11,000 Senegalese residents out of 11 million adults submit personal income tax returns each year[31] - about 0.1 percent of the adult population – reflecting a significant gap in compliance. Unlike audits for firms, individual audits are infrequent, indicating a potentially smaller tax base or insufficient control over the existing base. This results in a higher burden on a limited number of taxpayers, contributing to increased distortions in the tax system. The legal loopholes, along with the withholding mechanisms, make the PIT heavily reliable on wage earners.[32]

The absence of a strong data-driven approach has constrained the expansion of the tax base. Despite the Tax Code mandating an integrated income tax system, practical enforcement has been lacking, primarily due to the absence of a data-driven approach. Consequently,

[31] This represents the number of Senegalese residents over 15 years according to the Senegalese National Demographic Agency, 2023.

[32] Bachas et al (2023) estimates that about 250,000 individuals (about 3.1 percent of the adult population) were taxed through withholding only in 2020. About 158 000 of them were wage earners.

this has led to incomplete data coverage, undermining the overall accuracy and reliability of the database. In addition, the systematic transmission of data between the Tax Administration and the Directorate General of Taxation has been limited, creating challenges in identifying and addressing instances of non-compliance, resulting in revenue losses for the government. In the 2024 budget law however, efforts are made to improve tax compliance through enhanced cross-checking and validation techniques, which includes leveraging data from the survey of business rental properties and the national census of taxable properties to identify discrepancies and ensure the accuracy of reported income. This results in businesses and individuals largely evading taxation, raising concerns about equity and fairness. Efforts have been made by the tax administration to address this issue through synthetic tax simplifying procedures for informal businesses. However, without sufficient support and tax education, enforcing tax compliance in the informal sector remains challenging.

Within the MTRS framework, the Senegalese administration has to take numerous actions and reforms. In 2022, aligning with the Yaatal plan, a new tax bracket was introduced, raising the upper tax rate to 43 percent for income above 50 million CFA. The reporting of capital gains or profits from taxable securities sales also became mandatory. Despite these changes, the evaluation within the MTRS framework of the Senegalese tax system revealed persistent challenges that need to be addressed for an efficient DRM. In terms of income tax policy, MTRS actions focus on two main guidelines: initiating individuals' taxation and clarifying business income tax procedures. Table 3.1 below shows the level of implementation of PIT reforms included in the MTRS.

The progressivity of direct taxes contrast with its low incidence among high income households

In addition to contributing more to revenues, direct taxes have an important role in shaping the redistributive capacity of the fiscal system. In 2018–19, the fiscal system reduced income inequality by 1.8 Gini points, with direct taxes being the most important source

Table 3.1. Status on PIT reforms implementation of the MTRS

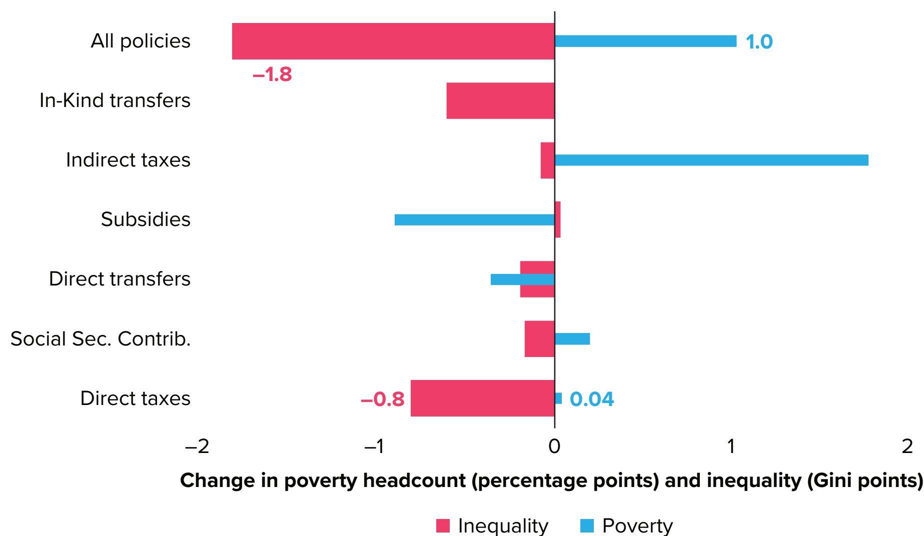
Guidelines	*Due Date*	*Status*
Initiating individuals taxation		
Establish a database of companies's executives and principal shareholders	2021	Done
Centralize information on assets (real estate, securities, vehicles, artworks . . .)	2021	Not done
Introduce a single form for salaries and withholding reports	2021	Done
Organize a public awareness campaign to enhance civic responsibility among high taxpayers	2023	Not done
Enforce mortgage registration procedure for non-payment of capital or property income tax	2022	Not done
Clarify Business Income tax procedures		
Clarify registration procedures for CGU	2023	Underway
Simplify calculation rules of CGU sales figures	2021	Done
Review micro-finance institutions and rates rate and threshold	2021	Not done
Make Non-Commercial Profits and Industrial and Commercial Profits taxes consistent with PIT, particularly tax credit for dependents with potential changes to the corporate tax rate	2022	Not done

of this decline—0.8 Gini points,[33] followed by in-kind transfers—0.6 Gini points (Figure 3.2). We expect this progressivity to have increased by 2022[34] for at least three reasons: the potential impact that the recent inflation crisis may have had on bracket creeping, the recent increase to the tax rate applied to income earners receiving more than 50 million CFA,[35] and the increase in tax compliance due to changes in the tax administration that took place under the Yaatal program. Moreover, direct taxes have a negligible impact on poverty—less than 0.1 percentage points, which is several orders of magnitude lower than what is observed for indirect taxes—1.8 percentage points.

Despite the benefits of direct taxation, the burden of direct taxes on households' income is below what is found in other African countries. In 2022, Senegalese households in the top decile of the income distribution devote about 5 percent of their income to pay direct taxes and social security contributions (Figure 3.3 and 3.4). This figure is well below what is found in Kenya—19, Namibia—12, and Mozambique—6.1. The low incidence of direct taxes suggests there is still room to increase the tax burden of top-income households. With Senegalese workers now subject to marginal tax rates of up to 43 percent for incomes over 50 million CFA, the government needs to look to alternative policies to increase revenue, such as expanding the tax base and enforcing compliance, particularly among top earners.

Direct taxation in Senegal hinges on collecting most of its revenues from households from the top decile of the income distribution – a feature that also limits

Figure 3.2. Effect of fiscal interventions on poverty and inequality in 2018–19



Source: Author's calculations based on the fiscal simulation tool for Senegal 2018- v1.2.[36]
Note: The effect of each policy on poverty and inequality is computed with respect to pre-fiscal income.

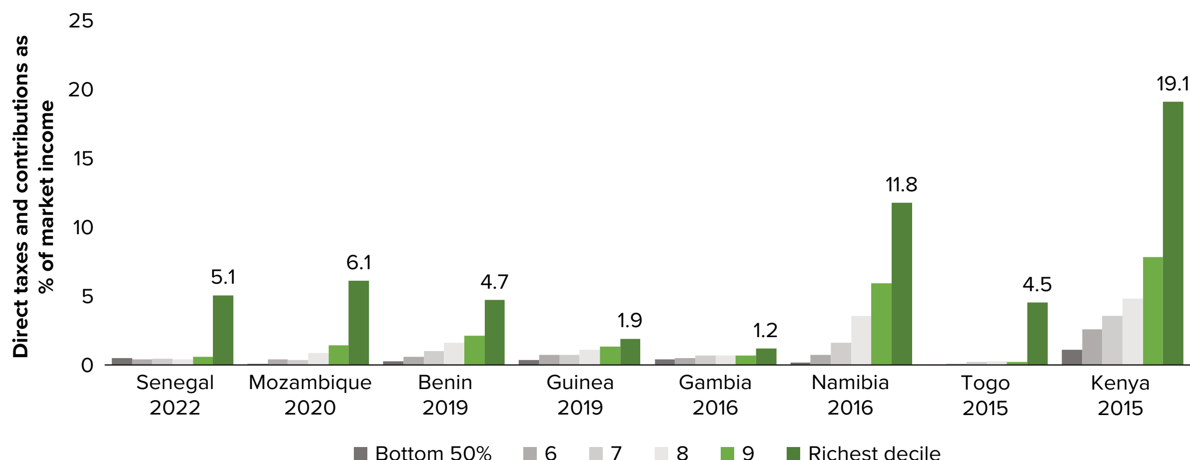
[33] Two channels explain the observed progressivity of direct taxes in Senegal. First, high income households are more likely to pay their tax obligations than their low-income counterparts. This results from high income households being more likely to work for firms that withhold their personal taxes or because their family businesses are more likely to be formal. Second, even if probability of paying taxes were the same among high- and low-income households, the progressivity of the marginal tax rates would lead to a higher tax burden for the former group of households, making direct taxes more progressive.

[34] We estimate the effect of direct taxes on inequality to also be 0.9 Gini points. However, our estimation includes more taxes and different assumptions about formality than the estimates from Gallegos et al (2024).

[35] Loi de finance n° 2022–19 du 27 Mai 2022 portant loi de finances rectificative pour l'année 2022. Publication au Journal Officiel N°7533 du 27 Mai 2022 Loi n 2022–19 du 27 mai 2022.

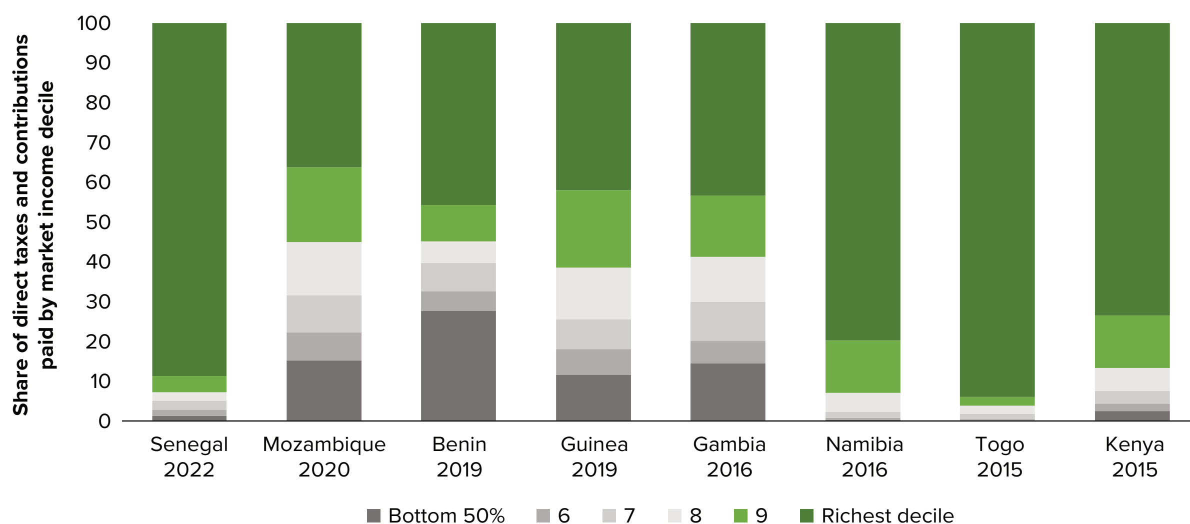
[36] Gallegos, Andres, Inchauste Gabriela and Valderrama Daniel. A new assessment of the impact of fiscal policy in Senegal. Unpublished Manuscript.

Figure 3.3. Relative incidence of direct taxes and contributions



Source: Author's calculations based on EHCVM-2019 and EHCVM 2022 and CEQ income database.
Notes: The figure reports the burden of direct taxes and contributions for each decile of market income plus pensions. This incidence is computed as a plutocratic average. We combine direct taxes with social security contributions because estimates on the tax burden for direct taxes are not available for other countries.

Figure 3.4. Distribution of direct taxes and contribution across income deciles



Source: Author's calculations based on EHCVM—2022 and CEQ income database.
Notes: The figure reports the distribution of direct taxes and contributions across the deciles of market income plus pensions. This incidence is computed as a plutocratic average. We combine direct taxes with social security contributions because estimates on the tax burden for direct taxes are not available for other countries.

revenue collection. In 2022, about 88 percent of the tax collection was paid by households in the top decile of the income distribution (see Figure 3.3). This value is higher than what is found in other African countries (e.g., Namibia, South Africa, and Kenya), where the top decile contributes up to 80 percent of the direct taxes' revenue. The main difference between Senegal and its regional peers is the relatively low share of contributions made by the second-richest decile. In countries like Kenya and Namibia, the second-richest decile made up 13 percent of tax revenues, a much higher figure than what is found for Senegal—close to 4 percent. The limited number of still high—income households paying PIT hinders the revenue potential for direct taxes. One potential reform to include other top income households in the social contract would be increase enforcement and progressivity of property taxation.

Job and business informality for high income earners hinders the redistributive capacity of direct taxes

The low levels of formality and the subsequent erosion of the tax base underscore the need for policy measures to reduce informality. The levels of formality for both jobs and businesses are particularly low, with worrying signals of deterioration. In 2018, 15.7 percent of wage earners had a formal job, defined as a job that made social security contributions to pensions. This figure has become much worse in 2022, with only 12.5 percent of wage workers being formal. This finding suggests that the post-pandemic recovery has brought lower quality jobs. Much lower levels of formality are found in the case of non-agricultural businesses, which has ranged between 4.3 and 4.9 percent during the 2019–2022 period. The low and even decreasing levels of formality erode the tax base, weakening the capacity of PIT to contribute to tax revenues. Moreover, a significant informal economy operates outside of the formal tax system, with corporate income tax contributing to less than 50 percent of total income, profits, and capital gains tax. The design of policies to reduce informality should focus on the fact that only one-third of informal workers would prefer to have a formal job (Rodríguez-Castelán and Vazquez, 2023)[37], in addition to labor market entry barriers where they may exist.

The low compliance among top earners suggests that there is still an untapped potential to increase both the revenue capacity and progressivity of direct taxes. Formality of jobs and businesses is associated with higher tax compliance. The formality rate of wage jobs and businesses is higher among high income households (See Figure 3.5 and 3.6),[38] which not only increase the progressivity of direct taxes but also prevent that changes in tax rates affect low-income households. Despite this positive association between formality and income, there is still room to enhance the redistributive capacity of direct taxes, as only one-third of jobs and less than one-fifth of businesses in the top-income decile are formal. Therefore, policies that enforce compliance among high worth net individuals have the potential to increase tax collection and enhance the redistribution of the fiscal system.

Tax rates on income sources not included in the personal income tax, are low and not progressive. Figure 3.7 shows the average tax burden among households who pay direct taxes. Focusing on taxpayers helps to isolate the effect of informality on the relative incidence of direct taxes. The figure shows that taxpayers in the tenth decile of income distribution spend up to 7.7 percent of their income on direct taxes, while households in the bottom 40 percent of the population spend less than half a percent of their income on direct taxes. On the other hand, the incidence of other taxes, such as taxes on capital, property taxes, and taxes on profits for small

[37] Rodríguez-Castelán, C. y E. Vazquez (2023). Labor Informality and Market Segmentation in Senegal. Documentos de Trabajo del CEDLAS N° 320, Octobre, 2023, CEDLAS Universidad Nacional de La Plata.

[38] Formal employees are defined as those who contribute to the pensions. Non-agricultural businesses are considered formal if they met one of the following conditions: i) the company has a TIN or a NINEA, 2) the company keeps written accounting books iii) the company is registered in the Trade Register, or iv) business' workers are registered with the Social Security Fund. All formal businesses pay taxes by filing their taxes.

Figure 3.5. Percentage of formal jobs and formal non-agricultural business

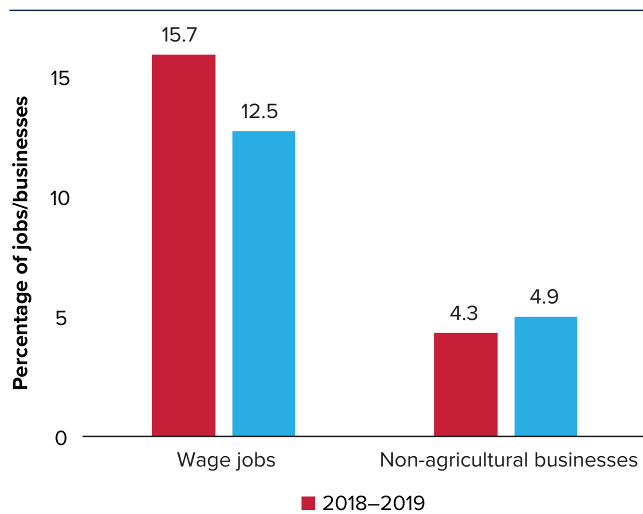
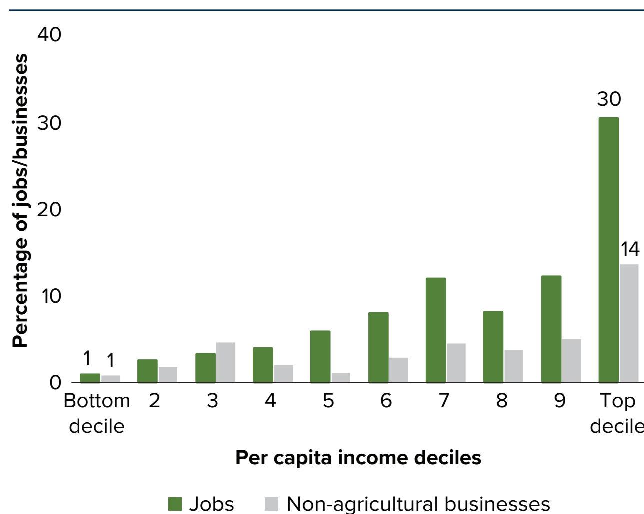
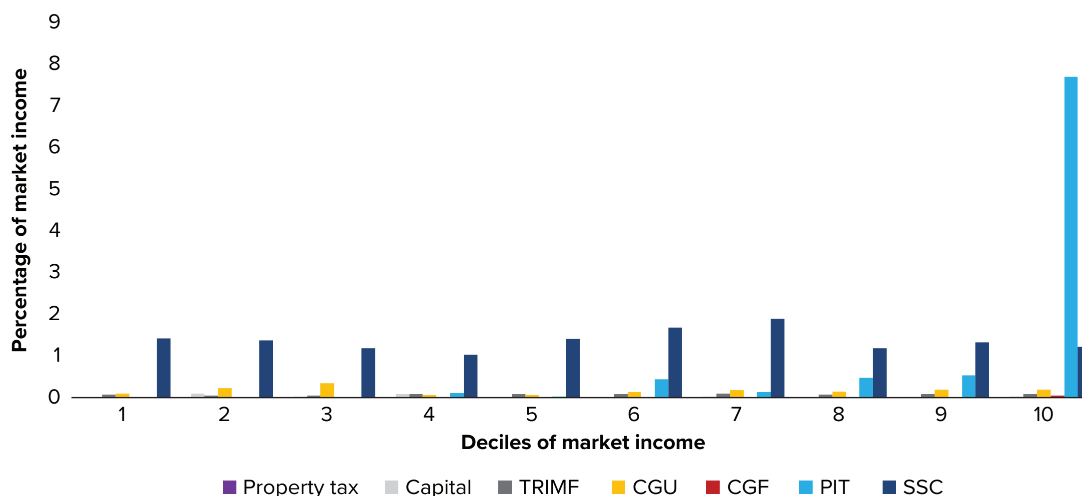


Figure 3.6. Percentage of jobs/non-agricultural business by deciles



Source: Author's calculations based on EHCVM 2022.
Notes: Formal employees are defined as those who contribute to the social security. Non-agricultural businesses are considered formal if they meet one of the following conditions: i) the company has a Tax Identification Number or a NINEA, 2) the company keeps written accounting books iii) the company is registered in the Trade Register, or iv) business' workers are registered with the Social Security Fund. The figure of panel B show the percentage of households receiving formal wages (profits from formal non-agricultural businesses) among the households reporting to receive wage income (profits from non-agricultural businesses). Deciles are computed for the per capita pre-fiscal income or the market income plus pensions.

Figure 3.7. Incidence of direct taxes among households who pay direct taxes or made social security contributions



Source: Author's calculations, based on EHCVM 2022.
Note: Property tax corresponds to the tax paid under Contribution Foncière des Propriétés Bâties, which applies to homeowners, and it assumed to be pay by population filing taxes. "Capital" refers to the capital withholdings mentioned in Art. 173 of the Tax Code, which we model as a flat rate over the dividends and financial income reported by the household. TRIMF is a synthetic tax perceived by subnational entities and it is pay through withholding by wage workers making social security contributions. CGU, the Contribution Globale Unique, is a simplified tax for small business with profits up to 50 million FCFA. CGF refers to the Contribution Globale Fonciere (CGF), a tax representative of the property tax when rental income is below 30 million CFA. PIT corresponds to the Impôt sur le Revenu, calculated over wage income, pension income, and rental income -when rental income is above 30 million FCFA, the CGF is replaced by Impôt sur le Revenu-, as well as business income over 50 million FCFA, known as Régime Réel. SSC refers to social security contributions to health. Deciles are computed for the per capita pre-fiscal income or the market income plus pensions.

firms—CGU; is relatively low (less than half a percent across all income deciles) and almost flat along the income distribution. This is in line with the fact that the tax rates applied to these other revenue sources are subject to low and non-progressive tax schedules, limiting revenues and the extent to which fiscal policy can reduce inequality. A confluence of different factors can explain the large difference between the effective tax rates and the tax rate of the top income bracket, for example: tax allowances, tax discounts due to family composition, low fraction of people earning more than 50 million CFA, the withholding mechanism that prevents individuals from pooling income sources, among others. An avenue for future analysis is to disentangle the role of these factors using tax record data.

3.2. Policy options to increase revenues from direct taxes without increasing poverty or inequality

Enforcing the filing of direct taxes could bring triple wins by increasing revenue while reducing both poverty and inequality

This subsection assesses the revenue and distributional implications of enforcing the filing of direct taxes. There is widespread agreement that all taxpayers should be filling PIT in line with YAATAL. As explained before, the law imposes a global tax base over PIT, where income sources from labor, business profits, pensions, and rental income should be pooled together in a tax declaration to define the tax rate and the tax discount to which each individual is liable for. However, less than 10 percent of individuals file tax declarations, with the majority paying PIT through withholding (Bachas et al. 2023). This section estimates the distributional impact of enforcing tax declarations on all income sources that are subject to direct taxation, which means income sources beyond those included in the personal income tax, namely rental income, property income, and profits for small firms with turnover below 50 million CFA.

Our estimates are only indicative of the direction of the expected impacts and can be improved if combined with tax record data. Our analysis relies heavily on the recently collected household living standards survey – EHCVM 2021–22, which implies that they should be considered a lower bound of potential benefits of enforcing tax filing. This is because top earners are under-represented in household surveys and tend to under-report their income. Obtaining access to tax records is a crucial next step to accurately quantify the benefits of policies around direct taxation.

Enforcing tax declarations over all types of income sources, not only over the ones that are subject to the PIT, will increase tax revenues through three channels:

- *Increasing marginal tax rates*. This effect affects the income sources that are subject to the PIT. Given the progressivity of the current tax schedule, pooling income sources in the tax declaration will increase the average tax rate applied to each income source, increasing both the revenues and progressivity of direct taxes.
- *Adding other income sources*. Filing taxes is expected to increase tax compliance on taxes that are not collected through withholding, such as: pensions, rental income, small business profits and property taxes. This assumes that enforcing tax filing will translate in a self-enforcing mechanism in which adults that were already subject to PIT through withholding or tax filing will start to report their other income sources.
- *Reducing tax discounts*. Tax discounts due to family characteristics (such as the number of dependents) are progressive, i.e., they are higher for individuals with lower taxable income. Therefore, pooling income sources will reduce the relative size of tax discounts, increasing the average tax rate of previously withheld sources.

High-income households would pay the bulk of revenue gains from enforcing tax filing. Figure 3.8 displays the deciles and income sources from which the additional revenues would come. Most of the additional revenues—about 95 percent of them—are anticipated to come from households in the top decile of the income distribution, with approximately 57 from rental income, 12 from property taxes, and 26 percent from labor income. Household surveys are not the best instrument to estimate absolute

Figure 3.8. Additional revenue gains from enforcing filing of direct taxes

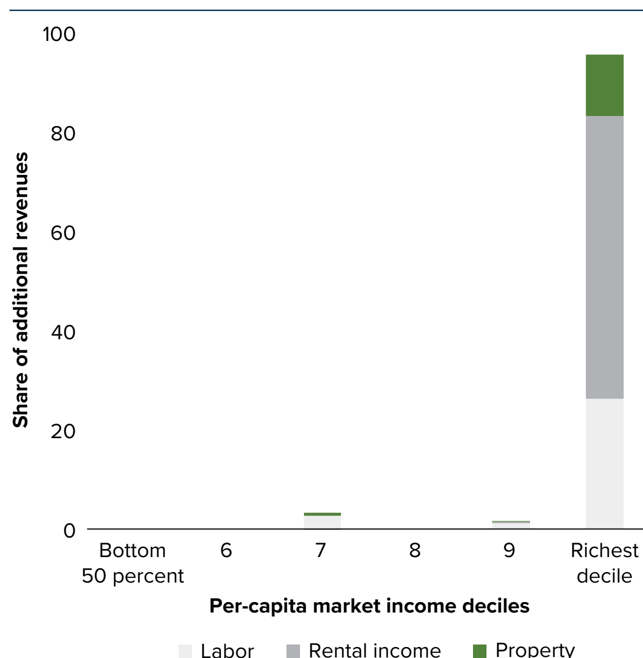
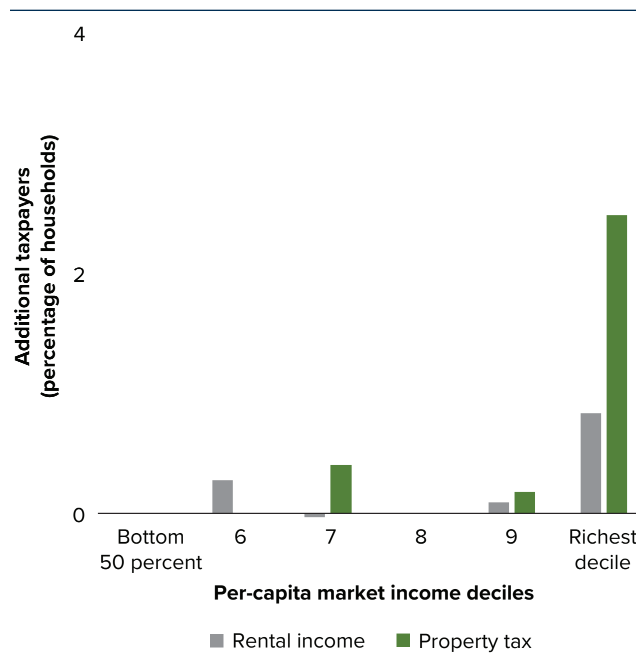


Figure 3.9. Incidence of direct taxes among households who pay direct taxes by decile



Source: Author's calculations based on EHCVM 2022.
Notes: Property refers to taxes collected from the Contribution Foncière des Propriétés Bâties, which applies to homeowners, and it is assumed to be paid only by the population filing taxes. Rental income refers to the Contribution Globale Fonciere (CGF), a tax representative of the property tax that is calculated over the rental income. Labor refers to the tax collected from previously withheld labor income and the addition of other income sources such as pensions and profits. Figure 3.8 plots the distribution of additional revenues by decile and income sources. Figure 3.9 plots the addition percentage of households paying tax over a specific income source as a result of the reform. *Deciles are computed for the per capita pre-fiscal income or the market income plus pensions.*

gains from policies targeted at top earners. We assume revenues from enforcing tax filing would increase by 30 billion CFA, which corresponds to the estimate obtained by Bachas et al. (2023) using tax record data.[39] Obtaining access to tax records is the natural next step of this analysis, and it would allow a more accurate quantification of the policy-induced impacts on both revenue and progressivity of the tax system in Senegal. Similar to what has been done in other developing countries like Colombia and Peru.[40]

The main channel behind the additional revenues is the increase of taxes from non-withheld income sources. We find that the increase in revenues is primarily due to an increase in taxpayers filing taxes over rental income and property. Even when property taxes are not an income component of the personal income tax, our exercise assumes that filing taxes would allow the tax authority to enforce the payment of all other income sources for which taxes are not collected through withholding (e.g., property taxes, small rental income). Figure 3.9 quantifies the potential size of this effect, with the simulated policy increasing the number of new taxpayers paying taxes over their rental income and properties. In particular, an additional 0.8 and 2.5 percent of households in the top decile would start paying taxes on their rental and property income, respectively. Notice our estimates assume that increasing tax filing among people only people filing taxes in the baseline scenario.

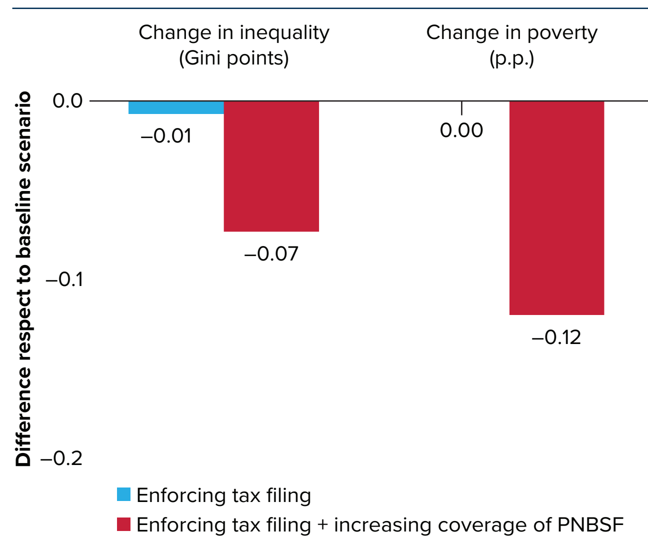
[39] Conducting this analysis with household survey leads to an estimate much lower than Bachas estimate, which stress out the need of tax record data to complement this exercise.

[40] See World Bank (2023) for the case of Peru and Baquero et al (2023) for the case of Colombia.

Enforcing tax filing could bring additional revenues without imposing any social cost in terms of poverty and inequality. As shown above, the simulated reform is not expected to collect additional revenue from the poorest 50 percent of the population, and therefore, it is not expected to increase the poverty headcount. The impact of the reform on inequality is expected to be negligible (i.e., 0.01 Gini point). This result should be considered a lower bound because, as explained before, our microdata is not well suited to illustrate the equalizing effect of policies targeting top-earners. It is important to note that this policy reform could affect poor population by imposing on them the cost of tax filing. Therefore, the design of this policy should target its enforcement over people identified as potential taxpayer, to minimize the people with zero tax liabilities paying the cost of tax filing. Our simulation enforced tax filing over people whose labor income tax was withheld and therefore who had nonzero tax liability.

Repurposing a fraction of the fiscal gains into direct transfers could bring triple wins: more revenues, less poverty, and less inequality. Figure 3.10 shows the effects of repurposing 25 percent of the tax gains to finance greater coverage of direct transfers, which are policies more equipped to reach low-income households. Since our estimate on additional tax revenues would be downward biased, we use the estimates obtained by Bachas et al. (2023), which amount to 30 billion CFA – approximately 48 million USD. Figure 3.10 shows that this complementary policy could expand the coverage of PNBSF to 75 thousand new households, which will reduce inequality -by 0.08 Gini points-, and poverty –0.13 percentage points-, helping to increase the redistributive capacity of Senegal's fiscal system (see Figure 3.10).

Figure 3.10. Effect of enforcing tax filing and increasing the coverage of direct transfers



Source: Author's calculations, based on EHCVM 2022.
Note: The figure reports the difference in poverty and inequality of disposable income between the baseline scenario and the simulated scenarios. Compensatory measures refer to an expansion of PNBSF such that its cost is equal to a quarter of the fiscal gains obtained from enforcing tax filling.

Focusing on high net worth individuals could bring substantial revenues[41]

Focus on the taxpayers at the very top of the income and/or wealth distribution – to optimize the limited resources of the tax administration, increase PIT revenue, and improve the progressivity of the tax system.

International practice varies in terms of the concepts and data used to define high net worth individuals (HNWI). Some countries focus on wealth only (e.g., UK and Australia) and others combine wealth with income (e.g., USA and South Africa). Other criteria used by tax administrations include property valuation and indirect indicators of wealth (such as known public figures or consumption of durable goods). These criteria are often combined and include income and/or wealth thresholds, although there is no general rule (OECD, 2013). Given the complexity of identifying, monitoring, and interacting with HNWI, countries often introduce dedicated units. High-income countries such as the US, the UK, New Zealand, and Australia have implemented such specialized task forces within their respective tax administrations (Van Vuuren, 2016) and low and middle-income countries are increasingly adopting this practice. A recent example is Uganda: its HNWI office recently started with a few hundred individuals, selected as follows: "the officials generated a list

[41] This section builds on Bachas and al. (2023).

of potential HNWIs, comprising directors of large companies under the Large Taxpayers Unit (LTU) and individuals whose wealth was publicly known. The list was scrutinized by top management in the Domestic Taxes Department, who made revisions on the basis of their own knowledge" (Kangave et al., 2018). Since then, the inclusion criteria evolved to a monthly income threshold of UGX 10,000,000 (2,800 USD).

Senegal could benefit from detecting high earners in a context of imperfect information. Senegal could focus on the taxpayers at the very top of the income and/or wealth distribution. Identifying very rich individuals is of primary relevance. The ideal target population are individuals with true income and wealth in the top percentiles of Senegal's distribution. There is no consensus on an international definition of HNWI, implying that Senegal would have to exploit all sources of data, ongoing digitalization processes, and local context to define the appropriate threshold (Box 3.3). Potential tax revenue gains could occur from the declaration of previously non-declared income, and changes in marginal tax rates due to the consolidation of income sources. Bachas et al (2023) find that if all income sources were integrated, the tax administration would have collected an additional 30 billion CFA (48 million USD) in 2020, i.e., about 1% of total tax revenue and 8.5% of PIT revenue. The main addition comes from the integration of property income

Box 3.3. How to detect high earners in a context of imperfect information

In the current context of Senegal, Bachas et al (2023) define HNWI individuals within the top 0.1 percent of the national income distribution. With no information on true income, they proxied total income and wealth with observable income and wealth using available data. They consider each data source individually and select the top of the distribution. They first chose thresholds to encompass the top 0.1 percent of the largest administrative data sources on income and wealth, respectively, data on salaries and property values. They then adapt these thresholds depending on the nature of the data (e.g., lower thresholds for dividends since infrequent). This allows them to generate what they refer to as the First List of 558 HNWIs at the very top of the income or wealth distribution (i.e. 0,007% of the national adult population). Importantly, 80% of them do not file PIT currently. The median annual income of this list is 121 million CFA (200,000 USD) and the median wealth is 6.35 billion CFA (10 million USD).

The first list considers taxpayers with extremely high income and wealth. To complement this first approach, the second approach enlarges the net to consider any taxpayer whose consolidated income places them in the former top marginal tax bracket, but who does not appear to be currently reporting all revenue sources, when comparing self-reported income with third-party reported income. This second list comprises 1,992 individuals (i.e., 0,02% of the national adult population) with a median yearly income of 21.1 millions CFA (34,000 USD). It includes (1) rich individuals (income eligible for the former highest MTR, i.e., yearly income above 13.5 million CFA – approx 22,000 USD) currently NOT filing the PIT but credibly identified as receiving income from multiple sources and, (2) Rich individuals currently filling the PIT but with discrepancies as compared to available information (PIT-filers not reporting or under-reporting a source of income identified from cross-checks).

The cross-validation of tax statements and the merging of data from different sources permitted to generate more complete information on individuals' total income and wealth and to estimate the potential loss in personal income tax revenue from high earners in Senegal. The authors then integrate income from the third-party sources (salaries, rents from property, dividends) with the personal income tax declarations, for individuals on the two lists of HNWIs. They then recalculate the PIT due on this consolidated tax base, as opposed to what was actually paid or withheld.

(which faces no withholding except for business leases), followed by higher rates on labor, and then on other capital income. The HNWI in the two lists (2,550 individuals or top 1% of the sample) contribute 40% of the total additional collectible revenue (12 billion CFA).

Establishment of a dedicated tax unit for HNWI. Currently, the responsibility of increasing compliance with the HNWI population is shared across several departments: the Directorate for Information and Audits, the Large Taxpayer Unit, and the local tax offices existing in each geographical district who are, in theory, the direct interlocutors of individual taxpayers. Because increasing compliance with HNWIs requires specific resources, skills, and analytical capacity, DGID could centralize these efforts and these responsibilities in a single unit, which would, of course, work in collaboration with all relevant directorates. The tax administration can leverage ongoing efforts to establish a data-driven approach to expand the tax base to identify HNWIs and conduct a pilot intervention targeted before extending a complete framework to all HNWIs.

Policies to improve tax administration capacity

Strengthen enforcement, data and evidence-based approach. DGID can increase PIT compliance and collect tax revenues by increasing enforcement activity. The DGID can consider setting up a dedicated team to focus HNWIs – similar to the Ugandan case. The local fiscal centers could facilitate the identification and contact of the selected HNWIs by helping to recover their digital IDs, addresses, and phone numbers. Complementary interventions could consist of harmonizing practices to follow-up with taxpayers, register contacts details, and audit procedures (Box 3.4). All these interventions would

Box 3.4. Digital IDs in Senegal. Practices and how to improve linkages

Senegal relies on two key digital IDs for tax-related purposes:

- NINEA: a unique taxpayer registration number, exists both for individuals (individual entrepreneurship) and corporations. It is delivered by the National Statistical Agency (ANSD).
- CNI: National ID Number. The IDs are delivered by the Ministry of the Interior. A CNI is required for the ANSD to create a NINEA for a given taxpayer.

The challenge is that many taxpayers are known to the DGID but are not linked to any of these IDs. This is the case for the majority of employees in the États 1024 data (Salaries withheld), for the majority of property owners in the SIGUIL data (Property tax), and for the majority of shareholders and administrators. Furthermore, to encourage interoperability across administrations, the DGID does not directly generate NINEAs, but instead sends creation requests one by one to the ANSD on a web platform.

Data quality and merging issues could be mitigated on several dimensions:

- Consistency in the use of digital IDs (NINEA, CNI): Providing them in every tax return and other administrative forms and working towards the association of an ID to each taxpayer already known by the DGID would improve the consistency of the reports and would facilitate auditing.
- Digitization: data is not always available in a numerical format, which is primordial to cross-checking information. Digitizing data is resource-consuming and has to be done in a timely manner to meet the legal prescription constraints, generalizing the numerical format would be incomparably more efficient.

Source: Bachas et al (2023).

require the tax administration to invest in the technical and human capacity of the tax administration to handle the increased volume of information from compulsory tax returns. This includes upgrading information systems and hiring diverse professionals with expertise in data analysis to process and manage the data efficiently. Limited resources could limit the possibility for the administration to exploit all the data and information submitted and to follow-up with all individuals, accordingly, implying the need to establish a clear strategy.

Implement Transparent Communication Strategies: Develop and execute transparent and engaging communication strategies to enhance tax compliance. This should involve proactive tax education initiatives, clear information dissemination about tax obligations and compliance benefits, and targeted awareness campaigns through various channels to build a trusting relationship between taxpayers and the tax administration. The communication strategy could be centered first around the complete list of all income sources that individuals are legally responsible for reporting and information on the progressive tax schedule. The tax administration could also dedicate efforts to explaining how withholding works in combination with payments related to PIT returns, providing information on e-filing, and supporting mechanisms for the submission of tax returns. There might be substantial risks to political interest in targeting HWNIs due to a potential overlap between political elites and top earners. To address these potential challenges, the tax administration could establish a clear communication strategy (letters to taxpayers incentivizing them, for instance) around the use of data and evidence to improve to avoid potential misunderstandings related to personal targeting.

Clarify Legal Framework for Tax Declarations: The tax administration could take a stronger stance on the legal obligation for all income earners to submit a PIT return through a revision of the tax code. The amendment of the tax code could resolve ambiguities between the “final” nature of withheld incomes and the requirement for a consolidated declaration. Strengthening the legal obligation for all income earners to submit a PIT return should be accompanied by clear guidelines on declarative obligations for all types of income, whether subject to withholding or not, to encourage taxpayers to obtain tax identification numbers and comply with tax laws.

Strengthen cooperation between tax administration and financial institutions. In theory, tax authorities can use financial institutions to request more information about taxpayers. However, these procedures are more difficult to carry out. Improving information exchange between revenue administration and financial institutions could enhance audits and tax collection among non-compliant taxpayers.

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