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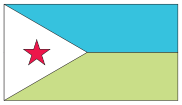
DJIBOUTI



ECONOMIC MONITOR

Strengthening the Sustainability and Equity of Public Finances

Fall 2024

PROSPERITY
Middle East and North Africa
THE WORLD BANK

Djibouti Economic Monitor

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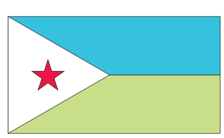

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Publication design and typesetting by The Word Express, Inc.

TABLE OF CONTENTS

List of Figures

List of Tables

List of Boxes

ACKNOWLEDGEMENTS

This edition of the Djibouti Economic Monitor was prepared by a team led by Rick Emery Tsouck Ibounde (Senior Economist for Djibouti) under the guidance of Stéphane Guimbert (Regional Director of Operations for Djibouti, Egypt, and Yemen), Nadir Mohammed (Regional Director for North Africa and the Middle East, Equitable Growth, Finance, and Institutions), Éric Le Borgne (Head of the Macroeconomics, Trade, and Investment Division for North Africa and the Middle East), Salman Zaidi (Head of the Poverty and Equity Division), Fatou Fall (Resident Representative for Djibouti), and Mark Eugene Ahern (Chief Economist, Equitable Growth, Finance, and Institutions Division for Djibouti, Egypt, and Yemen).

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Chapter III is a synthesis of a report[1] on the tax incidence on poverty and equity prepared by Bilal Malaeb, Sandra Martinez, Cristina Carrera, Giorgio Maarraoui, and Idriss Okiye Waais. Chapter IV is a synthesis of work conducted by Clotilde Minster, Nouhayla Boubekri, and Nada Bona, funded by the Quality Infrastructure Investment Partnership, for which the authors are thankful. The World Bank team would like to thank numerous governmental entities for their collaboration, in particular, the Ministry of Infrastructures and Equipment; the Djiboutian Road Agency; Djibouti Ports Corridor Roads SA; the Ministry of Social Affairs and Solidarity; the Central Bank of Djibouti; the Directorate of Economy and Planning; the Directorate of Customs and Indirect Rights; the Directorate of Public Debt; the

[1] This chapter is a synthesis of an in-depth analysis prepared by the World Bank's Poverty and Equity team: Bilal Malaeb, Sandra Martinez, Cristina Carrera, Giorgio Maarraoui and Idriss Okiye Waais. The team would like to thank the teams at the Ministry of the Budget, the Ministry of Economy and Finance and the Institut National de la Statistique de Djibouti (INSTAD) for their collaboration, information and advice in drafting the analyses used in this report. The team would also like to thank Alan Fuchs, Johannes Hoogeveen, Rick Tsouck Ibounde, Federica Marzo, Anne Marie Duplantier, Federica Alfani, Alex Kamurase and Asli Mohamed for their support, comments, and suggestions. The link to the full analysis is: https://documents1.worldbank.org/curated/en/099062223112522461/pdf/P1745720795cc20d10b03e00aeaea566192.pdf/.

Directorate of Budget; the National Institute of Statistics of Djibouti (INSTAD); and the Port Authority and Free Zones of Djibouti (APZFD), who provided the necessary data and information for this update.

The findings, interpretations, and conclusions expressed in this report are those of the authors alone and in no way reflect the views of the members of the Board of Directors of the World Bank or the countries they represent.

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EXECUTIVE SUMMARY

Djibouti's economy achieved an impressive rebound in 2023, outperforming forecasts with GDP growth estimated at 6.7 percent. The country benefited from a recovery in Ethiopia's growing demand for port and logistics services following the country's political stabilization. This demand boosted the volume of goods and containers handled in Djibouti's ports. In addition, domestic demand remained strong, supported by a recovery in private investment and government measures to mitigate the effects of inflation caused by the Russian invasion of Ukraine. Improvements were also seen in the primary sector, particularly due to the resumption of livestock exports to Gulf countries.

After peaking at 11 percent in June 2022, inflation stabilized at 3.8 percent in December 2023, with a reduction in core inflation. This stabilization is partly attributed to government measures to preserve purchasing power, such as awareness campaigns, strict price controls on basic foodstuffs, and VAT exemptions for certain products. Energy prices showed little change, while fresh food prices rose sharply, mainly due to shortages of imports from Ethiopia. On an annual average basis, consumer prices rose moderately by 1.4 percent, reflecting a year-on-year decline.

Djibouti faces budgetary challenges marked by a structural decline in revenues, notably due to the increase in tax exemptions which reached 19 percent of GDP in 2022, reducing tax pressure. Tax revenues fell from 13 percent of GDP in 2019 to 11.4 percent of GDP. In 2023, despite a nominal increase in revenues, tax revenues slightly increased to 11.5 percent of GDP thanks to economic recovery, but were offset by a decline in non-tax revenues. The increase in public spending, especially in capital, and the rise in LIBOR led to a budget deficit of 1.9 percent of GDP, financed by external borrowing. The primary deficit, which went from 0.7 percent of GDP in 2022 to 1.1 percent of GDP in 2023, confirms the deterioration of the budgetary situation, exacerbated by rising interest payments. This situation underscores the need for measures to increase domestic revenues and better manage public spending.

The debt situation remains concerning despite a debt-to-GDP ratio of 67 percent in 2023, which might seem moderate. The stock of arrears on external debt reached about 6 percent of GDP at the end of June 2023, suggesting cash flow tensions. This accumulation, mainly vis-à-vis China Eximbank and EXIMBANK India suggests challenges in cash flow management. The end of the G-20 Debt Service Suspension Initiative (DSSI), the maturity of the loan for the Djibouti-Ethiopia water pipeline, and the economic repercussions of the war in Ethiopia and the Russian invasion of Ukraine have exacerbated these tensions. The Djiboutian government announced on October 18, 2023, that it had reached an agreement with China Eximbank regarding the treatment of its debt to this institution. The agreement would include a four-year moratorium starting in 2024, during which Djibouti would only pay the equivalent of 20 percent of the service due during this period and would continue negotiations with China Eximbank on a debt restructuring. However, to get out of this over-indebtedness situation, Djibouti will need to fully clear its external arrears, including those vis-à-vis India Eximbank and the Paris Club. Moreover, the results of the simulation conducted by the World Bank team on the sustainability of Djibouti's public debt show that returning to a sustainable debt level would require a freeze on non-concessional borrowing, a deep restructuring of the entire portfolio of Djibouti's bilateral external debt, as well as intensified efforts to mobilize state revenues.

The banking sector has shown resilience to external shocks, with an increase in credit to the private sector and a significant reduction in non-performing loans. However, international reserves have decreased by 14.7 percent compared to the previous year. The balance of payments improved at the end of 2023, with a notable surplus in the current account balance of more than 32 percent, mainly due to an increase in exports of goods and services. The trade balance recorded a surplus of nearly 80 billion DJF, an increase of 64.5 percent year-on-year.

Ongoing disruptions in the Red Sea have mixed impacts on Djibouti's economy. Transshipment activity at the port of Djibouti has been strengthened, leading to a 39 percent increase in container volume handled in March 2024 compared to November 2023. The container volume more than doubled compared to March 2023, reaching 110,000 TEU and surpassing pre-pandemic levels. This rapid growth results from a strategy by carriers to minimize risks related to crossing the Red Sea. They have thus shifted their transshipment operations to Djibouti, strategically located south of this area, to bypass regions controlled by the Houthi movement. On the other hand, the crisis has led to a significant increase in maritime freight costs, which is reflected in the prices of consumer goods in Djibouti. In March 2024, inflation in Djibouti reached 5 percent, its highest level since December 2022, mainly due to a 6.1 percent increase in the prices of food and non-alcoholic beverages, affecting different regions of the country differently. Moreover, tensions in the Red Sea affect Djibouti's customs revenues, which fell by about 910 million Djiboutian francs (0.1 percent of GDP) in the first quarter of 2024, mainly affecting value-added tax and excise duties on tobacco and alcohol imports, exacerbating budgetary challenges already increased by the costs of oil subsidies.

The medium-term outlook is positive, with annual GDP growth expected at 5.1 percent from 2024 to 2026, supported by foreign trade and major public works projects. However, the continued accumulation of public debt and regional tensions are risks that require prudent management to ensure Djibouti's future financial stability. Moreover, Djibouti's growth model faces several vulnerabilities, notably a strong dependence on global maritime transport and exposure to regional conflicts, including those of its neighbors. To strengthen the viability and equity of public finances, particular attention must be paid to optimizing fiscal efficiency and prudent management of public finances. This will support economic growth while reducing vulnerabilities related to external shocks and debt.

The first special chapter of the Djibouti Economic Outlook examines the redistributive effects of the country's fiscal system, analyzing how different taxes and transfers affect poverty and inequality. The study includes simulations such as the expansion of cash transfers, the rising costs of stabilizing kerosene prices, and an increase in public spending on health. The analysis reveals that, despite promoting equality, the system exerts upward pressure on poverty. Direct taxes prove progressive, improving equity, while VAT, despite being crucial for revenue mobilization, increases the burden on the poorest given its regressive nature. The National Family Solidarity Program (PNSF) effectively targets low-income households, reinforcing its progressive nature. However, kerosene subsidies, while significant, mainly benefit the wealthiest households. Precisely, while these subsidies benefit the poorest in absolute terms due to the cost burden of kerosene being relatively heavier on their budgets, the benefits are disproportionately accrued to the wealthier households in relative terms due to their higher consumption of the kerosene product. Transfers in kind, such as education and health spending, while advantageous, do not always reach the poorest in an equitable manner. The need for tax reforms targeting more equitable redistribution and increased revenues without exacerbating poverty is underlined, notably by rethinking kerosene subsidies and maximizing the benefits of social programs such as the PNSF, which exclusively targets the poor populations.

At the same time, a study of public spending in the road sector—an essential sector for the competitiveness of Djibouti's ports—reveals major financing and management challenges. Institutional reform could clarify roles, strengthen local maintenance, and diversify funding sources, thereby significantly improving the efficiency of public spending in this vital sector. The second chapter presents the current mechanisms for financing the road sector and examines what institutional reform in the road sector would bring in terms of the budgetary efficiency of road infrastructure investments. This analysis reveals three main challenges: (1) an inefficient institutional organization with overlapping responsibilities, (2) a poorly maintained road network and a lack of small local enterprises for maintenance, and (3) insufficient and poorly managed funding, with high salary costs. To improve efficiency, it would be useful to clarify institutional roles, develop the local maintenance sector, and diversify funding sources, notably by creating a road fund and a road agency. These reforms require strong political will and could significantly transform Djibouti's transport sector.

RÉSUMÉ

L’économie de Djibouti a réalisé un rebond impressionnant en 2023, surpassant les prévisions avec une croissance du PIB estimée à +6,7 %. Le pays a bénéficié d’une reprise de la demande croissante de l’Éthiopie pour les services portuaires et logistiques après la stabilisation politique dans ce pays. Cette demande a stimulé le volume des marchandises et des conteneurs traités dans les ports djiboutiens. Par ailleurs, la demande intérieure est restée forte, soutenue par la reprise de l’investissement privé et les mesures gouvernementales visant à atténuer les effets de l’inflation causée par l’invasion russe. En outre, des améliorations ont été observées dans le secteur primaire, notamment grâce à la reprise des exportations de bétail vers les pays du Golfe.

Après avoir atteint un pic de 11 % en juin 2022, l’inflation s’est stabilisée à 3,8 % en décembre 2023, accompagnée d’une baisse de l’inflation sous-jacente. Cette stabilisation est attribuée en partie aux mesures gouvernementales de préservation du pouvoir d’achat, telles que des campagnes de sensibilisation, un contrôle strict des prix de produits alimentaires de base, et des exonérations de TVA pour certains produits. Les prix de l’énergie ont peu varié, tandis que les prix des produits alimentaires frais ont connu une forte hausse, notamment en raison de pénuries d’importations de l’Ethiopie. En moyenne annuelle, les prix à la consommation ont augmenté de façon modérée de 1,4%, reflétant une baisse par rapport à l’année précédente.

Djibouti fait face à des défis budgétaires marqués par une baisse structurelle des recettes, notamment en raison de l’augmentation des exonérations fiscales qui ont atteint 19 % du PIB en 2022, réduisant la pression fiscale. Les recettes fiscales ont baissé de 13 % du PIB en 2019 à 11,4 % du PIB. En 2023, malgré une hausse nominale des revenus, les recettes fiscales ont légèrement augmenté à 11,5 % du PIB grâce à la reprise économique, mais ont été contrebalancées par une baisse des recettes non fiscales. L’augmentation des dépenses publiques, surtout en capital, et la hausse du LIBOR ont conduit à un déficit budgétaire de 1,1 % du PIB, financé par des emprunts extérieurs. Le déficit primaire, passé de 0,7 % du PIB en 2022 à 1.1% du PIB en 2023, confirme la détérioration de la situation budgétaire, exacerbée par des paiements d’intérêts croissants. Cette situation souligne la nécessité de mesures pour augmenter les recettes intérieures et mieux gérer les dépenses publiques.

La situation d’endettement demeure préoccupante malgré un ratio dette/PIB de 67 % en 2023 qui pourrait sembler modéré. Le stock des arriérés sur la dette extérieure a atteint environ 6 % du PIB à la fin juin 2023, suggérant ainsi des tensions de trésorerie. Les autorités nationales ont toutefois rapporté qu’à la fin mars 2024, le stock des arriérés de la dette extérieure avait diminué à 1,6 % du PIB, légèrement au-dessus du seuil de surendettement. Cette accumulation, principalement vis-à-vis EXIMBANK Chine et EXIMBANK Inde, indique des défis significatifs en matière de gestion de la trésorerie. La fin de l'Initiative de suspension du service de la dette (ISSD) du G-20, l'arrivée à maturité du prêt pour le pipeline d'eau Djibouti-Éthiopie, et les répercussions économiques de la guerre en Éthiopie et de l'invasion russe en Ukraine ont exacerbé ces tensions. Le Gouvernement djiboutien a annoncé, le 18 octobre 2023, avoir conclu un accord avec EXIMBANK Chine concernant le traitement de sa dette envers cette institution. L'accord inclurait un moratoire sur quatre ans à partir de 2024, période au cours de laquelle Djibouti ne paierait que l'équivalent de 20 % du service dû pendant cette période et poursuivrait les négociations avec EXIMBANK Chine sur une restructuration de sa dette. Cependant, pour sortir de cette situation de surendettement, Djibouti devrait procéder à un apurement complet de ses arriérés extérieurs, y compris ceux vis-à-vis d' EXIMBANK Inde et du Club de Paris. Par ailleurs, les résultats de la simulation effectuée par l'équipe de la Banque mondiale sur la soutenabilité de la dette publique de Djibouti montrent que le retour à un niveau d'endettement soutenable nécessiterait un gel des emprunts non concessionnels, une restructuration profonde de l'ensemble du portefeuille de la dette extérieure bilatérale de Djibouti, ainsi qu'une intensification des efforts de mobilisation des revenus de l'État.

Le secteur bancaire a démontré une résilience face aux chocs externes, avec une augmentation des crédits au secteur privé et une réduction significative des prêts non performants. Cependant, les réserves internationales ont diminué de 14,7% par rapport à l'année précédente. La balance des paiements s'est améliorée fin 2023, avec un excédent notable du solde des transactions courantes de plus de 32%, principalement dû à une augmentation des exportations de biens et services. La balance commerciale a enregistré un excédent de près de 80 milliards de FDJ, une hausse de 64,5% sur un an.

Les perturbations en cours dans la mer Rouge produisent des impacts mitigés sur l'économie de Djibouti. L'activité de transbordement au port de Djibouti a été renforcée, entraînant une augmentation de 39 % du volume de conteneurs traités en mars 2024 par rapport à novembre 2023. Le volume des conteneurs a plus que doublé comparé à mars 2023, atteignant 110 000 TEU et surpassant les niveaux pré-pandémiques. Cette croissance rapide résulte d'une stratégie des transporteurs visant à minimiser les risques liés à la traversée de la mer Rouge. Ils ont ainsi déplacé leurs opérations de transbordement à Djibouti, situé stratégiquement au sud de cette zone, afin de contourner les régions contrôlées par le mouvement houthi. En revanche, la crise a conduit à une hausse significative des coûts du fret maritime, qui se répercute sur les prix des biens de consommation à Djibouti. En mars 2024, l'inflation à Djibouti a atteint 5 %, son plus haut niveau depuis décembre 2022, principalement en raison de la hausse de 6,1 % des prix des produits alimentaires et des boissons non alcoolisées, affectant différemment les régions du pays. Par ailleurs, les tensions en mer rouge affectent les recettes douanières de Djibouti, qui ont chuté d'environ 910 millions de francs djiboutiens (0.1% du PIB) au premier trimestre 2024, affectant principalement la taxe sur la valeur ajoutée et les droits d' accises sur les importations de tabac et d'alcool, exacerbant les défis budgétaires déjà accrus par les coûts des subventions pétrolières.

Les perspectives à moyen terme sont positives, avec une croissance annuelle du PIB prévue à 5,1% de 2024 à 2026, soutenue par le commerce extérieur et des projets majeurs de travaux publics. Cependant, l'accumulation continue de la dette publique et les tensions régionales sont des risques qui requièrent une gestion prudente pour garantir la stabilité financière future de Djibouti. Par ailleurs, le modèle de croissance de Djibouti fait face à plusieurs vulnérabilités, notamment une forte dépendance vis-à-vis du transport maritime mondial et une exposition aux conflits régionaux y compris de ses voisins. Pour renforcer la viabilité et l'équité des finances publiques, une attention particulière doit être portée à l'optimisation de l'efficacité fiscale et à la gestion prudente des finances publiques. Cela permettra de soutenir la croissance économique tout en réduisant les vulnérabilités liées aux chocs externes et à la dette.

Le premier chapitre spécial de ce Bulletin de Conjoncture de Djibouti examine les effets

redistributifs du système fiscal du pays, en analysant comment différents impôts et transferts affectent la pauvreté et les inégalités. L'étude inclut des simulations, telles que l'expansion des transferts monétaires, l'augmentation des coûts de stabilisation des prix du kérosène, et une hausse des dépenses publiques de santé. L'analyse révèle que, malgré les efforts de promotion de l'égalité le système exerce une pression à la hausse sur la pauvreté. Les impôts directs s'avèrent progressifs, améliorant l'équité tandis que la TVA, bien qu'elle soit importante pour la mobilisation des recettes, alourdit le fardeau des plus pauvres, compte tenu de sa nature régressive. Le Programme National de Solidarité Famille (PNSF) cible efficacement les ménages à faible revenu, renforçant son caractère progressif. Cependant, les subventions au kérosène, bien qu'importantes, bénéficient principalement aux ménages les plus aisés.

Précisément, alors que ces subventions profitent aux plus pauvres en termes absolus en raison du coût du kérosène qui pèse relativement plus lourd sur leurs budgets, les bénéfices profitent de manière disproportionnée aux ménages les plus riches en termes relatifs en raison de leur consommation plus élevée de kérosène.

Les transferts en nature, tels que les dépenses éducatives et de santé, bien qu'avantageux, n'atteignent pas toujours de manière équitable les plus démunis. La nécessité de réformes fiscales ciblant une redistribution plus équitable et une augmentation des recettes sans aggraver la pauvreté est soulignée, notamment en repensant les subventions au kérosène et en maximisant les bénéfices des programmes sociaux comme le PNSF, qui cible exclusivement les populations pauvres.

En parallèle, une étude de la dépense publique dans le secteur routier—secteur essentiel pour la compétitivité des ports djiboutiens—révèle d'importants défis de financement et de gestion. Une réforme institutionnelle pourrait clarifier les rôles, renforcer l'entretien local et diversifier les sources de financement, améliorant ainsi significativement l'efficacité des dépenses publiques dans ce secteur vital. Le deuxieme chapitre spécial présente les mécanismes actuels de financement du secteur routier et examine ce qu'apporterait une réforme institutionnelle dans le secteur routier à la lumière de l'efficacité budgétaire des investissements dans les infrastructures routières. Cette analyse révèle trois défis principaux : (1) une organisation institutionnelle inefficace avec des chevauchements de responsabilités, (2) un réseau routier mal entretenu et un manque de petites entreprises locales pour l'entretien, ainsi (3) qu'un financement insuffisant et inadapté avec des coûts salariaux élevés. Pour améliorer l'efficacité, il serait utile de clarifier les rôles institutionnels, de développer le secteur local de l'entretien routier et de diversifier les sources de financement, notamment par la création d'un fonds routier et d'une agence routière. Ces réformes nécessitent une forte volonté politique et pourraient significativement transformer le secteur des transports à Djibouti.

الموجز التنفيذي

حقق اقتصاد جيبوتي انتعاشًا مثيرًا للاهتمام في عام 2023، متجاوزًا التوقعات حيث يقدر نمو الناتج المحلي الإجمالي بنسبة 6.7%+. وقد استفادت جيبوتي من انتعاش الطلب المتزايد في إثيوبيا على خدمات الموانئ والخدمات اللوجستية بعد الاستقرار السياسي الذي شهده ذلك البلد. وقد أدى هذا الطلب إلى زيادة حجم البضائع والحاويات التي يتم مناولتها في الموانئ الجيبوتية. فضلا عن ذلك، ظل الطلب المحلي قويا، مدعوما باستئناف الاستثمار الخاص والتدابير الحكومية الرامية إلى تخفيف آثار التضخم الناجمة عن الغزو الروسي لأوكرانيا. وبالإضافة إلى ذلك، لوحظت تحسينات في القطاع الرئيسي، لا سيما بفضل استئناف صادرات الماشية إلى دول الخليج.

وبعد أن بلغ التضخم ذروته عند 11% في يونيو 2022، استقر عند 3.8% في ديسمبر 2023، مع انخفاض التضخم الأساسي. ويعزى هذا الاستقرار جزئيا إلى التدابير الحكومية للحفاظ على القوة الشرائية، مثل حملات التوعية، والرقابة الصارمة على أسعار المنتجات الغذائية الأساسية، والإعفاءات من ضريبة القيمة المضافة لبعض المنتجات. ولم تتغير أسعار الطاقة إلا بشكل بسيط، في حين ارتفعت أسعار المواد الغذائية الطازجة بشكل حاد، ويرجع ذلك جزئيا إلى نقص الواردات من إثيوبيا. وفي المتوسط السنوي، ارتفعت أسعار الاستهلاك بشكل معتدل بنسبة 1.4%، مما يعكس انخفاضا مقارنة بالعام السابق.

وتواجه جيبوتي تحديات تتعلق بالميزانية تتسم بانخفاض هيكلي في الإيرادات، لا سيما بسبب زيادة الإعفاءات الضريبية التي وصلت إلى 19% من الناتج المحلي الإجمالي في عام 2022، مما قلل من الضغوط الضريبية. وانخفضت الإيرادات الضريبية من 13% من الناتج المحلي الإجمالي عام 2019 إلى 11.4% من الناتج المحلي الإجمالي. وفي عام 2023، وعلى الرغم من الزيادة الاسمية في الدخل، ارتفعت الإيرادات الضريبية بشكل طفيف إلى 11.5% من الناتج المحلي الإجمالي بفضل الانتعاش الاقتصادي، ولكن تم تعويضها من خلال انخفاض الإيرادات غير الضريبية. وأدى ارتفاع الإنفاق العام، خاصة في رأس المال، وارتفاع سعر الليبور، إلى عجز في الموازنة بلغ 1.9% من الناتج المحلي الإجمالي، بتمويل من الاقتراض الخارجي. ويؤكد عجز الميزان الأولي، الذي انخفض من –0.7 من الناتج المحلي الإجمالي عام 2022إلى 1.1%- عام 2023، تدهور وضع الموازنة، والذي تفاقم بسبب زيادة مدفوعات الفائدة. ويسلط هذا الوضع الضوء على الحاجة إلى اتخاذ تدابير لزيادة الإيرادات المحلية وتحسين إدارة الإنفاق العام.

ولا يزال وضع الديون مثيرا للقلق على الرغم من أن نسبة الدين إلى الناتج المحلي الإجمالي ستبلغ 67% في عام 2023، وهو ما قد يبدو معتدلا. وبلغ رصيد متأخرات الديون الخارجية نحو 6% من الناتج المحلي الإجمالي في نهاية يونيو 2023، مما يشير إلى قيود التدفق النقدي. ويكشف هذا التراكم، بشكل رئيسي في مواجهة EXIMBANK China وEXIMBANK India، عن توترات حادة في التدفق النقدي. وقد أدى انتهاء مبادرة تعليق خدمة الديون لمجموعة العشرين، واستحقاق قرض خط أنابيب المياه بين جيبوتي وإثيوبيا، والتداعيات الاقتصادية الناجمة عن الحرب الإثيوبية والغزو الروسي لأوكرانيا، إلى تفاقم هذه التوترات. وأعلنت الحكومة الجيبوتية، في 18 أكتوبر 2023، عن توصلها إلى اتفاق مع بنك EXIMBANK الصيني بشأن معالجة ديونه لهذه المؤسسة. وسيتضمن الاتفاق وقفًا اختياريًا لمدة أربع سنوات بدءًا من عام 2024، تدفع خلالها جيبوتي ما يعادل 20٪ فقط من الخدمة المستحقة خلال تلك الفترة وتستمر في المفاوضات مع EXIMBANK China بشأن إعادة هيكلة ديونها. ومع ذلك، للخروج من حالة المديونية المفرطة هذه، سيتعين على جيبوتي سداد متأخراتها الخارجية بالكامل، بما في ذلك تلك المستحقة على بنك EXIMBANK India ونادي باريس. علاوة على ذلك، تظهر نتائج المحاكاة التي أجراها فريق البنك الدولي بشأن استدامة الدين العام لجيبوتي أن العودة إلى مستوى دين يمكن تحمله سيتطلب تجميد الاقتراض غير الميسر، وإعادة هيكلة عميقة لكامل محفظة الديون الخارجية الثنائية لجيبوتي ، فضلا عن تكثيف جهود تعبئة إيرادات الدولة.

وأظهر القطاع المصرفي مرونة في مواجهة الصدمات الخارجية، مع زيادة الائتمان المقدم للقطاع الخاص وانخفاض كبير في القروض المتعثرة. ومع ذلك، انخفضت الاحتياطيات الدولية بنسبة 14.7% مقارنة بالعام السابق. وتحسن ميزان المدفوعات في نهاية عام 2023، مع فائض ملحوظ في الحساب الجاري بنسبة تزيد عن 32%، ويرجع ذلك أساسا إلى

زيادة صادرات السلع والخدمات. وسجل الميزان التجاري فائضاً يقارب 80 مليار جنيه، أي بزيادة قدرها 64,5% خلال سنة واحدة.

تؤدي الاضطرابات المستمرة في البحر الأحمر إلى تأثيرات مختلطة على اقتصاد جيبوتي. تم تعزيز نشاط إعادة الشحن في ميناء جيبوتي، مما أدى إلى زيادة بنسبة 39٪ في حجم الحاويات التي تمت مناولتها في مارس 2024 مقارنة بنوفمبر 2023. وتضاعف حجم الحاويات مقارنة بشهر مارس 2023، حيث وصل إلى 110.000 حاوية مكافئة لعشرين قدم متجاوزًا مستويات ما قبل الجائحة. ويأتي هذا النمو السريع نتيجة لاستراتيجية شركات النقل التي تهدف إلى تقليل المخاطر المرتبطة بعبور البحر الأحمر. وهكذا لجأت تلك الشركات إلى تحويل عمليات إعادة الشحن الخاصة بها إلى جيبوتي ذات الموقع الاستراتيجي جنوب هذه المنطقة، من أجل تجاوز المناطق التي تسيطر عليها جماعة الحوثي. ومن ناحية أخرى، أدت الأزمة إلى ارتفاع كبير في تكاليف الشحن البحري، وهو ما انعكس على أسعار السلع الاستهلاكية في جيبوتي. وفي مارس 2024، وصل معدل التضخم في جيبوتي إلى 5%، وهو أعلى مستوى له منذ ديسمبر 2022، ويرجع ذلك أساسًا إلى ارتفاع أسعار المواد الغذائية والمشروبات غير الكحولية بنسبة 6.1%، مما أثر على مناطق البلاد بشكل مختلف. إضافة إلى ذلك، فإن التوترات في البحر الأحمر تؤثر على إيرادات الجمارك الجيبوتية، التي انخفضت بنحو 910 مليون فرنك جيبوتي (0.1٪ من الناتج المحلي الإجمالي) في الربع الأول من عام 2024، مما أثر بشكل رئيسي على ضريبة القيمة المضافة والرسوم غير المباشرة على واردات التبغ والكحول، مما أدى إلى تفاقم تحديات الميزانية التي زادت بالفعل بسبب التكاليف الناجمة عن دعم النفط.

وتعد التوقعات على المدى المتوسط إيجابية، حيث من المتوقع أن يبلغ نمو الناتج المحلي الإجمالي السنوي 5.1% في الفترة من 2024 إلى 2026، بدعم من التجارة الخارجية ومشاريع الأشغال العامة الكبرى. ورغم ذلك، فإن التراكم المستمر للدين العام والتوترات الإقليمية هي من المخاطر التي تتطلب إدارة حذرة لضمان الاستقرار المالي المستقبلي لجيبوتي. فضلا عن ذلك، يواجه نموذج النمو في جيبوتي العديد من نقاط الضعف، بما في ذلك الاعتماد القوي على النقل البحري العالمي وتأثره بالصراعات الإقليمية، بما في ذلك صراعات الدول المجاورة. ولتعزيز استدامة ومساواة المالية العامة، يجب إيلاء اهتمام خاص لتحسين الكفاءة الضريبية والإدارة الحكيمة للمالية العامة. ومن شأن ذلك أن يدعم النمو الاقتصادي مع الحد من نقاط الضعف المرتبطة بالصدمات الخارجية والديون.

يتناول الفصل الخاص الأول من هذه النشرة الاقتصادية لجيبوتي آثار إعادة التوزيع للنظام الضريبي في البلاد، مع تحليل كيفية تأثير الضرائب والتحويلات المختلفة على الفقر وعدم المساواة. وتتضمن الدراسة عمليات محاكاة، مثل التوسع في التحويلات النقدية، وزيادة تكاليف تثبيت أسعار الكيروسين، وزيادة الإنفاق العام على الصحة. ويكشف التحليل أنه على الرغم من تعزيز المساواة، فإن النظام يمارس ضغوطا تصاعدية على الفقر. واتضح أن الضرائب المباشرة تصاعدية، حيث تعمل على تحسين العدالة في حين أن ضريبة القيمة المضافة، على الرغم من أهميتها في جلب الإيرادات، تزيد العبء على الفئات الأشد فقرا، نظرا لطبيعتها التنازلية. يستهدف البرنامج الوطني للتضامن الأسري بشكل فعال الأسر ذات الدخل المنخفض، مما يعزز طبيعته التقدمية. ومع ذلك، فإن دعم الكيروسين، على الرغم من أهميته، يفيد بشكل رئيسي الأسر الأكثر ثراء. وعلى الرغم من أن التحويلات العينية، مثل الإنفاق على التعليم والصحة، مفيدة، إلا أنها لا تصل دائما إلى أشد الناس فقرا بشكل عادل. وقد تم تسليط الضوء على الحاجة إلى إصلاحات ضريبية تستهدف إعادة توزيع أكثر إنصافا وزيادة الإيرادات دون تفاقم الفقر، وخاصة من خلال إعادة النظر في إعانات دعم الكيروسين وتعظيم فوائد البرامج الاجتماعية مثل الصندوق الوطني للضمان الاجتماعي.

وفي الوقت نفسه، كشفت دراسة للإنفاق العام في قطاع الطرق - وهو قطاع أساسي للقدرة التنافسية للموانئ الجيبوتية - عن تحديات كبيرة في مجالي التمويل والإدارة. ومن الممكن أن يؤدي الإصلاح المؤسسي إلى توضيح الأدوار، ويعزز الصيانة المحلية، وينوع مصادر التمويل، وبالتالي تحسين كفاءة الإنفاق العام في هذا القطاع الحيوي بشكل كبير. ويعرض الفصل الخاص الثاني آليات التمويل الحالية لقطاع الطرق ويبحث ما يمكن أن يحققه الإصلاح المؤسسي في قطاع الطرق في ضوء كفاءة الميزانية للاستثمارات في البنية التحتية للطرق. يكشف هذا التحليل عن ثلاثة تحديات رئيسية: (1) تنظيم مؤسسي غير فعال مع مسؤوليات متداخلة، (2) شبكة طرق سيئة الصيانة والافتقار إلى شركات محلية صغيرة للصيانة، بالإضافة إلى (3) عدم كفاية التمويل وسوء إدارته، مع تكاليف عالية للرواتب. ولتحسين الفعالية، سيكون من المفيد توضيح الأدوار المؤسسية، وتطوير قطاع الصيانة المحلي، وتنويع مصادر التمويل، لا سيما من خلال إنشاء صندوق للطرق ووكالة للطرق. وتتطلب هذه الإصلاحات إرادة سياسية قوية ويمكن أن تحدث تحولا كبيرا في قطاع النقل في جيبوتي.

INTRODUCTION

This edition of the Djibouti Economic Monitor (DEM) is part of a program of biannual reports analyzing Djibouti's development trends and constraints. The aim of each issue is to present the country's recent economic developments (chapter 1), as well as the medium-term economic outlook and the main risks that accompany it (chapter 2). This edition also includes two thematic chapters of interest to the public. The first deals with the redistributive effects and potential efficiency gains of Djibouti's budgetary system (chapter 3). The second deals with the efficiency of public spending in the road sector (chapter 4). The ECB aims to share information and stimulate debate among those interested in and working to improve Djibouti's economic management. It seeks to be accessible to non-specialists to be useful to a wide range of stakeholders.

Djibouti enjoyed rapid economic growth, averaging over 4 percent per year over the period 2000–21, thanks to major investments in transport and port infrastructure. However, this upturn has also been a source of growing vulnerability. This growth, financed by borrowing on increasingly onerous terms, has increased debt vulnerability, limiting budgetary leeway for essential social spending. The COVID-19 pandemic, the conflict in neighboring Ethiopia, and the Russian invasion of Ukraine have exacerbated economic and budgetary tensions through foreign trade, finance, and commodity prices, making debt unsustainable since February 2022.

Djibouti's ambition to leverage its unique geographical position at the entrance to the Red Sea and become a major transport and logistics hub continues to face challenges. Heavy dependence on imports exposes the economy to world price fluctuations and transport disruptions. Moreover, Djibouti's fuel price subsidy is a burden on public finances without effectively reducing poverty. This is all the truer as the fuel subsidy is mainly consumed by wealthier households. Nevertheless, poverty rates are expected to have fallen from their baseline of 19 percent in 2017 to around 14.7 percent in 2024. This reduction is slower than expected, mainly due to factors influenced by COVID-19 and regional instability. Poverty at the lower middle-income poverty line remains high, at around 36 percent, down from 44 percent in 2017.

Ongoing disruptions in the Red Sea are having mixed effects on Djibouti's economy. On the one hand, Djibouti's port activity has increased due to the detour of vessels, particularly for transshipment services, to the point of exceeding its (new) port capacity. On the other hand, escalating sea freight costs and higher insurance premiums due to maritime risks are likely to lead to higher prices for consumer goods, exacerbating Djibouti's vulnerability to these fluctuations. In addition, tensions in the Red Sea have significant fiscal implications, with a potential impact on customs revenues and fuel pricing strategies.

On February 13, 2022, the Government of Djibouti launched the National Development Plan

(NDP) entitled "Djibouti ICI" for the period 2020–2024, to boost growth and exploit the country's full potential. This second five-year plan of Vision 2035 aims to make Djibouti a trade and logistics hub in Africa, and is built around three strategic axes: inclusion, connectivity, and institutions. The first axis of the NDP aims to adopt a more inclusive economic development model to ensure a better distribution of the fruits of growth. The second strategic axis aims to make the country a regional and continental economic hub, and to improve national integration and coverage of socioeconomic services. The third axis of the NDP aims to strengthen the country's human and institutional capacities, while consolidating democracy, public transparency, and social cohesion.

It remains paramount for national authorities to maintain and intensify their efforts to promote growth that is both inclusive and resilient. This will include improving the business environment and governance of public enterprises to attract private investment and reduce the costs of key services to the economy, improving revenue mobilization to restore fiscal sustainability, and rationalizing untargeted subsidies to create space for higher social spending.

1

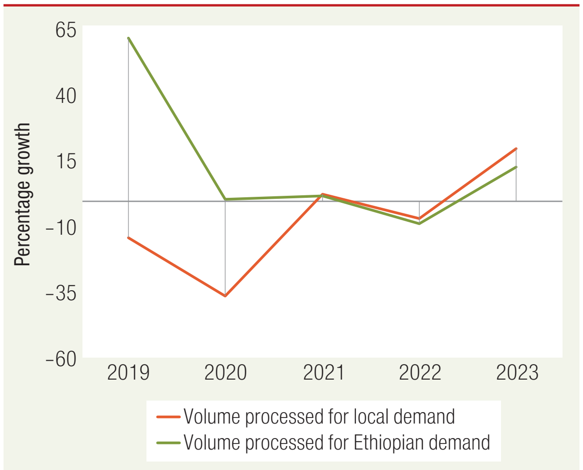
RECENT ECONOMIC DEVELOPMENTS

Real sector: Experienced an upturn in economic activity driven by Ethiopian demand for port and logistics services

Djibouti's economy recorded a remarkable rebound in 2023, exceeding initial growth forecasts. This recovery is largely attributable to the upturn in demand from Ethiopia, Djibouti's main trading partner, for port and logistics services. The gradual normalization of the political and social situation in Ethiopia, following the peace agreement signed in November 2022 between the Ethiopian government and the Tigray rebel movement, was a key factor in this improvement. By the end of December 2023, the total volume of goods handled at Djibouti's ports had increased by around 14 percent compared with the same period in 2022. Ethiopian demand, which accounts for 80 percent of the volume handled, increased by 13 percent, while local demand grew by around 20 percent over the same period (see figure 1). This positive trend is also confirmed by a notable 36 percent increase in the total number of containers handled in Djibouti's ports in 2023, exceeding 890,000 units (see Figure 2). This increase comes after a steady decline in 2021 and 2022 due to the conflict in Ethiopia and the Russian invasion of Ukraine. This rebound has also been made possible by increased productivity at the Doraleh container terminal, following the acquisition in 2022 of four new gantry cranes and the expansion of the terminal. This now enables Doraleh Container Terminal Management Company (SGTD) to operate the latest generation of vessels, with a capacity of over 23,000 Twenty-Foot Equivalent Units (TEU).

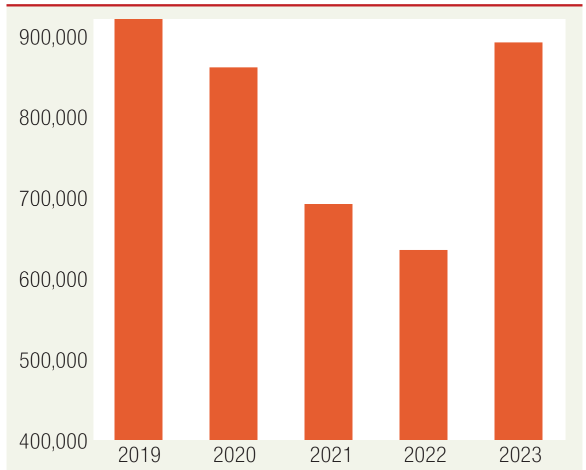
Domestic demand remained robust, stimulated by ongoing public works and construction projects, and their positive impact on the economy as a whole. Production in the "Building-Public Works" sector, estimated through cement sales, doubled in 2023 compared with 2022 (figure 3). This significant increase stems from several factors, including the continuation of construction work on the Damerjog oil port by the Djibouti Ports and Free Zones Authority (APZFD), the resumption of private investment in the tourism and trade sectors after a pause due to the pandemic and the war in Ethiopia, and efforts to renovate road corridors. Government initiatives to promote social housing have also contributed to this growth. Electricity consumption and the number of subscribers also rose by 7 percent and 5 percent respectively over the same period, reflecting Electricity of Djibouti

FIGURE 1 • The volume of goods handled in Djibouti's ports in 2023 increased by around 14 percent compared with 2022



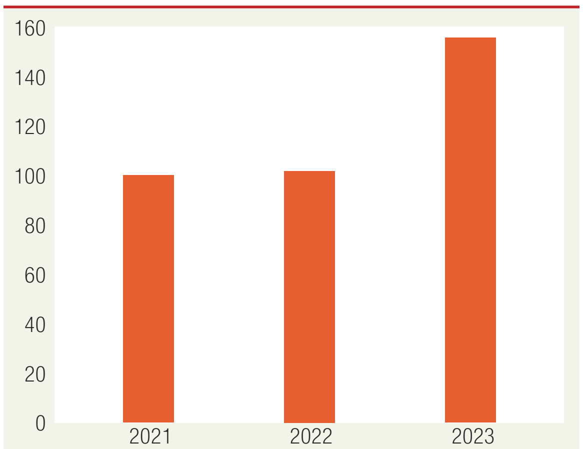
Source: National authorities and team estimates.

FIGURE 2 • The number of containers handled in Djibouti's ports in 2023 exceeded 890,000 units



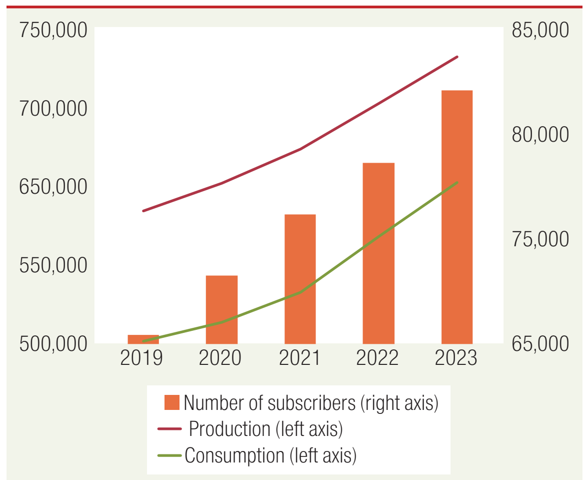
Source: National authorities and team estimates.

FIGURE 3 • Cement sales surge in 2023 as pandemic-induced construction resumes (2021 = 100)



Source: National authorities and team estimates.

FIGURE 4 • Electricity consumption and number of customers up by 7 percent and 5 percent respectively (in thousands of MWH)

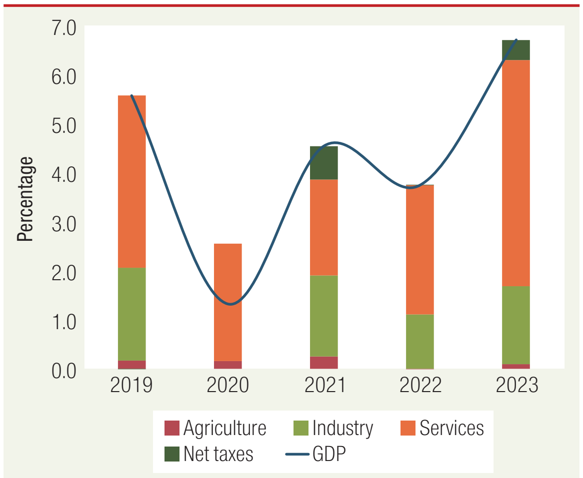


Source: National authorities and team estimates.

(EDD) investments to increase access to electricity services. The continued rise in electricity production and consumption, averaging 5 percent and 6 percent between 2019 and 2023 despite high consumer prices, is the result of several converging factors, including public and private investment in the power grid that has increased electricity generation capacity, and growing urbanization and initiatives to promote rural electrification that have improved access to electricity throughout the country (see figure 4).

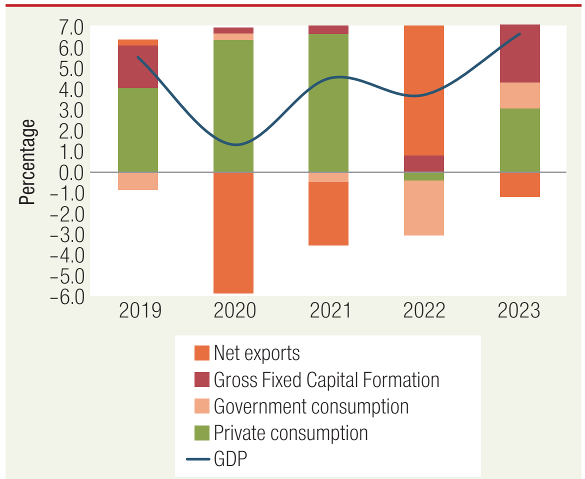
Overall, real GDP growth in 2023 reached 6.7 percent, 3 percentage points up compared to 2022. The service sector remained predominant, contributing 4.6 percentage points to GDP (figure 5). The secondary sector contributed 1.6 points in 2023, up from 1.3 points in 2022. There was also an improvement in the agricultural sector, with a contribution of 0.1 points versus stagnation in 2022. This increase is partly attributable to the resumption of livestock exports to Gulf countries, following the lifting of

FIGURE 5 • The service sector remains the leading contributor to GDP in 2023



Source: National authorities and team estimates.

FIGURE 6 • On the demand side, household consumption is the main contributor to GDP



Source: National authorities and team estimates.

restrictions linked to the COVID-19 pandemic. On the demand side (figure 6), private investment picked up following the resumption of public works and construction projects interrupted during the pandemic, while private consumption was sustained by the continuation of government support measures to counter the inflationary effects of the Russian invasion of Ukraine.

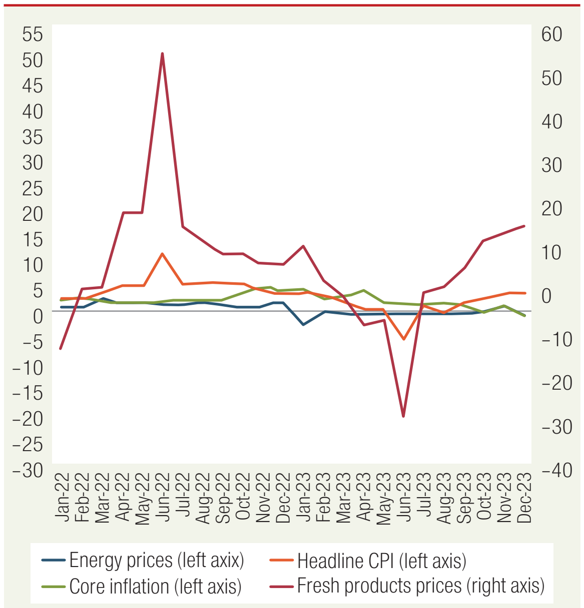
Inflation: A downward trend attributable to the slowdown in world oil and food prices and to government intervention

After peaking at 11 percent in June 2022, inflation stood at 3.8 percent year-on-year in December 2023 (figure 7). Core inflation eased (–0.5 percent in December 2023 versus +4.5 percent for the same period in 2022), partly reflecting the continuation of some of the government measures adopted in 2022 to preserve consumer purchasing power. These include: (i) a campaign to raise awareness among importers, local wholesalers, and retailers; (ii) strict control and monthly publication of approved prices for seven essential food staples (wheat, sugar, cooking oil, flour, rice, milk, and pasta); and (iii) a VAT exemption for the national palm oil refinery. Energy prices were virtually stagnant (–0.2 percent), reflecting the slowdown in international prices, while food products saw their highest rise since June 2022 (almost 15 percent). This sharp rise in fresh produce prices was due to a combination of factors, including periodic shortages of imports from Ethiopia. In addition, to reduce the loss of revenue from taxes and excise duties on petroleum products, the government decided to raise the price of a liter of diesel (+2.5 percent), super diesel (+1.6 percent), and kerosene (+7.7 percent) in July 2023. These prices had been frozen since January 2022, resulting in high tax expenditure (see below). Considering the above trends, the general level of consumer prices rose by a moderate 1.4 percent on an annual average, down 3.7 percentage points on the previous year's level.

Public finances: The budget remains under pressure due to the increase in tax exemptions and the rise in public debt servicing

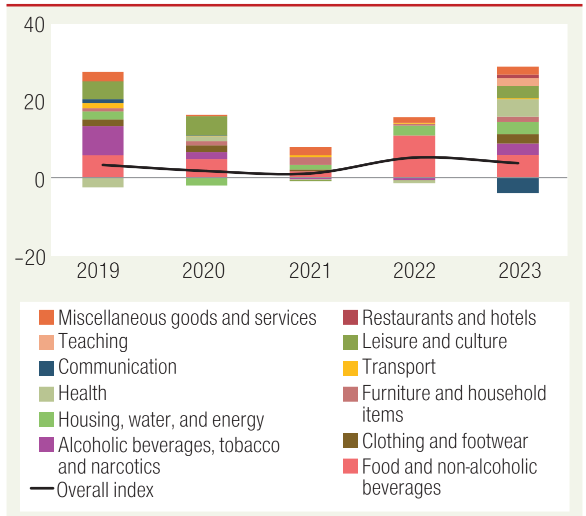
Djibouti continues to face budgetary challenges marked by a downward trend in revenues, mainly attributable to an increase in tax exemptions (table 1). The tax burden declined steadily between 2015 and 2022, from 14.3 percent to 11.4 percent of GDP in 2022, mainly due to the rise in tax exemptions, estimated at 19 percent of GDP in 2022. This decline is a cause for concern, particularly in relation to the African average of 16 percent of GDP and the Sustainable

FIGURE 7 • The fall in inflation that began in August 2022 has continued into 2023 (Annual variation in %)



Source: National authorities and World Bank estimates.

FIGURE 8 • The rise in the consumer price index was driven by food and non-alcoholic beverages (+5.9 percent), housing, water and energy (+2.4 percent) and health services (+4.3 percent)



Source: National authorities and World Bank estimates.

Development Goals (SDGs) target of 15 percent of GDP, and especially in view of the country's unsustainable sovereign debt. By the end of 2023, although revenues had increased nominally by 4 percent on the previous year, they are estimated to have remained stable as a proportion of GDP, at 18.5 percent in 2023. This stagnation is the result of opposing trends in tax and non-tax revenues. Tax revenues enjoyed an increase of 0.2 percentage points of GDP, reaching 11.5 percent of GDP, thanks to the upturn in economic activity mainly resulting from higher indirect taxes, such as VAT, TIC, khat taxes, and taxes on petroleum products. However, this upward trend in tax revenues was offset by a decline in non-tax revenues, due to lower income from securities and military base rents, whose nominal amounts have not increased since 2016. Furthermore, despite receiving exceptional budget support of DF 2 billion (equivalent to USD 11.3 million) from Saudi Arabia, which partially offset the decline in government revenues, grants stabilized at 1 percent of GDP. However, grants have sharply declined from nearly 4 percent of GDP in 2021 following the suspension of COVID-19-related financial aid.

The acceleration in the implementation of NDP-ICI projects and the rise in LIBOR, the main interest rate of Djibouti's bilateral creditors, have led to an increase in public spending, mainly in capital expenditure. To offset this significant rise in capital expenditure, the government renewed measures to reduce current expenditure in the 2023 Finance Act, such as freezing promotions, not filling vacant posts (except for the Ministries of Education, Health, Agriculture, the Interior, and Higher Education), creating a central purchasing unit and launching global tenders for the needs of the administration. However, these measures only partially offset the increase in capital expenditure. As a result, the budget balance based on scheduling recorded a larger variance. For 2023, the overall budget deficit declined to 1.9 percent of GDP, an increase of 0.3 percentage points compared to 2022, mainly financed by new bilateral and multilateral external borrowing.

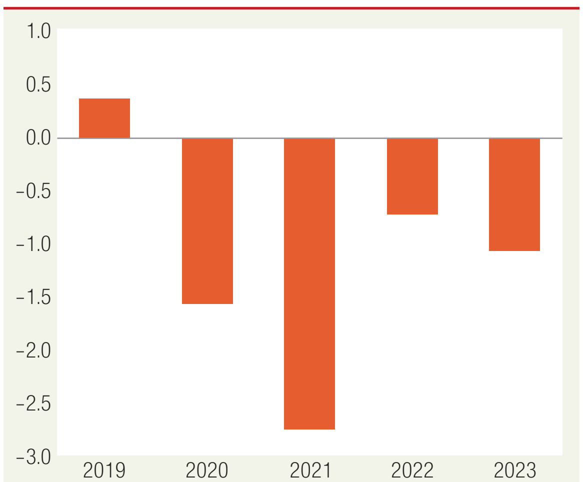
The evolution of the primary balance since 2020 reveals a worsening of debt management challenges. Initially at –1.5 percent of GDP in 2020, this balance has evolved to reach –2.9 percent of GDP in 2021, before compressing to –1.9 percent in 2023 (figure 9). This trend shows that the government is finding it difficult to rebalance the budget balance independently of debt interest payments, which remain

TABLE 1 • Djibouti faces budgetary challenges marked by a downward trend in revenues, mainly attributable to an increase in tax exemptions

	2019	2020	2021	2022	2023
Overall budget balance	−0.9	−1.7	−2.9	−1.4	−1.9
Primary balance	0.4	−1.6	−2.7	−0.7	−1.1
Total revenues and donations	23.5	23.4	20.0	18.9	18.9
Tax revenues	13.0	11.6	11.5	11.3	11.5
Non-tax revenues	6.9	8.2	6.7	6.5	6.4
Donations	3.6	3.6	1.8	1.0	1.0
Total expenditure	24.4	25.2	22.9	20.3	20.8
Current expenses	16.0	14.6	14.2	15.3	14.7
Wages and salaries	6.5	6.3	6.2	5.8	5.7
Goods and services	5.6	5.6	5.3	5.7	5.3
Interest payments	1.3	0.2	0.2	0.7	0.8
Current transfers	2.6	2.6	2.5	3.1	2.9
Capital expenditure	7.7	7.1	7.1	5.1	6.1
Financing	0. 9	1.7	2.9	1.4	1.9
Exterior (Net)	1.5	1.4	1.8	1.1	1.1
Domestic (Net)	−0.6	0.3	1.1	0.3	0.8

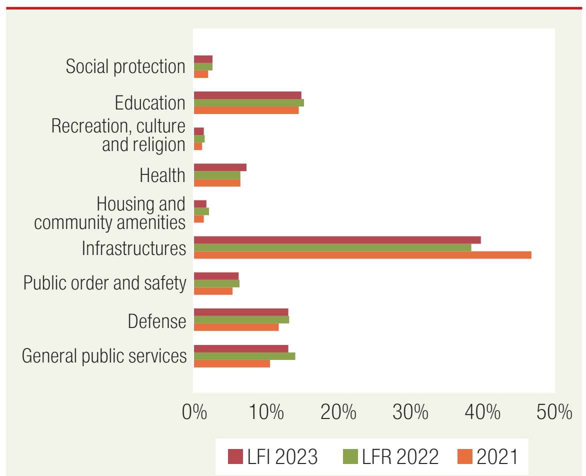
Source: National authorities and World Bank estimates.

FIGURE 9 • The primary budget balance has deteriorated since 2020, requiring immediate action to restore financial equilibrium



Source: National authorities and team estimates.

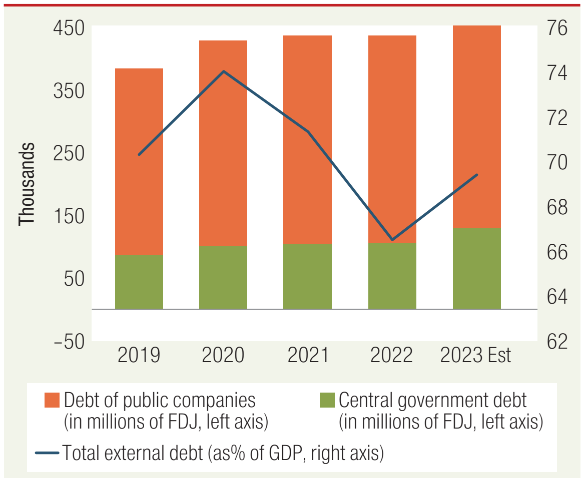
FIGURE 10 • 40 percent of budget spending is allocated to infrastructure, reflecting the priority given to this sector in the State budget



Source: 2021 Original Finance Law and 2022 and 2023 Amended Finance Law.

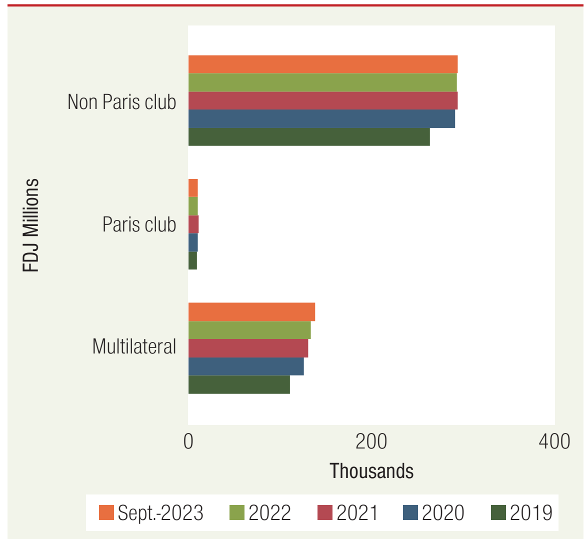
a major challenge. When interest payments are added to the equation, the budget deficit widens even further in 2023, as previously mentioned. In addition, the ratio of interest payments to revenues, a key indicator of a country's ability to service its debt, remains high for the Djibouti economy in 2023, reaching 5 percent. Although

FIGURE 11 • The stock of foreign debt will continue to grow in 2023, with state-guaranteed debt of public enterprises accounting for 76 percent of the total



Source: National authorities and authors' estimates.

FIGURE 12 • The bulk of non-Paris Club bilateral and multilateral debt



Source: National authorities and authors' estimates.

relatively low, this represents a five-fold increase on the 2020 ratio. This significant increase underscores the need to take significant measures to reduce the budget deficit, mainly through an increase in domestic revenues, moderate recourse to non-concessional debt, and more effective management of public expenditure to stabilize the country's financial situation.

Sectoral allocations of the state budget show that priority is given to infrastructure spending, with around 40 percent of budget expenditure. Education is the second largest item of state expenditure, accounting for 15 percent of the total. General public services and defense allocations are estimated at 13–14 percent of budget expenditure. Health care spending will peak at 7 percent of public spending in 2023, while security spending will rise to 6 percent of total spending. Social protection receives a budget allocation of 3 percent of total government expenditure (figure 10).

Public debt: The level of external public debt is increasing following the subscription of new non-concessional loans in March and July 2023.

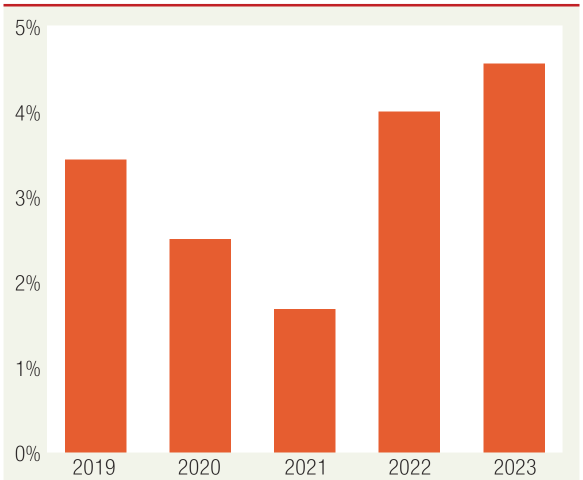
Official data indicate an increase in outstanding public debt, reaching USD 2,745.9 million at the end of December 2023[2], equivalent to 67 percent of nominal GDP forecast for 2023[3]. Djibouti's outstanding public external debt increased significantly in 2023 due to the disbursement of three new loans contracted this year, as well as the integration of arrears accumulated in 2022, which could raise the public external debt ratio to at least 67 percent of GDP. Borrowings in 2023 include financing for the shipyard project (USD 92.2 million), the Damerjog oil pipeline (USD 155 million) and the Doraleh desalination plant (EUR 91.9 million).

Debt to public enterprises accounts for around 76 percent of public external debt (figure 11). The composition of public external debt by beneficiary shows that 76 percent of public debt is made up of state-guaranteed loans to large public enterprises working on regional infrastructure projects. The main public-sector creditors are: Djiboutian Railway Company—SDCF—(25 percent), The Djibouti National Office for Water and Sanitation—ONEAD—(21 percent), Djibouti Ports and Free Zones Authority

2 Bulletin Statistique de la Dette Publique -quatrième 2023, Direction de la Dette Publique.

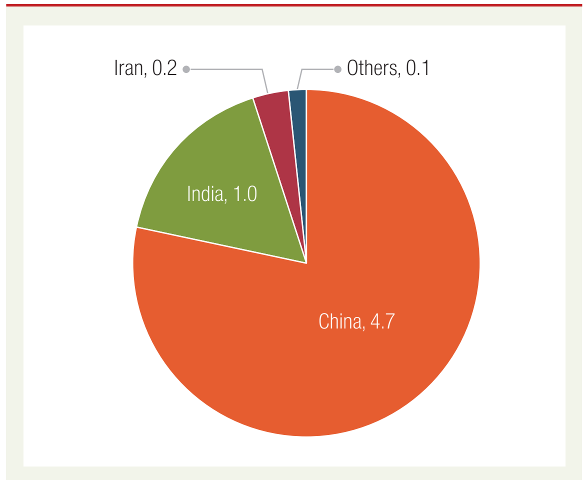
3 According to World Bank GDP estimates, public debt represented 66.9 percent of GDP, while national authorities put it at 68 percent of GDP.

FIGURE 13 • Debt service doubled in 2022 following the end of the G20 Initiative and the maturity of the Djibouti-Ethiopia water pipeline loan



Source: Authors' calculations based on data from the Bulletin Public Debt Statistics for the fourth quarter of 2023.

FIGURE 14 • The stock of arrears on external debt, mainly with EXIMBANK CHINA and EXIMBANK INDIA, reached 6 percent of GDP at the end of September 2023



Source: Authors' calculations based on data from Economic of Outlook Note of the fourth quarter of 2023 from the Ministry of Finance (MEFI).

(APZFD) and Djibouti Port Corridor Roads SA (APZF 32.6 percent + DPCR 10.8 percent of the total). External borrowings were mainly directed toward the infrastructure sector (76 percent), in line with the government's 2035 vision of transforming the country into a commercial, logistics, and financial hub for the Horn of Africa region.

Most of Djibouti's external public debt is held by bilateral creditors who are not members of the Paris Club (Figure 12). In September 2023, these non-member countries accounted for around 69 percent of total external debt, while multilateral partners held 31 percent (figure 12). Non-Paris Club members include major players such as China, India, and Iran. China has become the largest lender, accounting for almost 50 percent of total external debt, mainly through commercial loans from the State Export-Import Bank of China (EXIMBANK China). Key multilateral lenders include the World Bank (10 percent), the Arab Fund for Economic and Social Development-FADES- (8 percent), the African Development Bank-AfDB- (5 percent), and the Islamic Development Bank-IDB- (5 percent).

The breakdown of public external debt by currency indicates a low foreign exchange risk, due to the predominance of US dollar-denominated debt in the portfolio (68 percent of total debt) and the fixed parity between the Djibouti franc and the US dollar. Currency risk is further reduced by the fact that a significant proportion of the loan portfolio is denominated in currencies correlated to the US dollar, such as the Saudi Riyal (SAR) and the Emirati Dirham (AED). Other currencies account for a more modest share, notably the Kuwaiti Dinar (5 percent), the Euro (8 percent), and the Yuan (4 percent).

Public debt servicing, estimated at 4.6 percent of GDP in 2023, had doubled by 2022 with the end of the G-20 Debt Service Suspension Initiative (DSSI) and the maturity of the EXIMBANK China loan for the Djibouti-Ethiopia water pipeline (figure 13). In addition to the freeze on public debt servicing under the DSSI, Djibouti had benefited from IMF debt relief thanks to the Disaster Assistance and Response Trust Fund designed to help the country cope with the COVID-19 pandemic. These reliefs had reduced public debt servicing from 3.4 percent of GDP in 2019 to 1.7 percent of GDP in 2021. In addition, the IMF's disbursement of USD 43.4 million under the Rapid Credit Facility, as well as an ADB grant of USD 41.16 million to Djibouti to mitigate the impacts of the COVID-19 pandemic, had helped address cash flow pressures resulting from the depressive economic impact of the pandemic on public finances.

The end of international pandemic aid, combined with the loan maturity for the Ethiopia-Djibouti water pipeline and the effects of the war in Ethiopia and the Russian invasion of Ukraine, has led to cash flow tensions. These tensions have resulted in an accumulation of external debt arrears, which reached approximately USD 211 million by the end of September 2023, equivalent to around 6 percent of the projected GDP for 2023[3] (figure 14). The arrears were accumulated mainly vis-à-vis EXIMBANK China (around USD 162.4 million) and EXIMBANK India (around USD 34.3 million). On October 18, 2023[4], the Government of Djibouti announced an agreement with EXIMBANK China that included a four-year moratorium starting in 2024, during which Djibouti would pay only the equivalent of 20 percent of the service due during this period. The government will continue negotiations with EXIMBANK China on restructuring the debt.

The results of simulations carried out by the World Bank team on the sustainability of Djibouti's public debt (Box 1), show that a return to a sustainable level of debt would require a freeze on non-concessional borrowing, a thorough restructuring of Djibouti's entire bilateral external debt portfolio, as well as an intensification of efforts to mobilize state revenues to return to pre-COVID-19 levels of tax pressure.

Monetary sector: Currency board coverage remains adequate despite a significant drop in gross reserves following the cessation of pandemic-related international aid.

Djibouti's monetary system is distinguished by its currency board arrangement, which is characterized by its longevity and stability. Set up on March 20, 1949, this specific system, with a fixed parity between the national currency and the US dollar, has enabled the country to contain inflationary pressures and build the confidence of international investors. However, the currency board system does

4 Note de conjoncture économique du troisième trimestre 2023-DEP (MEFI), August 2023.

5 https://x.com/Ilyasdawaleh/status/1714501926681973083.
https://www.adi.dj/index.php/site/Plus/11353#:~:text=Dileita%20de%20la%20d%C3%A9cision%20de,are%20in%20course%20of%C3%A9study.

BOX 1: SIMULATIONS OF DJIBOUTI'S EXTERNAL DEBT SUSTAINABILITY

The aim of this exercise is to simulate the conditions under which Djibouti's debt overhang situation could improve, during which the external debt sustainability analysis indicators would not exceed their respective critical thresholds. The reference scenario for this exercise is the public debt sustainability analysis (February 2023), whose debt burden indicators revealed that the country was in debt distress.

A scenario based on the preliminary agreement reached with China in October 2023, which considers a 4-year moratorium starting in 2024, during which Djibouti would pay only 20 percent of the debt service due to EXIMBANK China has been considered . In the absence of details on the terms of the debt restructuring for the railway and water pipeline projects that would take place at the end of the 4-year moratorium, this scenario assumes that Djibouti could benefit from favorable terms similar to those obtained by some countries under the G20 common framework for debt treatment of low-income countries. These conditions include an average interest rate of 1 percent, an average grace period of 5 years, and a maturity of 25 years.

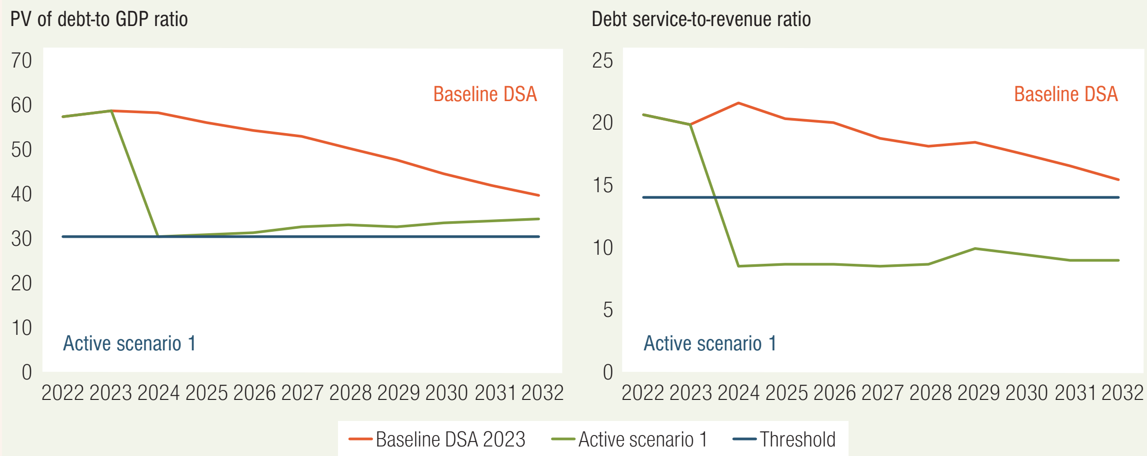
The results of the simulations show that under that scenario , the risk of debt distress would remain high (Figure 1.1). In this scenario, the country's tax revenues would be able to cover debt servicing over the projection period (2024–2042). Indeed, although the net present value of external debt would improve compared to the baseline scenario, with the ratio of net present value of debt to GDP falling from 57.3 percent in 2022 to 30.0 percent in 2024 and 2025, it would return above the critical threshold from 2026 until the end of the projection period. The other two indicators in the analysis of external debt sustainability show trends below their respective thresholds.

Simulation results show the scale of the debt overhang challenge facing Djibouti. It emerges that despite initial improvements, Djibouti would remain at high risk of debt distress. It appears that a return to a sustainable level of public debt would require a freeze on non-concessional borrowing, a thorough restructuring of Djibouti's entire bilateral external debt portfolio, and an intensification of resource mobilization efforts to regain, at the very least, the levels of fiscal pressure seen prior to the COVID-19 pandemic.

(continued on next page)

BOX 1: SIMULATIONS OF DJIBOUTI'S EXTERNAL DEBT SUSTAINABILITY *(continued)*

FIGURE 1.1 • Indicators of External Public and publicly guaranteed debt under scenario 1, 2022-2032

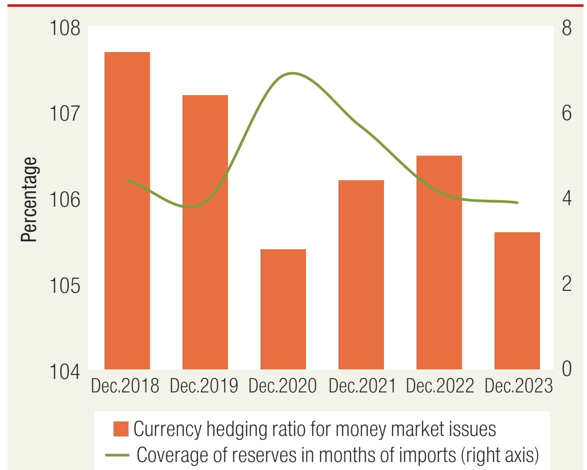


Source: World Bank, DSA framework, World Bank staff calculations.

not allow the Central Bank of Djibouti to pursue an active monetary policy and act as lender of last resort. Its main tasks are to ensure that foreign exchange reserves cover 100 percent of the banknote issue, to monitor banks' liquidity risks, and to strengthen their control and management of these risks. The level of the country's official reserves, which are almost entirely held in US dollars, is largely determined by capital movements and rental income from foreign military bases in Djibouti.

The currency board coverage is robust despite declines in money supply and international reserves (figure 15). Money supply growth was mainly driven by the increase in time deposits and, to a lesser extent, sight deposits, reflecting the rebound in growth observed in 2023. The monetary authorities' gross foreign assets fell by 14.7 percent at end-December 2023 compared with end-December 2022, to almost USD 496 million. Currency board coverage remained above 105 percent, which is above the required minimum threshold of 100 percent. International reserves, which had been rising sharply since 2020 thanks to financial support from the IMF and the AfDB, have been falling steadily since the beginning of 2023, reflecting the country's current cash flow problems. With the upturn in growth in 2023,

FIGURE 15 • Currency board coverage remains at an adequate level, although official reserves have continued to fall since the end of 2022

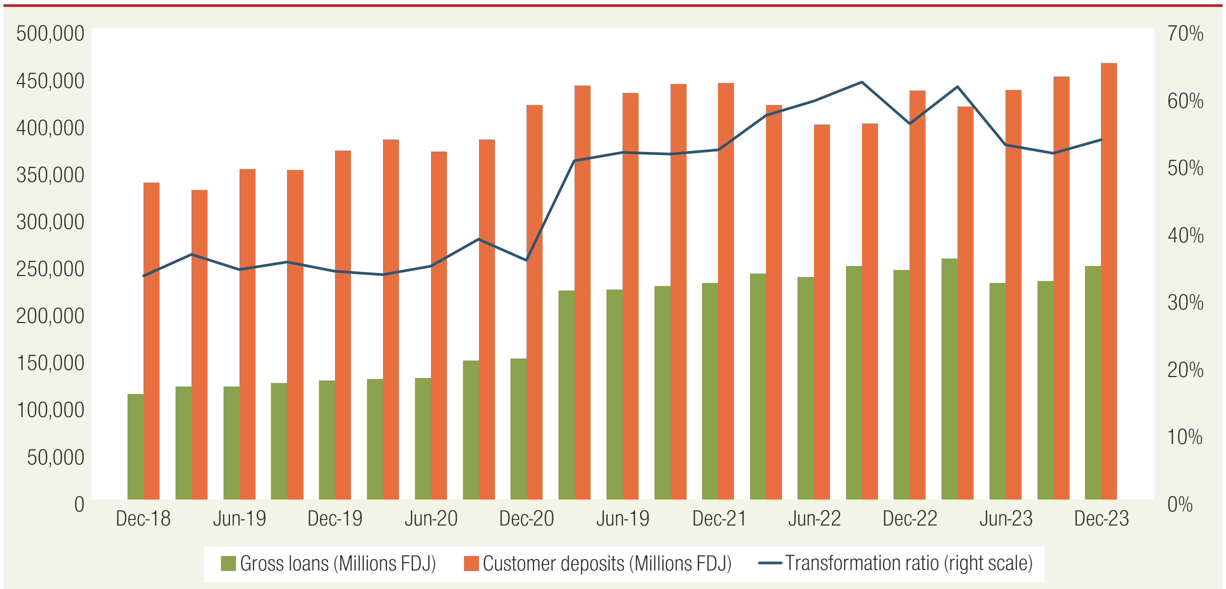


Source: Central Bank of Djibouti and World Bank team estimates.

credit to the private sector was 20.4 percent higher at the end of 2023 than at the end of 2022, while claims on the central government jumped 103.1 percent over the same period.

There has been a significant increase in bank deposits and loans in 2023, with a strong

FIGURE 16 • The decline in the loan-to-deposit ratio between December 2022 and December 2023 reflects customers' growing preference for term accounts



Source: Central Bank of Djibouti and World Bank team estimates.

preference for term accounts. The transformation ratio of loans to bank deposits fell from 56 percent to 53.6 percent between December 2022 and December 2023 (figure 17) due to a significant increase in deposits, particularly in term accounts, reflecting a growing customer preference for these savings instruments. This preference may be motivated by the attractive interest rates offered on term accounts, encouraging customers to invest more funds over the long term, thereby reducing the availability of immediate funds for bank lending.

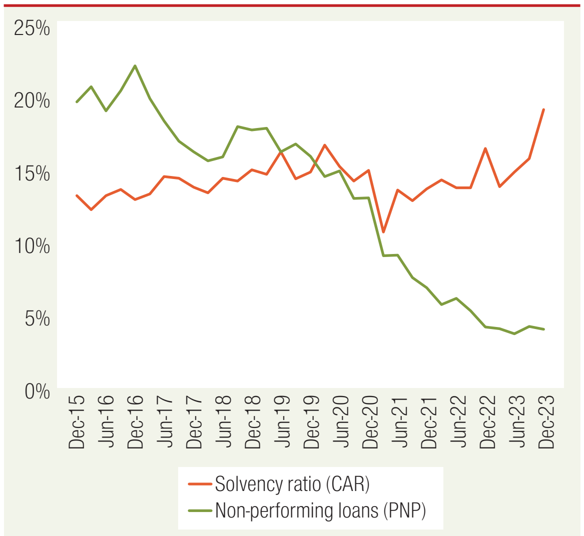
Overall, the banking sector remains stable and resilient to the multiple exogenous shocks that have affected the Djiboutian economy in recent years. The solvency ratio of the Djiboutian banking system has maintained a position well above the minimum regulatory threshold of 12 percent, indicating solid financial stability despite the recent economic shocks (figure 17). However, bank profitability declined, with the return on assets (ROA) ratio falling from 1.67 percent to 1.43 percent between December 2022 and December 2023. Similarly, the return on equity (ROE) ratio increased temporarily to 22.02 percent in September 2023, before falling back to 19.15 percent in December 2023. This decline in profitability can be attributed to a combination of factors, including lower interest margins on banking products due to high international interest rates, as well as the general deterioration in banks' financial performance.

The liquidity level of Djibouti's banks remains relatively high, and the rate of non-performing loans in the banking sector continues to fall. The banking sector's consolidated non-performing loans (NPLs) have continued to fall, from 22.4 percent of total credit distributed in December 2016 to just 4.2 percent in December 2023 (figure 18). This significant reduction can be attributed to the banks' efforts to clean up their loan portfolios, with the provisioning rate for NPLs falling steadily to 72.7 percent in December 2023. The decrease in the stock of provisions on past-due loans, accompanied by a fall in consolidated NPLs, reflects a steady improvement in the quality of Djibouti banks' assets and reinforces their long-term financial stability.

External sector: The balance of payments current account improved by the end of 2023 due to the recovery in Ethiopian demand.

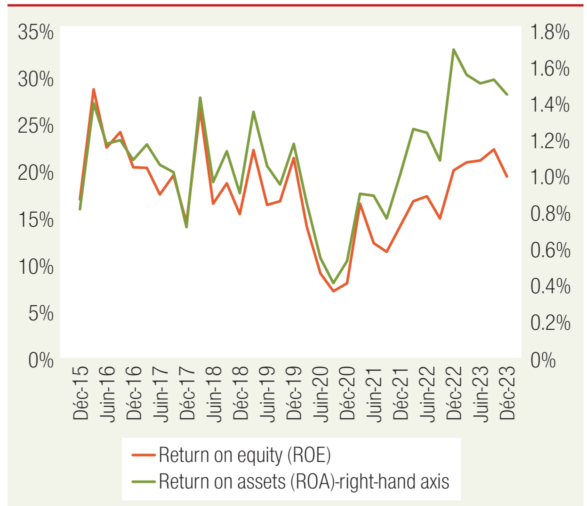
Djibouti's balance of payments showed a marked improvement at the end of December 2023, mainly thanks to an acceleration in exports of goods and

FIGURE 17 • The banking system remains solvent…



Source: Central Bank of Djibouti and team estimates.

FIGURE 18 • ... but its profitability has declined partly due to pressure on interest margins



Source: Central Bank of Djibouti and team estimates.

services, according to 2023 estimates. The current account balance increased by over 32 percent in one year, boosted by notable improvements in both the trade and services balances (figure 19).

In particular, the trade balance, which has been in surplus since 2021 has consolidated, achieving an impressive positive balance of almost DF 80 billion by the end of 2023 marking a year-on-year increase of 64.5 percent. This significant increase in the trade surplus was mainly due to export growth outstripping import growth. This dynamic was largely attributable to the economic recovery in Ethiopia, with annual export growth of 9.6 percent, dominated by reexports of livestock and Ethiopian products. Imports, meanwhile, rose by a moderate 6 percent. The services balance had also seen an annual rise of 7.8 percent by the end of 2023, supported by an increase in service exports, notably in the shipping sector, which had grown by over 6 percent annually. However, the primary income deficit in the balance of payments deteriorated slightly by 2.2 percent between December 2022 and December 2023, while current transfers to the general government increased by 8.7 percent.

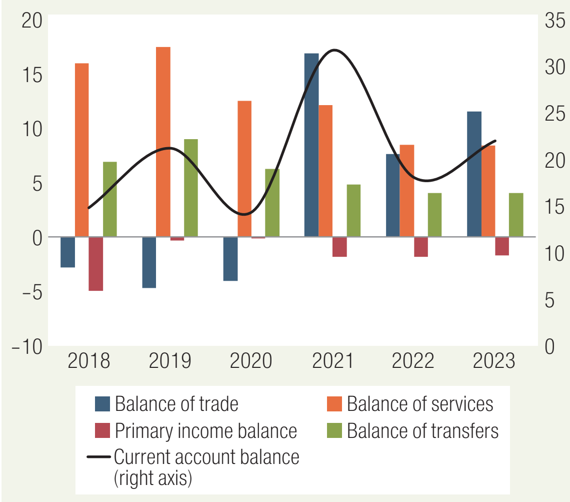
Despite a significant decline since 2021, the capital account surplus is estimated to have consolidated in 2023, supported by an increase in international financing. On the other hand, the balance of financial operations declined slightly over the last 12 months. After a sharp fall in 2022, support from international partners more than doubled in 2023, with a particular surge in foreign direct investment and long-term loans, which recorded an annual growth of 10 percent. Other investments, however, fell by over 57 percent between the end of 2022 and the end of 2023. In addition, the official reserve assets of the Central Bank of Djibouti fell by over DF 26.8 billion by December 2023, after a modest gain of DF 479 million in 2022 (figure 20).

Labor market: Djibouti's economic growth has not been accompanied by a significant reduction in poverty and unemployment.

Despite strong economic growth prior to recent shocks, there has been no significant improvement in Djibouti's labor market. The Djibouti Economic Memorandum, recently produced by the World Bank[4], highlights the persistent challenges

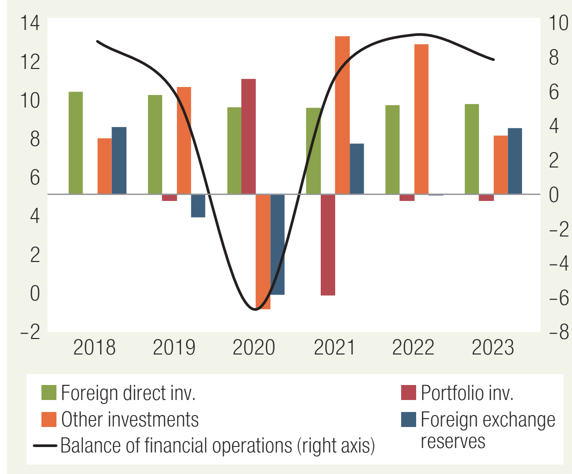
6 https://documents1.worldbank.org/curated/en/099013124082525843/pdf/P17794913d0f7c0d319c7d125f26432112d.pdf.

FIGURE 19 • Current account improved in 2023



Source: Central Bank of Djibouti and World Bank team estimates.

FIGURE 20 • Falling reserve levels in 2023

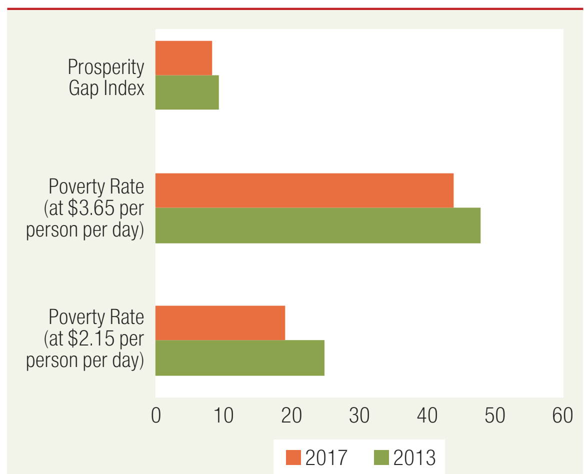


Source: Central Bank of Djibouti and World Bank team estimates.

associated with job creation despite strong economic growth. These concerns are particularly pronounced in a context where the labor force participation rate remains alarmingly low, with 40 percent of people of working age neither employed nor actively seeking work, or enrolled in an educational institution. In addition, unemployment remains high, affecting around half of the working population, 60 percent of whom are discouraged workers. These findings underline the urgent need for Djibouti to meet the challenge of creating sufficient employment opportunities for its growing workforce, particularly for young people, women, and people living outside Djibouti city. Djibouti's precarious labor market situation stems from several factors. First, the underdeveloped private sector is a major obstacle, as it limits employment opportunities in a context where capital-intensive sectors dominate the economy. In addition, the challenges of an expanding working-age population combined with persistent public health problems such as malaria and low life expectancy, hamper the country's economic potential by limiting the availability of skilled workers. Furthermore, despite some progress in access to education, enrolment rates in secondary education remain low, and the quality of education is insufficient to adequately prepare the workforce for the demands of the modern labor market. Finally, mismatches between labor supply and demand, characterized by a demand for skilled workers and an oversupply of low-skilled workers, contribute to keeping unemployment at high levels. These factors combine to fuel Djibouti's persistent labor market challenges and underscore the need for targeted policy action to stimulate job creation and improve economic prospects for the population as a whole.

Djibouti also continues to face high levels of poverty and inequality. According to international poverty lines, 19 percent of Djibouti's population lives

FIGURE 21 • Despite a downward trend, the poverty rate remains high after a decade of reduction



Source: Poverty and Inequality Platform, World Bank (2024).

below the poverty line for low-income countries ($2.15 per person per day) and 44 percent below the poverty line for lower-middle-income countries ($3.65 per person per day) (figure 21). A new prosperity gap index, developed by the World Bank, shows that this gap, although reduced over the last decade, remains substantial. This index measures the financial distance separating individuals from a prosperity threshold set at US $25 dollar per person per day, weighing particularly heavily on the poorest. In 2019, this gap was estimated at 8.06 for Djibouti, meaning that people's incomes would have to be multiplied by 8 to reach this prosperity threshold, an improvement on a decade earlier, when the gap stood at 9.33.

2

MEDIUM-TERM OUTLOOK

Real sector: Trade and public works will remain the main growth drivers in the medium term

Djibouti's economic outlook remains promising despite regional uncertainties, including proximity to conflict-ridden neighbors, unforeseen inflationary pressures, and a possible slowdown in consumption. The Ethiopian Prime Minister's visit to Lamu, Kenya, in February 2024 to sign a memorandum of understanding for direct access to the sea underlines this dynamic[7].

In the medium term, Djibouti's GDP should grow solidly at 5.1 percent annually between 2024 and 2026, driven by foreign trade and public works (Table 2). Djibouti will continue to benefit from its strategic position and world-class port complex which has been strengthened over the past three decades. Although forecast to slow slightly in the medium term compared with 2023, Ethiopia's economic growth is expected to remain high, averaging 7 percent between 2024 and 2026[8]. This pace of growth should be sufficient to support sustained and growing demand for Ethiopia's transport and logistics services.

Domestically, fixed capital investment is stimulated by major infrastructure projects. These include the development of the Damerjog industrial park, the construction of a new fuel storage terminal and oil jetty, the extension of the Ghoubet onshore wind farm to boost electricity production, and the completion of the third phase of the Ali Sabieh cement plant. These projects will support economic activity in the medium term and boost domestic production capacity. Although these projects will support economic activity in the medium term and enhance domestic production capacity, growth is expected to remain below Djibouti's potential. To optimize growth, Djibouti must address the constraints highlighted in the World Bank's Country Economic Memorandum published in February 2024. These include the high costs of basic services such as electricity and telecommunications, which pose significant barriers

7 https://www.theeastafrican.co.ke/tea/news/east-africa/abiy-ahmed-visit-kenya-improved-ties-addis-ababa-nairobi-4537244.

8 https://thedocs.worldbank.org/en/doc/bae48ff2fefc5a869546775b3f010735-0500062021/related/mpo-eth.pdf.

to private sector development. Other identified constraints in the CEM involve limited human capital, characterized by low secondary school enrollment rates, particularly among girls, and poor-quality education, resulting in a mismatched labor market with an oversupply of low-skilled workers and a shortage of skilled labor. Furthermore, the substantial presence of state-owned enterprises, crucial for growth, presents challenges such as monopolistic practices, high debt levels, and governance issues, which hinder the competitiveness and economic efficiency of the private sector.

Public finances: despite the Government's ongoing adjustment efforts, additional measures will be needed to ensure the sustainability of public finances.

Tax revenues and total government revenues are expected to remain stable in 2024–2025, representing 11.7 percent and 18.9 percent of GDP, respectively. This nevertheless represents a decrease of 1.3 percentage points and 4.6 percentage points compared with pre-pandemic levels. This stability is underpinned by targeted tax reforms, including the reintroduction of the quarterly instalment payment system and the introduction of new surcharges on certain luxury goods. These measures are designed to offset revenue losses due to previous tax exemptions and to mobilize additional revenue. This underlines the continuing importance of reform efforts to improve tax oversight and debt collection.

On the expenditure side, the budget calls for a freeze on promotions and reclassifications, except in priority social sectors. Total expenditure should stabilize at 20.2 percent of GDP. Efforts also include the centralization of public procurement and a strict reprioritization of capital expenditure, leading to better resource management and a reduction in non-priority spending.

The budget deficit is set to contract slightly, reaching 1.3 percent of GDP in 2024 and 1.4 percent in 2025. This deficit will be financed by concessional borrowing from multilateral and bilateral lenders, as well as a four-year moratorium on loans from EXIMBANK China. This financing strategy reflects a prudent approach, aimed at minimizing financing costs while ensuring the sustainable development of essential infrastructures, such as those connecting Djibouti to Ethiopia.

Nevertheless, the fiscal consolidation efforts initiated by the Government of Djibouti since 2022 are a positive step, but further measures are necessary to ensure the sustainability of public finances. According to the debt sustainability analysis, significant efforts will be required in the medium and long term to increase revenue mobilization, enhance the efficiency of public spending, and undertake a comprehensive restructuring of public debt.

External sector: The current account balance is set to further deteriorate slightly due to increased imports of hydrocarbons and materials for infrastructure projects.

Between 2024 and 2025, a slight deterioration in the current account balance is forecast. This is mainly due to an increase in imports of hydrocarbons and equipment required for infrastructure projects. This rise could also be encouraged by increased demand for logistics and transport services from Ethiopia, which would boost re-export activity in the free trade zones and boost exports of services such as transport, logistics and telecommunications. A return to stability in Ethiopia and a recovery in household consumption and investment would also boost GDP growth and capital goods imports via Djibouti's ports.

The capital account position should improve between 2024 and 2025. On the other hand, the financial transactions account could contract during this period. Current negotiations on capital transfers, including debt cancellations, should play a positive role for the capital account in the medium term. At the same time, the financial account is expected to shrink during 2024–2025, due to a decline in foreign direct investment and a slowdown in other forms of investment, attributable to persistent uncertainties in the region.

Risks: The medium-term economic outlook faces risks such as fiscal deterioration, regional tensions, climate shocks, and worsening conflict in the Middle East.

Djibouti's medium-term economic outlook, while promising some positive developments, remains subject to several significant risks that could compromise the country's stability and growth. These risks include public debt accumulation and fiscal vulnerabilities; regional instability and climate impacts; and risks linked to relations with Ethiopia and conflicts in the Middle East. Djibouti's fiscal situation gives cause for concern due to the continued accumulation of public debt and the extension of tax exemptions, which could limit the government's ability to respond effectively to future shocks and finance essential public services such as education and public health. This trend is likely to lead to a deterioration in human development and an increase in inequalities in the country.

Regional tensions continue to represent a major risk, exacerbated by the impacts of climate change, notably droughts and floods. These conditions can affect the primary and secondary sectors, as well as disrupt trade and logistics, particularly with Ethiopia, a key trading partner.

Economic conditions in Ethiopia, including constraints on trade and transport activities, have a direct impact on Djibouti's economy. A slowdown in Ethiopia could reduce road and rail traffic, thus affecting the supply of water and fresh produce, and increasing budgetary tensions due to humanitarian and security expenses linked to migratory movements.

Escalating conflicts, particularly between Israel and Hamas, could degenerate into a wider regional conflict, with potential negative repercussions for Djibouti, particularly in terms of import costs. Djibouti relies heavily on imports of agricultural products, processed foods, and fuels. Any disruption to commodity markets could therefore have severe economic consequences for the country.

These factors require careful monitoring and management by Djibouti's decision makers to navigate through these uncertainties and secure a more stable economic future for the country (Box 2).

BOX 2: ECONOMIC IMPACT OF THE RED SEA CRISIS IN DJIBOUTI

Regional political and geopolitical context. Djibouti, strategically located at the entrance to the Bab el-Mandeb Strait, plays a crucial role in ensuring the security of this vital maritime trade route. Faced with escalating threats to maritime security in the region, including attacks on commercial vessels by the Houthis since November 2023, Djibouti has stepped up its coastal security measures. Recent reports from the Djibouti Coast Guard confirm the intensification of patrols and the strengthening of cooperation with international maritime security forces. This proactive attitude reflects Djibouti's commitment to safeguarding regional stability and protecting vital maritime routes.

Ongoing disruptions in the Red Sea have boosted transshipment activity in Djibouti's ports. As a result of these tensions, Maersk, one of the two main shipping operators serving the port, suspended its routes through the area. At the same time, MSC, the second major shipping line operating in Djibouti, has ceased direct sailings through the Red Sea, but continues to use the port as one of its main transshipment hubs. This situation has also prompted other companies to step up their operations in the port. It is important to note that around 80 percent of shipping to and from Djibouti comes from China and India. The volume of containers handled at the Djibouti container terminal, which had already seen a spectacular 41 percent increase in 2023 compared with 2022, continued to grow in the first quarter of 2024. In March 2024, container volume rose by 39 percent compared with November 2023, a month marked by the start of the Houthi movement's attacks on ships in the Red Sea. This volume now exceeds the levels recorded prior to the COVID-19 pandemic (see figure 2.1). Compared with March 2023, container volume more than doubled, reaching 110,000 TEU. This increase is mainly attributable to growth in transshipment activity, which rose by 35 percent between November 2023 and January 2024. This rapid growth is the result of a strategy by carriers to minimize the risks associated with crossing the Red Sea. They have moved their transshipment operations to Djibouti, strategically located to the south of this area, to bypass the regions controlled by the Houthi movement. Djibouti's port authorities anticipate that the share of transshipment activity will reach 60 percent in the medium term. As a result, the share of transshipped containers, which averaged 21 percent of total container volume in 2023, has doubled to 47 percent by early 2024. Société de Gestion du Terminal de Doraleh (SGTD) is also benefiting from increased productivity at the Doraleh container terminal, following the acquisition of four new gantry cranes in 2022 and the expansion of the terminal. This has enabled SGTD to operate the latest generation of vessels, with a capacity of over 23,000 TEUs. SGTD plans to increase the share of transshipment activity to 60 percent in the medium term. SGTD's diversification strategy is proving to

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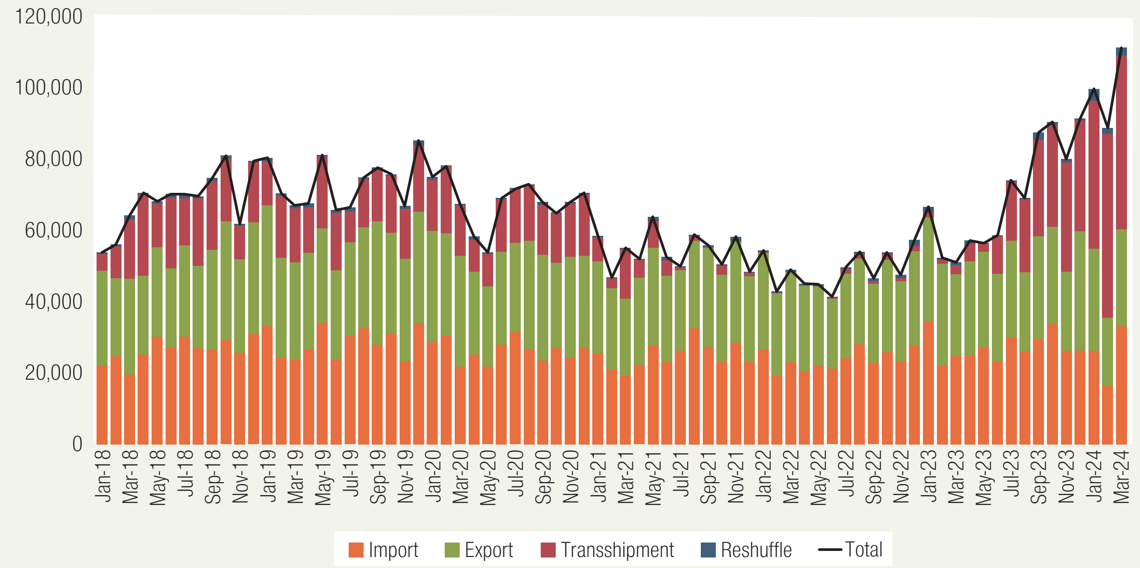
BOX 2: ECONOMIC IMPACT OF THE RED SEA CRISIS IN DJIBOUTI *(continued)*

FIGURE 2.1 • Volume of containers (TEU) handled at the Djibouti container terminal (SGTD) from January 2019 to March 2024



Source: Authors' calculations based on SGTD data.

be an effective bulwark against market fluctuations, reducing Djibouti's dependence on reexports to Ethiopia. By increasing its capacity to accommodate new-generation vessels, SGTD is strengthening the country's economic resilience and regional competitiveness.

The rising cost of sea freight, caused by tensions in the Red Sea, is affecting the prices of consumer goods in Djibouti and impacting household purchasing power. The main shipowners serving the port of Djibouti reported that by February 2024, the cost of sea freight per TEU on seven main shipping lines had doubled between Djibouti and Sokhna (Egypt), and by four and a half times between Djibouti and Qingdao (China). This increase has had repercussions on the prices of basic consumer goods, leading to a marked and steady rise in the price of rice, an essential staple food for Djiboutians. As shown in Figure 2.2, the price of a 50-kilogram bag of imported rice, which had remained relatively stable since 2022, began to rise in October 2023. This rise became more pronounced, reaching DF 3,463 at the end of March 2024, an increase of 22 percent compared with the end of November 2023. The latest Consumer Price Index (CPI) data from INSTAD indicates that, following several months of stability, the CPI increased by 5 percent in March 2024 compared to the same period the previous year. This inflation rate is the highest observed since December 2022, driven primarily by a 6.1 percent rise in food and non-alcoholic beverage prices. Prices for housing, water, electricity, gas, and other fuels also rose by 3.7 percent. Alcoholic beverages, tobacco, and narcotics saw a 3.2 percent increase, while health services prices went up by 6.7 percent. According to the June 2024 edition of the Integrated Food Security Phase Classification (IPC) and Malnutrition in Djibouti report published by the United Nations system, price increases have varied across regions. In Dikhil and Ali Sabieh, there was a significant rise in the price of rice in January 2024, whereas Tadjourah was more affected by the increase in pasta prices. Sugar prices also surged by over 10 percent in Tadjourah, Arta, and Dikhil compared to the previous year. Regarding fuel, kerosene prices rose by 13 percent in northern Djibouti between February and March 2024, and between 7 percent and 18 percent across all regions over the past 12 months. In Djibouti City, sugar prices increased by 6 percent compared to November 2023 and by 20 percent compared to the previous year.

Food insecurity has worsened over the past six months, with a concerning outlook ahead. The June 2024 edition of the UN system's Integrated Food Security Phase Classification (IPC) and Malnutrition report reveals that from April to June 2024, approximately 221,000 people, or 19 percent of the analyzed population (1.18 million people), face acute food insecurity (IPC IAA Phase 3 or higher). Among these, 38,000 individuals (3 percent) are in emergency situations (IPC IAA Phase 4), and 183,000 are in crisis situations (IPC IAA Phase 3). Rural populations are disproportionately affected due to limited dietary diversity, challenging economic conditions, low purchasing power, and restricted access to subsistence activities. Looking ahead to July to December 2024, a period marked by high temperatures and transhumance movements, an estimated 285,000 people (24 percent of the analyzed population) are projected to experience acute food insecurity. This includes 53,000 people in emergency situations (IPC IAA Phase 4) and 232,000 in crisis situations (IPC IAA Phase

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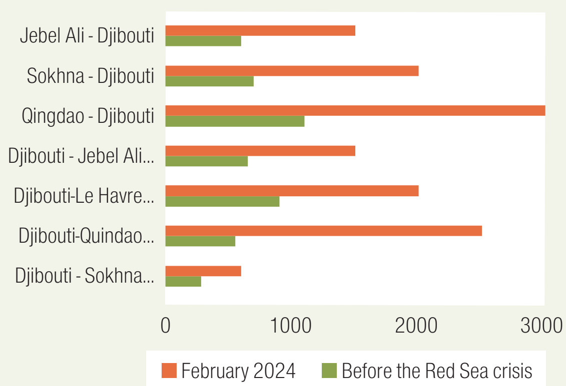
BOX 2: ECONOMIC IMPACT OF THE RED SEA CRISIS IN DJIBOUTI *(continued)*

3). Approximately 34 percent of the rural population will face acute food insecurity, with notable challenges in refugee camps such as Markazi (Obock), Holl-Holl, and Ali Addeh (Ali Sabieh). In urban areas, including Djibouti City, 15 percent of the analyzed population will be food insecure, primarily affecting the poorest and those reliant on daily wage labor. The main drivers of this food insecurity are price shocks, limited employment opportunities, and inadequate rainfall in certain regions. In response to this situation, it is recommended that the Government bolster food security efforts, particularly by enhancing resources for programs targeting the most vulnerable populations. This includes expanding food assistance and cash transfer initiatives.

Tensions in the Red Sea are having a significant impact on Djibouti's budget, adversely affecting customs revenues. For the first quarter of 2024, the preliminary and fragmentary data available show financial results below the forecasts in the initial finance law for the year. These reveal a drop in customs revenues of around DF 910 million (around US$5 million, or 0.1 percent of GDP). This decline is particularly noticeable in revenues from VAT and excise duties on tobacco and alcohol products, which are mainly imported. This decline is partly explained by the economic repercussions of the conflict that broke out on October 7, 2023, between Israel and Hamas, which is delaying imports from Europe, forcing ships to bypass Africa, with a direct impact on imports for the domestic market and customs revenues. These budgetary tensions are nothing new, as Djibouti had already suffered a $500 million shortfall by the last quarter of 2023, mainly due to subsidies on refined petroleum products. In 2022, despite global fluctuations in fuel prices following the Russian invasion of Ukraine, Djibouti maintained fixed kerosene and gasoline prices to support low-income earners. This policy, while guaranteeing affordable prices, has nevertheless exacerbated the budget deficit. Revenue losses will worsen with the continuation of these subsidies in 2023 and 2024.

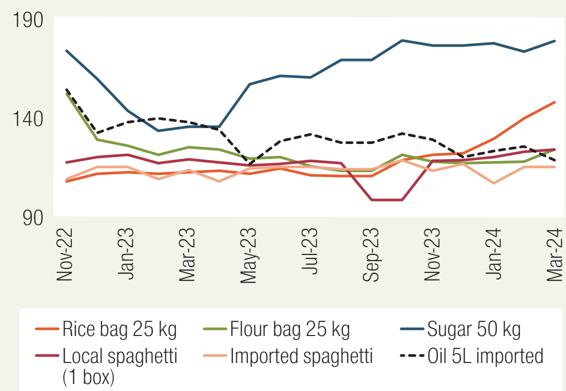
FIGURE 2.2 • Rising sea freight costs, due to tensions in the Red Sea, affect prices of consumer goods in Djibouti, particularly rice

a. Evolution of sea freight costs per TEU transported
By main shipping line



Source: CMA/CGM.

b. Djibouti prices for basic foodstuffs
(index: base 100, January 2022)



Source: World Bank staff calculations, based on data from data from INSTAD (National Institute of Statistics of Djibouti)

[a] https://thedocs.worldbank.org/en/doc/5d903e848db1d1b83e0ec8f744e55570-0350012021/related/CMO-Pink-Sheet-April-2024.pdf.

TABLE 2 • Selected Economic Indicators

		2019	2020	2021e	2022p	2023p	2024p	2025p	2026p
Real economy: annual percent change, unless indicated otherwise									
Real GDP	g	5.5	1.2	4.5	3.7	6.7	5.1	5.1	5.2
Private Consumption (growth)	g	5.0	–5.0	9.6	–0.6	4.4	5.0	5.0	5.0
Government Consumption	g	–3.9	–2.1	-2.5	-14.3	8.1	2.9	2.2	2.2
Gross Fixed Investment (growth)	g	7.3	1.0	4.9	2.7	12.4	8.5	6.8	7.6
Exports (growth)	g	9.2	–29.7	29.5	-12.5	8.4	9	10	10
Imports (growth)	g	10.1	–29.5	18.2	–6.2	10.4	11	11.3	11.3
Contributions to Real GDP									
Agriculture	% PIB	0.2	0.2	0.3	0.0	0.1	0.1	0.1	0.1
Industry	% PIB	1.9	-0.6	1.6	1.1	1.6	1.6	1.7	1.8
Services	% PIB	3.5	2.4	1.9	2.6	4.5	3.0	3.0	3.0
Consumer Price Index (end of period)	g	3.3	1.0	1.5	5.1	1.4	2.6	2.0	2.5
Fiscal Account, percent of GDP unless otherwise indicated									
Total Revenues and Grants	% PIB	23.5	23.4	20.0	18.9	18.9	18.9	18.9	18.8
Tax Revenues	% PIB	13.0	11.6	11.5	11.3	11.5	11.6	11.7	11.7
Non-Tax Revenues	% PIB	6.9	8.2	5.7	6.5	6.4	6.3	6.2	6.1
Grants	% PIB	3.6	3.6	1.8	1.0	1.0	1.0	1.0	1.0
Total Expenditures	% PIB	24.4	25.1	22.9	20.3	20.8	20.2	20.3	20.2
Current Expenditures	% PIB	15.9	14.6	14.2	15.3	14.7	14.7	14.7	14.7
Wages and Compensation	% PIB	6.5	6.3	6.2	5.8	5.7	5.7	5.7	5.7
Goods and Services	% PIB	5.6	5.6	5.3	5.7	5.3	5.3	5.3	5.3
Interest Payments	% PIB	1.3	0.2	0.2	0.7	0.8	0.8	0.8	0.8
Current Transfers	% PIB	2.6	2.6	2.5	3.1	2.9	2.9	2.9	2.9
Capital Expenditures	% PIB	7.6	7.1	7.1	5.1	6.1	5.5	5.5	5.5
Overall Balance (comittment basis)	% PIB	–0.9	–1.7	–2.9	–1.4	–1.9	–1.3	–1.4	–1.4
Government Financing	% PIB	0.9	1.7	2.9	1.4	1.9	1.3	1.4	1.4
External (Net)	% PIB	1.5	1.4	1.8	1.1	1.1	1.0	1.3	1.3
Domestic (Net)	% PIB	-0.6	0.3	1.1	0.3	0.8	0.3	0.1	0.1
Money and Prices									
Real Exchange Rate Index (2015=100)	l	104.6	99.4	97.9	96.6	94.8			
Domestic Credit to the Private Sector (% of GDP)	% PIB	22.4	20.9	18.6	20.1	18.5			
Balance of Payments, percent of GDP unless indicated otherwise									
Current Account Balance	% PIB	20.1	14.2	31.2	17.9	15.6	13.0	12.3	17.10
Imports, Goods and Services	% PIB	154.2	107.5	121.0	139.2	141.1	151.5	162.4	174.2
Exports, Goods and Services	% PIB	166.7	115.8	149.4	154.4	154.5	162.9	172.5	182.9
External Government Debt	% PIB	70.3	74	71.3	66.5	67.0	66.6	63.7	61.0
Exchange rate (per USD, average)	l	177.7	177.7	177.7	177.7	177.7	177.7	177.7	177.7
Other memo items									
GDP nominal in US$ (millions)	l	3,088.9	3,185.2	3,385.8	3,674.3	4,098.6	4,306.9	4,543.6	4,788.9

Source: Government data and World Bank staff calculati

3

STRENGTHENING THE REDISTRIBUTIVE EFFECTS OF DJIBOUTI'S FISCAL SYSTEM: OPPORTUNITIES FOR EFFICIENCY GAINS

This special chapter of Djibouti's Economic Monitor examines the redistributive effects of the country's fiscal system, analyzing how different taxes and transfers affect poverty and inequality. Using the Commitment to Equity (CEQ) methodology (Box 3) based on the 2017 Djibouti Household Budget Survey (EDAM) survey and administrative data, the study assesses the efficiency and equity of the fiscal system, and explores the impact of fiscal elements such as subsidies on different groups. It includes simulations for 2022, such as the expansion of cash transfers, the rising costs of stabilizing kerosene prices, and an increase in public spending on health. Analysis of Djibouti's fiscal system in 2017 reveals that, despite promoting equality, the system exerts upward pressure on poverty. Direct taxes prove progressive, therefore improving equity, while VAT, despite its importance for revenue mobilization, does increase the burden on the poorest, given its regressive nature. The National Family Solidarity Program (PNSF) which is designed to target low-income households, reinforces its progressive nature. However, kerosene subsidies, while significant, mainly benefit wealthier households. Precisely, while these subsidies benefit the poorest in absolute terms due to the cost burden of kerosene being relatively heavier on their budgets, the benefits are disproportionately accrued to the wealthier households in relative terms due to their higher consumption of the kerosene product. *Transfers in kind, such as education and health spending, while advantageous, do not always reach the poorest in an equitable way. The need for fiscal reforms targeting more equitable redistribution and increased revenues without exacerbating poverty is underlined, notably by rethinking kerosene subsidies and maximizing the benefits of social programs such as the PNSF, which exclusively targets the poor populations.*

Overview of Djibouti's fiscal system in 2017

Despite significant economic growth over the past decade, Djibouti faces persistent challenges of poverty and inequality. The poverty rate in Djibouti stands at 21 percent, with a high Gini coefficient of over 0.4, indicating an unequal distribution of wealth. Growth, mainly driven by services and port trade, has not been sufficiently inclusive, and the COVID-19 pandemic revealed the economy's vulnerability to global shocks. Fiscal policy, including taxation and social spending, is a key lever for sustainable and inclusive growth, enabling an equitable redistribution of resources. However, challenges such as pandemics, regional conflicts and debt limit the fiscal space needed to achieve these objectives. This analysis of fiscal incidence on poverty and inequality, based on 2017 data, aims to identify avenues for reform to combat poverty and inequality, while assessing the impact of taxes and social spending on the latter.

Compared with other countries, Djibouti's dependence on non-tax revenues is higher and social spending is lower. Djibouti's budget relies heavily on non-tax revenues, which make up 43.3 percent of total revenues (according to 2017 data), significantly higher than the MENA average, and allocates a modest 8 percent of GDP to social spending, significantly lower than the global average for low-income countries. Nevertheless, the main source of revenue comes from tax revenue. The tax system includes a progressive income tax for wage earners[9] and a 25 percent flat-rate tax on the profits of self-employed workers, with a universal VAT of 10 percent on most transactions, exempting essential products such as food and medicines. Social security contributions, capped at DF 400,000 per month, are shared between employers and employees and cover retirement, health, family allowances, and industrial accidents. The PNSF program provides direct transfers to the extremely poor, and discretionary fuel price adjustments counteract the volatility of international energy prices, acting either as a subsidy or a tax. Djibouti's health and education systems are mainly financed by public expenditure, in addition to health contributions from salaried workers. Djibouti's universal compulsory health insurance system (AMO) covers salaried workers, the self-employed, employees and pensioners. In addition, the Social Health Assistance Program (PASS) targets those not eligible for AMO. Income and expenditure included in this analysis are summarized in Table 3.

Djibouti's fiscal incidence analysis for 2017 led to the development of two simulated scenarios in addition to the base scenario. The first scenario (S1) reflects conditions in 2022, with an increase in cash transfers similar to that of the PNSF, a rise in the number of PASS beneficiaries, and an increase in kerosene subsidies from DF 24.4 to DF 94.84 per liter, in response to soaring international energy prices[10]. The second scenario (S2) proposes a fiscally neutral reallocation of kerosene subsidy funds to targeted cash transfers, thereby increasing the number of beneficiary households without increasing total expenditure, in response to macroeconomic challenges and social needs. The different scenarios are summarized in Table 4.

The fiscal system has a positive effect on equality

The fiscal system as a whole improved equality, reducing inequality by 8 Gini points in 2017; however, the effects of each individual tax intervention vary. Tax measures and direct transfers reduced the Gini coefficient, a measure of inequality,

9 Between 2 percent (for income up to DF 360,000) and 30 percent (for income over DF 7,200,000), except for salaried workers earning DF 50,000 or less per month, who pay no income tax.

10 The initial price of kerosene (as imported) is called the free on board (FOB) price. The final price, as received by households, is called the pump price. Price adjustments, as well as other charges and taxes, are added to the FOB price according to specific formulas. Unlike most costs and taxes, the price adjustment for 2017 (and 2022) is not available in government figures. To calculate the price adjustment for kerosene, we average the FOB price, pump price, costs and taxes for all months of 2017 (and 2022), then revert to the price adjustment. Whenever specific items related to costs and taxes are not available, assumptions are made about what costs should be by looking at data from subsequent years. These costs and taxes have hardly changed over time, if at all.

TABLE 3 • Revenues and expenses included in the analysis

Public revenues, social security contributions and subsidies	Administrative data: Total (Millions DF 2017)	Data administrative: % of total	Administrative data: % of GDP	Survey: Total (Millions DF 2017)	Survey: % of administration data	Included in the analysis?	Allocation method
Total	**123,413**		**33.3 %**				
Revenue	**114,490**	**92.8 %**	**30.9 %**			Partially	
Tax on wages and salaries	11,337	9.2 %	3.1 %	5,712	50 %	Yes	Identification
Income, profit, and capital gains tax[a]	10,705	8.7 %	2.9 %	4,192	39 %	Partially	Identification
V.A.T.	14,863	12.0 %	4.0 %	6,878	46 %	Yes	Identification
Help	**8,923**	**7.2 %**	**2.4 %**			**No**	
Government spending	**Administrative data: Total (Million DF 2017)**	**Administrative data: % of total**	**Administrative data: % of GDP**	**Survey: Total (Millions DF 2017)**	**Survey: % of administration data**	**Included in the analysis?**	**Allocation method**
Social expenses	**27,143**	**22.0 %**	**7.3 %**				
Social protection	4,859	3.9 %	1.3 %				
PNSF	403[b]	0.33 %	0.01 %	407	101 %	Yes	Simulation
Education	18,054	14.6 %	4.9 %				
Preschool	121	0.1 %	0.03 %			No	
Primary	5,900	4.8 %	1.6 %	6,494	110 %	Yes	Allocation
Secondary	8,860	7.2 %	2.4 %	9,752	110 %	Yes	Allocation
Commercial	3,173	2.6 %	0.9 %	3,493	110 %	Yes	Allocation
Health	4,230	3.4 %	1.1 %				
Social Health Assistance Program (PASS)	1,000[c]	0.8 %	0.3 %	507	51 %	Yes	Simulation
Stabilization of kerosene prices	**398[d]**	**0.32 %**	**0.1 %**	**192**	**48 %**	**Yes**	**Identification**

Source: Authors' calculations and compilation based on data from EDAM (2017), UNICEF (2020), MASS (2019), Revenue Law (2017) and Ministry of Education and Vocational Training (2020)..

[a] This figure for the CEQ analysis includes taxes on the profits of self-employed workers.

[b] This figure is calculated manually by taking the total number of households benefiting from the PNSF and multiplying by DF 120,000, which is the annual amount of cash transfers received by each household.

[c] This value corresponds to that of 2016, but as the data available for 2016 (DF 1,000 million) and 2019 (DF 1,093 million) show that there is not much change over time, this assumption is thought to be reasonable.

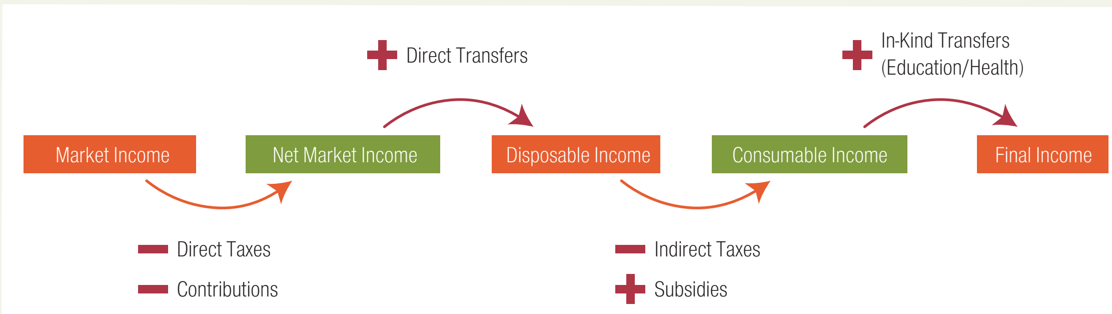
[d] This figure is not taken directly from the administrative records, but rather is calculated manually using the total quantity (in liters) of kerosene consumed in 2017 in Djibouti, obtained from the customs service, and multiplying this amount by the amount of the average kerosene subsidy in 2017, which is imputed manually.

from 0.44 at market income to 0.41 at disposable income, as Figure 22 shows. The PNSF program played a key role in this reduction. However, indirect taxes and subsidies did not alter the Gini coefficient when moving from disposable to consumable income. In-kind transfers, such as public spending on education and health, reduced inequality, lowering the Gini coefficient by a further 5 points. Simulations S1 and

BOX 3: METHODOLOGY

The CEQ methodology[a] develops different income concepts resulting from various fiscal interventions and analyzes their profiles in terms of poverty and inequality. This method comprises five income concepts, as detailed in Figure 3.1: i) market income[b], which refers to the income an individual earns on the market, ii) net market income, which results from the deduction of direct taxes and social security contributions from market income, iii) disposable income, which includes direct transfers (e.g., cash transfers) to net market income, iv) consumable income, which includes subsidies and from which indirect taxes (such as VAT) are deducted, and v) final income, which compared to consumable income, includes transfers in kind (such as public spending on education and health). Poverty and inequality are calculated at the level of each income concept, using respective headcounts of the population living below the national poverty line and the Gini coefficient. The attribution method for each tax intervention is defined either by (i) direct identification, when the survey indicates the benefit recipient or tax payer as well as the amount received, or by (ii) imputation, when the survey indicates the benefit recipient but not the amount received, or by (iii) simulation, when none of the above methods can be used, in which case the recipients and amounts received must be calculated according to program rules in line with administrative data. The results obtained for specific tax items are described by quintile of consumption distribution. The analysis is based on the EDAM 2017 as well as administrative data.

FIGURE 3.1 • Income concepts used in CEQ analysis



Source: Lustig (2018).
Note: This analysis is based on fiscal data of 2017 due to the availability of EDAM household survey data for 2017. This is a relatively stable year compared to the later period, which was affected by the COVID-19 pandemic. The main objective of this report is to map the country's main tax policies and assess their effects on poverty and inequality with a view to examining whether they can be made more effective by adjusting the various tax elements. The tax elements used by the Djibouti government are direct taxes and social security contributions for salaried and non-salaried workers, indirect taxes (VAT) on consumption, a program of direct cash transfers, fuel subsidies and spending on health and education.

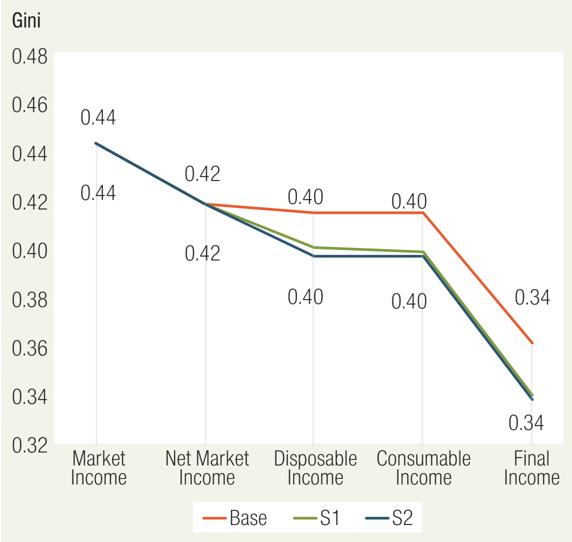
[a] Lustig, N. (2018). N.B. Although this analysis is instructive in assessing the effects of the fiscal system in Djibouti on poverty and inequality, there are several caveats and limitations worth mentioning: 1) The assessment excludes certain tax and expenditure items likely to have an effect on household welfare, notably excise taxes due to lack of data availability; 2) The CEQ analysis is based on an accounting framework, so it does not incorporate behavioral, intertemporal and second-order effects; 3) The analysis of benefits in kind measures the transfer at its average cost of provision and does not take account of the quality of services; 4) Tax policy is analyzed solely from the distributional angle. Indeed, while redistribution is a key objective of tax policy and an important tool for poverty reduction, tax policy may have broader objectives that are not taken into account in this type of analysis; 5) The availability and quality of data in Djibouti posed a significant challenge to the analysis.
[b] It should be noted that contributory pensions can be treated either as a government transfer or as deferred income—an issue on which there is no agreement in the tax literature. The CEQ methodology takes a neutral stance on such treatment by performing the tax incidence analysis for both scenarios. For this tax analysis, pensions are treated as deferred income, which means that the reference income is market income plus pensions. However, for the sake of simplicity, market income plus pensions are referred to as market income.

TABLE 4 • Number of beneficiaries and public spending under different scenarios

	Base	S1	S2
PNSF beneficiary households	3,362	14,361	21,195
PASS households	9,270	32,000	32,000
Total beneficiary households	12,632	46,361	53,195
Kerosene subsidy (in DF per liter)	24,4	94,84	0

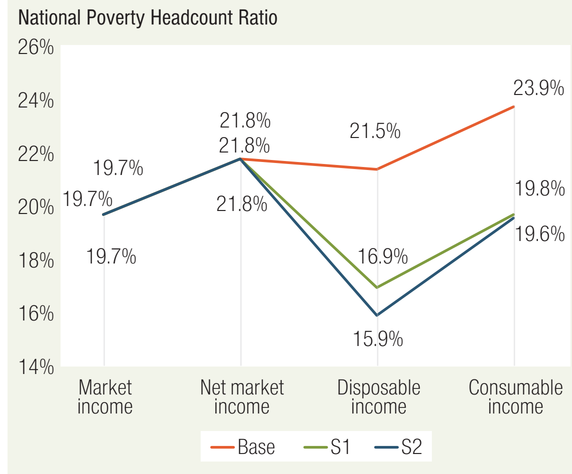
Source: Authors' calculations based on EDAM (2017) and administrative data.
Note 1: The number of PNSF and PASS beneficiaries is calculated using data from the Ministry of Social Affairs' administrative social register for 2017 (baseline) and 2022 (S1). The number of beneficiaries for S2 is calculated by the total savings on the kerosene subsidy in the event of abolition, divided by the annual transfer per household in the PNSF.
Note 2: The kerosene subsidy per liter is calculated by adjusting the average price over the whole year on the basis of FOB prices and the kerosene price structure.

FIGURE 22 • Effects of tax interventions on income inequality



Source: Authors' calculations based on EDAM (2017).

FIGURE 23 • Impact of tax measures on poverty



Source: Authors' calculations based on EDAM (2017).
Note: The results assume perfect targeting of direct transfers. As is standard practice in the CEQ methodology, the poverty rate is not calculated for transfers in kind (e.g., education and health).

S2, which provided for higher levels of beneficiaries, succeeded in lowering the Gini from 0.44 to 0.40, surpassing the effect of the baseline scenario, which had a reduction of 8 Gini points. These simulations also increased the number of PASS beneficiaries, leading to a further 6-point reduction in inequality. Spending on education reduces inequality, but this effect diminishes as the level of education increases, with a decreasing impact from primary to tertiary level, mainly because poorer households participate less in higher levels of education. Finally, the effect of VAT exemptions on reducing inequality is limited, as consumption of both exempted and non-exempted products varies little between quintiles.

Although the fiscal system exerts upward pressure on poverty, increased social transfers reduce it

As in many other countries, while the fiscal system reduces inequality (in 2017), it exerts upward pressure on the poverty rate (Figure 23). This is because taxes and contributions have a greater negative impact on poverty than the positive effects of transfers and subsidies. In detail, the poverty rate, measured on market incomes, increases slightly when consumable incomes are taken into account, although this increase is not statistically significant. The PNSF and subsidies reduce poverty[11], but their impact is small (0.003 and 0.001 respectively), especially when compared to the negative effect of indirect taxes such as VAT (–0.027), direct taxes (–0.015) and contributions (–0.011). The poorest people, often in the informal sector, are less affected by direct taxes and contributions, but bear the impact of indirect taxes. The latter fall into poverty when this income is converted into adult equivalents, despite some incomes exceeding the tax allowance. Thus, taxes tend to increase poverty, while transfers attempt to reduce it, with indirect taxes being the most penalizing and direct transfers the most beneficial for poverty reduction.

The effectiveness of the PNSF program[12] in the fight against poverty improves markedly with

[11] These effects are measured through marginal contributions, with final income as the reference income.

[12] From a purely technical point of view, the headcount reduction between net market income and disposable income is made up of an income reduction (from direct taxes, which is observable and included), another income reduction (from savings, which is unobservable and not included), and an income supplement (from the PNSF, which is observable and included). Nevertheless, it may be reasonable to assume that the marginal propensity to save for the poorest quintile, who are the main beneficiaries of the PNSF, is very low, if not zero.

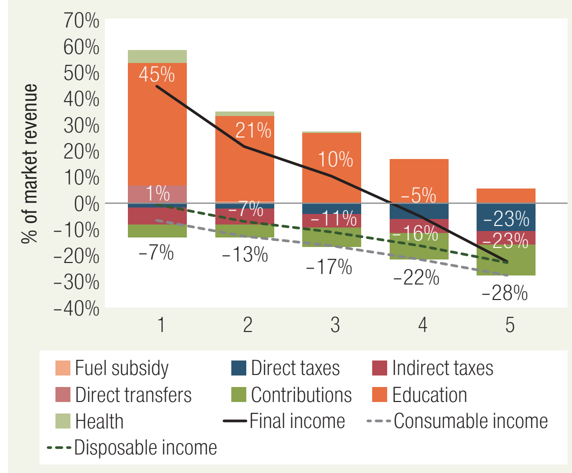
its expansion in 2022, following a modest impact in 2017. Initially, the PNSF reduced poverty by just 0.3 percentage points from net market income to disposable income, as illustrated in Figure 23. However, recent simulations show a notable change: poverty has slightly increased by 0.1 percentage points in S1, while it has decreased by 0.1 percentage points in S2, as a result of redirecting kerosene subsidies to the PNSF. This marks a significant improvement in the program's impact on poverty reduction.

Analysis of the Implications of Fiscal and Social Expenditure Policies on Equality and Poverty in Djibouti

Some elements of Djibouti's fiscal system are progressive, while other elements do not benefit poor households sufficiently. Here is a summary of the results:

- **In general, wealthier households contribute more to the fiscal system than they benefit from it, while poorer households are the main beneficiaries.** The poorest households receive transfers equivalent to 45 percent of their market income, mainly in the form of education and health services (52 percent of these transfers), and direct transfers via the PNSF program (6 percent). Conversely, the richest pay 23 percent more than they receive, reducing their net income by 23 percent, according to Figure 24. However, if consumable and disposable income, including all taxes and transfers, are considered, even the poorest end up paying a considerable proportion of their market income in taxes, thus also becoming net contributors.
- **Direct and indirect taxes:** The richest 40 percent, consuming 60 percent of total consumption, pay the majority of taxes and benefit most from VAT exemptions. Direct taxes are progressive, increasing with income, while VAT is regressive, despite its importance in revenue mobilization, impacting low-income earners more despite similar consumption structures.
- **Direct cash transfers:** PNSF allocations are designed to benefit mainly the poorest, based on the assumption of perfect targeting. However, this effectiveness is conditioned by the precision of the targeting; in fact, imperfect targeting could reduce its impact on the target populations.
- **Education:** Overall, education spending becomes less progressive at higher levels of education, reflecting inequitable access to higher education opportunities in Djibouti in 2017. Spending on primary education is evenly distributed, reflecting equitable access at this level. Lower secondary education shows an inverted U-shaped distribution of spending, concentrated in the middle class.
- **Health:** The impact of PASS on household income was initially low in 2017 due to the low number of beneficiaries, but has increased over time.
- **Kerosene subsidy:** The Djibouti government operates a mechanism to stabilize the price of kerosene, the fuel product most consumed by households[13]. Although intended to protect

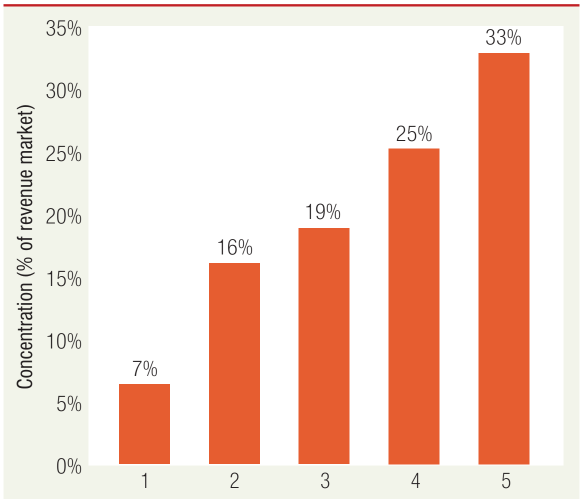
FIGURE 24 • Distribution of benefits and payments by tax instrument for each quintile (2017)



Source: Authors' calculations based on EDAM (2017).

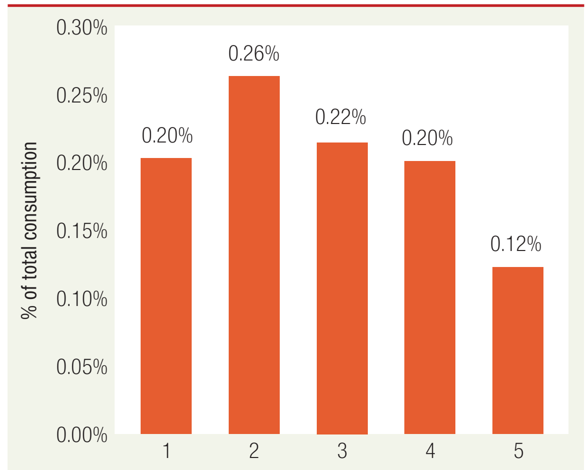
[13] Only a tiny segment of EDAM households reported consuming diesel or gasoline in 2017. Moreover, as diesel and gasoline are used for production services, any change in the subsidy structure requires a broader analysis of the effects on production, form benefits, corporate taxes, and end-user prices.

FIGURE 25 • Concentration (distribution of kerosene subsidies by market income quintile)



Source: author's calculations based on EDAM (2017).

FIGURE 26 • Impact (kerosene subsidy as a share of market revenue (%) by quintile)



Source: author's calculations based on EDAM (2017).

poor households against fluctuations in fuel prices, the subsidies mainly benefit wealthier households, who consume more kerosene. The results show that, although the poorest quintile benefit more from these subsidies in absolute terms, the richest households concentrate the majority of the benefits, as shown in Figure 25. However, in relative terms, expenditure on kerosene weighs more heavily on the budgets of poor households, as illustrated in Figure 26. This indicates that kerosene subsidies are not the most effective means of reducing poverty and inequality. The resulting analysis, simulating the reallocation of the budget to direct cash transfers, which exclusively target the poor, shows that this type of targeted transfers yields better results in terms of poverty reduction.

Conclusions

Thanks to direct taxes and in-kind transfers, the fiscal system plays a key role in reducing inequality, lowering the Gini coefficient by 8 points. The analysis also shows that when the number of beneficiaries of the PNSF and PASS programs increases, the reduction in inequality reaches 10 Gini points. However, redirecting all subsidies to direct cash transfers under the PNSF does not reduce inequalities any further, with the reduction remaining at 10 Gini points. Finally, it appears that investment in lower levels of education has a greater impact on reducing inequality than investment in higher levels of education.

Although Djibouti's fiscal system reduces inequality, it exerts upward pressure on poverty, increasing it by 4 percentage points in 2017, though this is a non-statistically significant increase**.** This pressure stems mainly from the regressive nature of VAT. However, the expansion of the PNSF and PASS programs in 2022 could lead to a significant reduction in extreme poverty of 1.2 percentage points in terms of disposable income, as a result of the increase in the number of beneficiaries. Nevertheless, the scale of transfers, which represent on average 40 percent of market income for the poorest quintile, is not enough to balance out the burden of indirect taxes or enable an overall reduction in poverty. Since 2017, and more intensely after the COVID-19 pandemic, the government has significantly stepped up its cash transfer program, despite the budgetary implications of these expansions, including a budget deficit of 1.4 percent of GDP in 2022.

Kerosene subsidies, although intended to stabilize fuel prices, have a limited impact

on reducing inequality and poverty, being three times less effective than direct transfers from the PNSF, which target the poor. Wealthier households consume more kerosene and therefore benefit more from these subsidies than poorer households. This suggests that these subsidies do not really favor the poorest, despite their intention to protect them against price volatility. Targeted cash transfers to the poorest prove to be a far more effective strategy for combating inequality and poverty. The results of the simulations in this chapter support the notion that reallocating funds from kerosene subsidies to direct cash transfers, similar to those of the PNSF, could achieve a far more significant reduction in poverty and inequality.

Unlike in many other countries, even the poorest households are among the net payers when only consumable and disposable income is taken into account. However, when in-kind transfers such as education and health care are included, only the richest households remain net payers. Indeed, at the level of final income, which incorporates these in-kind transfers, the poorest households benefit greatly from the fiscal system, becoming net recipients, while the richest contribute progressively more to the financing of taxes and transfers. This highlights how essential public services such as health and education can reverse the tax burden of the most disadvantaged households, offering them a net advantage in their tax contribution.

For greater effectiveness in the fight against poverty, the results of this analysis suggest potential avenues for subsidy and social protection reform. While this analysis provides an overview of Djibouti's fiscal system and its effects on poverty and inequality in 2017, policy changes, budgetary pressures and the global food and commodity price shocks of regional and international conflicts, require more up-to-date data and analysis to inform policy reforms. Moreover, it is important to note that fiscal policy is only one of several areas that can contribute to the fight against poverty (encouraging a more dynamic private sector, institutional and legal reforms that guarantee greater equality of opportunity, are examples of other areas). Some of the avenues for tax reform are :

- **Implementing targeted transfers to use resources more efficiently.** Assuming that the objective of kerosene subsidies is to protect the poor, and that the majority of kerosene imports are consumed by households (as opposed to value chain inputs), this subsidy may not be the most efficient use of resources. While this subsidy may protect the poorest segment of the population from price fluctuations, more substantial poverty gains may be derived from more targeted transfers. Indeed, this paper reveals that this tax instrument is not pro-poor. Policy reform analysis requires more data and an assessment of the indirect and general equilibrium effects of the subsidy. Furthermore, the implementation of such reforms requires strong governance systems and the building of public confidence that the resulting budget savings will be used in programs that protect the poorest segment of the population (e.g., cash transfers).
- **Continuing to invest in social protection and the provision of services that boost human capital, both essential to stimulate poverty reduction and shared prosperity.** One of the key findings of the analysis is the progressive, pro-poor nature of this spending. Expanding the coverage of the cash transfer program (PNSF) from 2017 to its 2022 levels has shown considerable effects on poverty reduction. Similarly, spending on health and education has had a positive impact on reducing inequality. These underline the importance of continuing efforts to invest in human capital and social protection to promote inclusive growth.
- **Expanding pro-poor social programs, whether in the form of direct transfers or in-kind.** This requires substantial resource mobilization. Given Djibouti's heavy dependence on non-tax revenues, it is advisable to explore ways of increasing tax revenues and mobilizing domestic resources by progressive means. Policy solutions for revenue mobilization that have been recommended for government consideration include reducing tax exemptions and increasing efficiency in public enterprises[14].

[14] International Monetary Fund Article IV Mission 2022 to Djibouti, December 16, 2022. Press release no. 22/437.

4

THE EFFICIENCY OF PUBLIC SPENDING IN THE ROAD SECTOR

Road infrastructure is essential to development. On a regional scale, roads contribute to the competitiveness of Djibouti's ports by ensuring good connectivity with the hinterland. Transport infrastructure requires substantial investment. It is therefore essential that public spending on road infrastructure is as efficient as possible. This chapter presents the mechanisms for financing the road sector and examines the benefits of institutional reform in the road sector in the light of the budgetary efficiency of road infrastructure investments. Analysis of Djibouti's road sector reveals three main challenges: inefficient institutional organization with overlapping responsibilities, a poorly maintained road network and a lack of small local enterprises to maintain, secure, and diversify revenues and insufficient and poorly managed funding, with high salary costs. These reforms require strong political will and could significantly transform Djibouti's transport sector.

Because of its location and the presence of its ports, the road infrastructure that links its ports to its hinterland is crucial for Djibouti. The emergence of other ports in the region could, however, alter the balance. The quality and durability of road infrastructure is therefore essential to ensure good connectivity between seaports and their hinterlands. Roads are therefore crucial to the country's competitiveness as a port of entry to the sub-region, and to Ethiopia in particular.

Financing the construction and maintenance of road infrastructure is an important part of a country's transportation system. Roads are generally built by public authorities. All over the world, governments are faced with the need to build new roads and maintain existing ones. In general, however, transport infrastructures require a singularly high level of investment in relation to the revenue generated by their use, particularly in the road sector. The scale of capital expenditure calls for large-scale public or concessionary contributions to finance road infrastructure development. Thus, governments, users, the private sector, and external sources all contribute to financing the construction and maintenance of road infrastructures. Against this backdrop, and given the constraints on national public finances, it is essential that public spending on road infrastructure is as efficient as possible.

A high-quality road network is crucial to the continued competitiveness of Djibouti's ports. Djibouti's road network is 1,793 km long, 66 percent of which are national roads and 34 percent urban roads, mainly in the city of Djibouti. Corridor roads are crucial for the country, as they ensure accessibility between seaports and their hinterland. And yet, according to the data collected during interviews, 66 percent of these roads are in poor condition. As a result of low tax revenues in relation to GDP, the gap between financial needs and required resources is considerable for the road sector. In the case of roads of regional importance, i.e. those linking ports to the hinterland, only around 50 percent of needs are covered. The poor condition of corridor roads leads to higher transport costs, particularly in terms of premature wear and tear of rolling stock and increased risks for users. In addition, the lack of enforcement of legislation controlling the axle load of trucks travelling along the corridor linking Djibouti's ports to Ethiopia means that the roads have a shorter life cycle than anticipated. All these factors lead to higher transport costs, prevent the road sector from playing its role as a generator of economic development, and could undermine the competitiveness of Djibouti's ports.

Institutional fragmentation and overlapping responsibilities in road sector management are not conducive to efficient public spending (Box 4). This situation affects the country on two levels. At the national level, corridor roads in poor condition pose a risk to the competitiveness of ports, which are vital to the country's economy. On a national scale, urban roads are also in poor condition. Annual maintenance requirements for Djibouti's urban roads are estimated at DF 1.5 billion, with expenditure in 2022 amounting to just DF 258 million. Spatial accessibility to economic opportunities is therefore not easy for the population, and this can slow down economic development.

This chapter presents the current mechanisms for financing the road sector, and then examines the benefits of institutional reform in the road sector in the light of the budgetary efficiency of road infrastructure investments.

Financing mechanisms for the road sector

The corridor road network is a key element in ensuring the competitiveness of Djibouti's ports. The value of road assets and the financial consequences of delayed maintenance for the economy and for users mean that road maintenance is a high priority, particularly in Sub-Saharan African countries. This is true in Djibouti, where road transport accounts for around 90 percent of the movement of goods and people in the country, underlining the economic importance of roads on a national

BOX 4: PLAYERS IN ROAD SECTOR GOVERNANCE

The current institutional organization of the road sector is sometimes difficult to read, as the functions and responsibilities of the institutions in charge of the road sector overlap.

The Ministry of Infrastructure and Equipment (MIE) is responsible for implementing and coordinating policy on road, rail, sea and air transport infrastructure and services. The Djibouti Roads Agency (ADR) and Djibouti Ports Corridor Road (DPCR SA) are under its supervision. In terms of road sector management, MIE's main missions are to design and implement the government's road infrastructure policy, coordinate transport policy, and develop and maintain roads serving production zones and tourist sites.

The ADR, created in 2013 by Decree, is the result of the merger of the Road Maintenance Fund (FER) and the Department of Equipment of the former MIE. It has the status of a public company and is the delegated contracting authority for roadworks. The agency is responsible for both road agencies and roadwork contractors. Roadworks in Djibouti are carried out by ADR (partnership contract) and by large public works companies, often of foreign origin. ADR generally works with large international companies and design offices. Small and medium-sized companies and engineering firms are not yet well developed in Djibouti. Routine maintenance work on urban roads, other national roads, and tracks is financed by the national budget. Road rehabilitation and construction work is financed by the national budget and donors.

DPCR SA was created by Presidential Decree on February 23, 2017, as a public industrial and commercial establishment (EPIC) with the status of a state-owned company. The two shareholders are Great Horn Investment Holding (GHIH), with 65 percent of the capital, and ADR, with 35 percent of the capital. DPCR SA has had exclusive management (rehabilitation, modernization, and development) of the road corridor network since 2018. DPCR also holds the exclusive right to collect road fees from traffic using the corridor roads.

and regional scale. While sourcing funding for road construction is important, it is essential to mobilize resources for road maintenance to maximize the life cycle and profitability of investments in roads.

It is currently difficult to obtain precise figures on the total amount of fees and taxes collected from Djibouti's road sector and the sector's needs. Interviews highlighted the fragmentation of the players involved. At present, sources of funding for road maintenance (urban roads, national roads, and corridor roads) are:

i. The road user fee (tax on loaded trucks), collected by DPCR on the corridor routes from Djibouti's ports to neighboring countries (mainly Ethiopia). The fee is set at US$20 per loaded truck, and applies to the round trip of the truck. The rate is set by the Joint Commission of Djibouti and Ethiopia. DPCR collects corridor road user fees directly on its own behalf, at points and stations located at port exits and along corridor roads;
ii. Income from related activities (crane lifting proceeds, penalties and fines collected by the Road Safety Squadron);
iii. Direct subsidies from the State (national budget) via ADR finance for routine maintenance work on Djibouti's urban and national roads;
iv. Fees levied by the Ministry of the Budget, i.e., charges paid by users in return for the use of a public service, and taxes, i.e., charges paid by the taxpayer on certain transactions. Taxes or royalties on fuels/lubricants, insurance, vehicle registration fees, and driving licenses are paid into the general budget and allocated to other sectors of the country's economy.

The contribution of governance reform in the road sector

Governance reforms in the road sector would increase the efficiency of public spending. The Infrasap study conducted by the World Bank highlighted that ADR and DPCR are below their comparators in Sub-Saharan Africa in terms of accountability and autonomy.

International experience shows that roads are often managed by the Ministry of Transport, a road agency, and a road fund. Optimal functioning of the institutional context of the road sector raises the question of better defining the responsibilities of the institutions and organizations involved in road management in Djibouti. Assessment studies of road funds and agencies, such as those by S. Brushett in 2004 and the European Union in 2009, have shown that when these structures are in place, the funds devoted to road construction and maintenance increase, and the quality of the road network also improves. Reforming Djibouti's road sector by allocating funds to the road sector, clarifying the roles of the road agency and the road fund, and ensuring strong governance, would enable better control of the funding earmarked for the road sector.

Better scheduling through a road agency

The creation of road agencies enables a clear division of management functions between the road administration (administrative functions) and the management of public contracts by the executing agencies (operational functions delegated by the administration). This division of responsibilities and activities between the State and the road agency must be clearly defined. The activities transferred concern the construction, rehabilitation, and maintenance of main roads in general. The agencies' core business is programming and contracting, which includes awarding contracts, monitoring contract performance, supervising works, and managing road databases. Road agencies' revenues come from road funds, the state budget, and donor funding. Table 5 highlights examples of road agency resources.

Road agencies are government agencies in which the public authorities have retained their influence and power. The overwhelming majority of road agency expenditure is for road maintenance or construction. In Tanzania and Ghana, for example, 92 percent of national road agency expenditure is devoted to road maintenance or construction while in Zambia it is 84 percent; however, in Djibouti, less than 25 percent of revenues are allocated to road maintenance (see Box 5). It is essential to note that the operating costs of road agencies generally remain below 10 percent of expenditure. The ratio of the number of kilometers per

TABLE 5 • Examples of road agency resources in 2007

	Tanzania TANROADS (Tanzania Road Agency)	Zambia RDA (Zambia Road Agency)	Ghana GHA (Ghana Road Agency)
Total resources In millions of euros	192	83	141
Resources from:			
Road fund	42.7 %	38.6 %	23.4 %
State budget	47.9 %	25.3 %	58.2 %
Lessors	9.4 %	36.1 %	18.4 %
Km/agent	123	224	7

Source: European Union, 2009.

agent speaks to the allocation of implied resources and in Djibouti, this ratio is 2.9 if ADR and DPCR employees are combined. As their functions overlap, a strict comparison is not possible. However, this ratio gives a sense of the difference between Djibouti and other countries. Efficient public spending in the road sector requires maximum investment in the sector to enable the maintenance of a quality road network and make it possible to attract additional sources of funding from, for example, the private sector.

The need to secure financing for the transport sector

Earmarking revenues for the road sector would help secure funding. Although the solution is not ideal from a fiscal policy point of view, earmarking revenues from taxes and fees to a predetermined expenditure item may be justified in the context of Djibouti's road sector. In Djibouti, the a priori allocation of revenues would make it possible to increase the budget dedicated to the sector and thus the country's competitiveness. Since the revenues in question are limited in amount (Box 5) and already collected, this strategy would provide the long-term visibility needed for transport investments, and could help mobilize private-sector financing.

The majority of countries with a road agency also have a road fund which aims to collect revenues for road maintenance (routine and periodic maintenance) of the entire national network (urban and pre-urban, interurban, and regional), make funds available to companies on a regular and stable basis, and ensure efficient and transparent management of these funds to ensure their exclusive use for road maintenance.

BOX 5: A MORE APPROPRIATE ALLOCATION OF INCOME WOULD BENEFIT THE TRANSPORT SECTOR

The team's interviews with road sector players revealed that the total amount of fees and taxes collected from the road sector by DPCR and the Ministry of Budget amounts to DFA 3.6 billion per year, equivalent to USD 20 million or 0.6 percent of GDP. According to the figures provided, road maintenance requirements amount to DFA 2.5 billion. The amount of revenue generated by the road sector would therefore exceed road maintenance requirements. At present, only 21 percent to 23 percent of revenues collected are used for road maintenance, despite the fact that road infrastructures require major investment to rehabilitate them to maintain the country's connectivity and competitiveness.

In terms of public spending, ADR and DPCR have high payroll costs, representing 47 percent and 37 percent of total expenditure, respectively.

In the light of the figures gathered in interviews, it would appear that the a priori under-financing of the road sector is partly linked to a less-than-optimal allocation of financial resources within institutions. The issue of under-financing in the transport sector raises the question of the country's connectivity and competitiveness. Investment in logistics and port activities has played a key role in the country's economic growth. The sector is therefore at the forefront of the country's efforts to maintain its economic engine and competitiveness.

BOX 6: THE IMPORTANCE OF DIVERSIFYING FUNDING SOURCES FOR THE TRANSPORT SECTOR

When it comes to financing transport infrastructure, implementing the "user pays" principle is a sound approach in terms of public finance. Ardila-Gomez and Ortegon-Sanchez identify three categories of transport infrastructure beneficiaries: direct, indirect, and the general public (2016). It is therefore essential to identify the various beneficiaries, ensure that their contributions are commensurate with the service received, and determine the terms and conditions of their contributions.

The most natural source of funding for road transport is toll revenue, thus applying the "beneficiary pays" principle. But these revenues are not enough. Many countries have introduced a fuel tax, the proceeds of which are used directly to finance, even partially, transport infrastructure. In the United States, part of the federal fuel tax goes into the Highway Trust Fund, which was set up to finance highways. Since 1983, part of the fuel tax has been paid into the Mass Transit Trust Fund, which helps finance public transport services (U.S. Department of Transportation, 2024). Fuel taxes are also based on the "beneficiary pays" principle.

A good transport infrastructure project will have a multiplier effect. Ardila-Gomez and Ortegon-Sanchez point out that a good transport project will transform cities by launching a virtuous circle. As cities become more attractive, they attract a variety of funding sources, further enhancing their attractiveness. The authors point out that a good investment will help to modify both the supply and demand for transport (2016). Similar reasoning can be applied to the road sector, particularly in Djibouti, where the road sector supports the country's economic engine—the ports.

The resources likely to be collected and allocated to the road fund depend on the resources available in each country. It is worth noting, however, that road fund resources mainly come from fuel levies (or taxes). For example, the share of these fees in total revenues is 94 percent in Ghana, 95 percent in Tanzania and 97 percent in Zambia. However, the total resources mobilized remain below network maintenance requirements. To ensure sustainability from a public finance perspective, it is necessary to diversify funding sources (Box 6).

For Djibouti, resources could come from taxes dedicated to financing the road sector and road user fees, which is crucial in a context where corridor roads are of regional interest. In Djibouti, the resources allocated to the road fund could include crane hoisting revenues, taxes or surcharges on fuels and lubricants, taxes or fees on insurance, registration fees, taxes on port goods, and direct government contributions. These taxes are already levied in Djibouti. All that is needed is for these revenues to be allocated strictly to the road sector.

Road funds are extremely lean structures in terms of personnel. Table 6 highlights the low level of expenditure on operating costs in four African countries. Once again, these expenses can be compared with the operating expenses of the institutions currently in place in Djibouti. The ratio of road network kilometers per agent employed by the road fund is 7,128 in Tanzania, 3,760 in Zambia, 5,094 in

TABLE 6 • Road fund expenditure, in millions of euros

	Tanzania (2008)	Zambia (2007)	Ghana (2007)	Burkina Faso (2008)
Operating expenses	1.06	0.26	Not available	0.13
Priority network maintenance	84.8	37.26	20.1	22.3
Local authority network maintenance	37.4	11.16	43.2	0.30
Costs incurred by Ministries for road maintenance	8.70	0	3.2	0.98
Consulting and other fees	0	3.68	0.63	0.3
Total	**131.96**	**52.36**	**67.1**	**24.0**

Source: European Union, 2009.

Ghana and 4,093 in Burkina Faso. Once again, the comparison is not optimal due to the different areas of responsibility. However, by way of illustration, this ratio is 3.6 for the DPCR, considering that the agency operates nine corridor roads with a total length of 532 km and a workforce of 149 employees in 2023.

Setting up a road fund must be a long-term process to ensure its stability. The effectiveness of a road fund is linked to the solidity of its governance system, the transparency of its management, and coordination with the road agency and the Ministry of Transport.

Training is key

The clarification of roles between the functions dedicated to a road agency and those of a road fund requires the presence of a strong Ministry of Transport, which retains all administrative functions. Setting up these governance structures requires prioritizing work, so that resources are allocated in order of priority. All players need to be properly trained, to ensure that staff are as qualified as possible, and to enable coordination between the various players.

Conclusion

A situational analysis highlights three challenges in the road sector which currently prevent efficient public spending in the road sector. The situation raises the strategic question of institutional reform of the road sector, taking into account the simultaneous development of private sector involvement.

The institutional organization of the road sector could be improved, thereby enhancing the efficiency of public spending. A country's ability to manage its road sector well depends on the efficiency with which it can use resources—in other words, efficiency depends on institutional capabilities. In Djibouti, tasks and responsibilities are dispersed among road sector institutions, and decision-making processes are too cumbersome to allow effective coordination. Furthermore, the functions and responsibilities of the main institutions in charge of the road sector overlap. These overlaps need to be eliminated to improve clarity and efficiency.

The current road network is poorly maintained and inadequate. The country does not have a solid fabric of small and medium-sized enterprises and design offices for road maintenance. These shortcomings prevent the road sector from maximizing its role in Djibouti's economic and social development. The development of local small and medium-sized enterprises and design offices would help reduce Djibouti's high road maintenance costs and develop the national economy.

Finally, financing is not sufficiently developed, controlled, or diversified. Financing requirements for investments and road maintenance are high, yet only 21 percent to 23 percent of revenues collected are devoted to road maintenance. Payroll costs are also high, representing 47 percent and 37 percent of total expenditure. The optimization of the institutional structure of the sector would allow for a more efficient use of funds allocated to the road sector. An effective institutional organization is also key to facilitating the mobilization of private financing sources. The private sector could find its place in the Djiboutian road landscape in the form of Performance-Based Road Contracts, as recently introduced by the country, or through Public-Private Partnerships, or eventually, by the increase of companies operating in the sector.

A thorough review of the road sector's players, their responsibilities, and their revenues and expenditure, is needed to identify where efficiency gains are possible. Increasing the efficiency of the road sector's institutional organization could be achieved by improving governance of the sector, clarifying functions and roles, and setting up a road fund and a road agency that act in a coordinated and transparent manner. Strong political will is required to bring these long-term reforms to fruition. Properly implemented, these reforms have the potential to profoundly transform the transport sector for decades to come, ensuring a comparative advantage for Djibouti's ports and enabling the country to benefit from the economic spin-offs associated with quality road infrastructure.

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