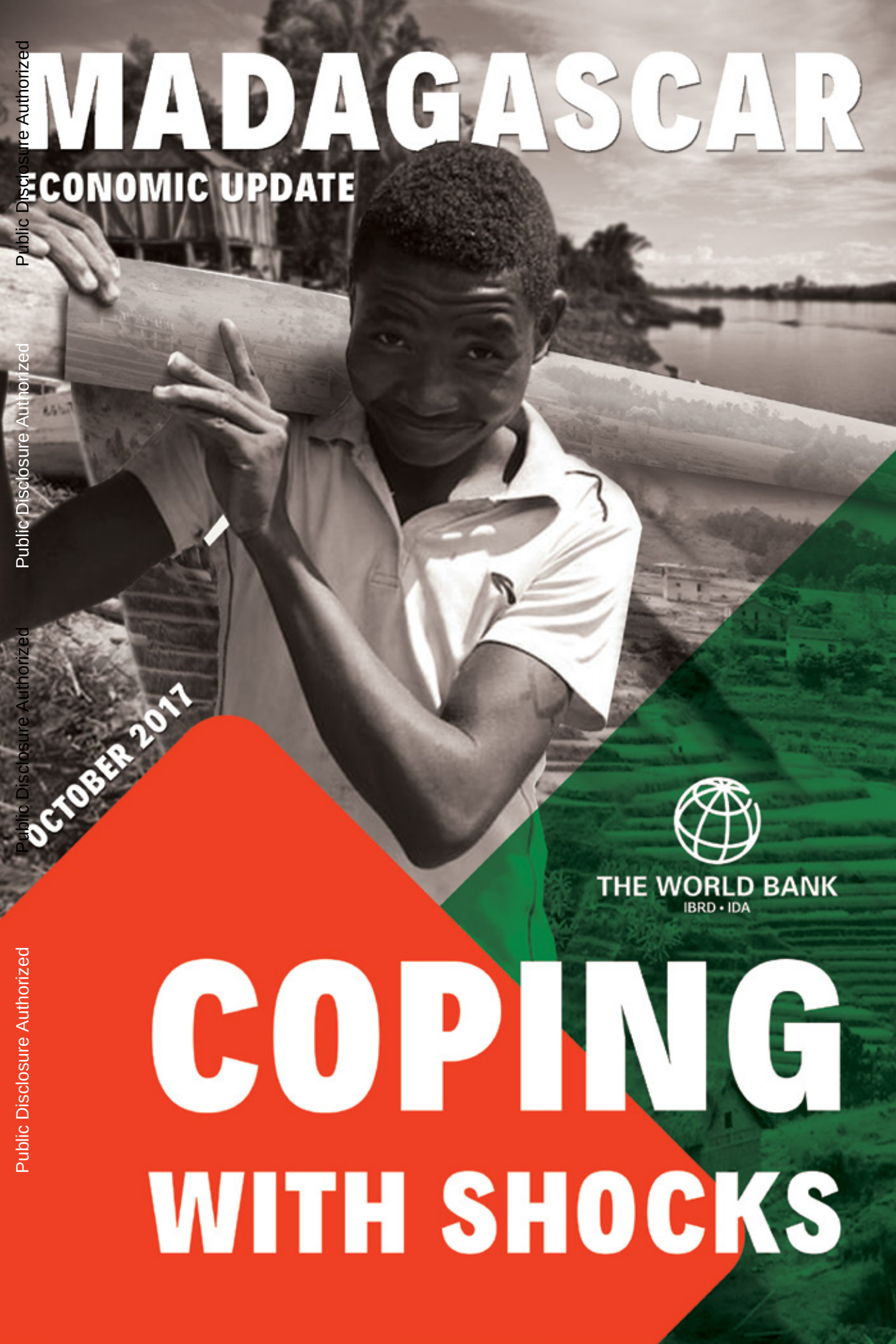
Public Disclosure Authorized
Public Disclosure Authorized
Public Disclosure Authorized
Public Disclosure Authorized

MADAGASCAR

ECONOMIC UPDATE



OCTOBER 2017

THE WORLD BANK
IBRD • IDA

COPING WITH SHOCKS

CONTENTS

Acronyms iv
Foreword v
Acknowledgements vi

Part One: Recent Economic Developments 1
The Real Sector 2
The External Sector 8
Monetary Policy 10
Fiscal Policy 13

Part Two: Economic Outlook 17

Part Three: Assessing Changes to Madagascar's Institutions and Policy Environment 18
The quality of Madagascar's institutions today 21
The potential to further improve the institutional environment 23

References 27

Figure 1 Sectoral contributions to growth by sector (%), 2007– 2017 **2**
Figure 2 Sectoral Distribution of Emergency Relief-Related Expenditure by the Government **5**
Figure 3 Madagascar's production share has been steadily increasing **7**
Figure 4 Vanilla is processed in Europe and N. America **7**
Figure 5 Vanilla prices have surged in recent years **7**
Figure 6 The current account balance is projected to come under pressure in 2017 **8**
Figure 7 Imports of equipment are rising with the scale-up in investments **8**
Figure 8 High vanilla prices and textiles means that exports also continue to perform well **9**
Figure 9 The trade balance in 2017 is running a structural deficit **9**
Figure 10 Levels of international reserves remain adequate **9**
Figure 11 FDI flows are projected to slightly decline **9**
Figure 12 Inflation is on an upward trend, with prices for rice increasing **11**
Figure 13 The Ariary has been appreciating, particularly against the US$ **11**
Figure 14 Lending to the Private Sector is generally stable, while lending to the government has slowed **12**
Figure 15 The increase in the Central Bank's policy rate has resulted in a reduced gap with commercial bank rates **12**
Figure 16 In the first half of 2017, credit has largely been short-term in nature **12**
Figure 17 Tightening of monetary policy has resulted in a more recent reduction of the monetary base **12**
Figure 18 Tax administration reforms are starting to yield higher revenues **13**
Figure 19 Compared to peer countries, tax revenue collection is relatively low **13**
Figure 20 Spending on selected transfers and subsidies is projected to decline **14**
Figure 21 Spending on social priority sectors is expected to increase in the 2017 Revised Budget **14**
Figure 22 Present Value of Debt-to-GDP Ratio **16**
Figure 23 Countries that improve the CPIA score also see advances in their human development index **20**
Figure 24 In general, countries with higher CPIA scores have better regulatory environments for doing business **20**
Figure 25 After a decline during the political crisis period, Madagascar's CPIA score is higher than the average for IDA countries **23**
Figure 26 The quality of Public Sector Management and Institutions indicators worsened between 2008 and 2016 **23**
Figure 27 CPIA score in Madagascar and other countries with same score in 2008 **24**

Table 1 Selected Macroeconomic Data **3**
Table 2 Balance of Payments (in US$ millions) **10**
Table 3 Fiscal Operations of the Central Government (% GDP) **15**
Table 4 CPIA criteria **20**
Table 5 Improvements in selected CPIA criteria **22**
Table 6 Madagascar's CPIA Summary Table **26**

Box 1 Counting the Costs – The Economic Impacts of Cyclone ENAWO **4**
Box 2 What's your flavor? Why vanilla market dynamics are keeping costs high **6**
Box 3 What is the CPIA and how is it used? **20**
Box 4 How Rwanda improved its policies and institutions **24**

ACRONYMS

AfDB	African Development Bank
AGOA	African Growth Opportunity Act
BNGRC	National Bureau for Disaster and Risk Management(Bureau National de Gestion des Risques et Catastrophes)
CBM	Central Bank of Madagascar
CPI	Consumer Price Index
CPIA	Country Policy and Institutional Assessment
DSA	Debt Sustainability Analysis
ECF	Extended Credit Facility
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GNI	Gross National Income
HFA	Hyogo Framework for Action
IDA	International Development Agency
IMF	International Monetary Fund
INSTAT	Madagascar Central Bureau of Statistics (Institut National de la Statistique)
IRM	Immediate Response Mechanism
JIRAMA	State-Owned Electricity and Water Company (Jiro sy Rano Malagasy)
MFB	Ministry of Finance and Budget
DRM	Disaster Risk Management
PPG	Public and Publicly Guaranteed
PV	Present Value
SOEs	State Owned Enterprises
SSA	Sub-Saharan Africa
USAID	United States Agency for International Development
WB	World Bank
WDI	World Development Indicators

FOREWORD

We are pleased to share the latest edition of the Madagascar Economic Update, which reports up to the beginning of October 2017, and provides our economic outlook for the medium-term. Despite a challenging start due to two climatic shocks, we project growth at 4.1 percent in 2017, a continuation of the positive trend from last year. Key growth drivers in 2017 are expected to remain as services-related activities, construction works to partly support the reconstruction efforts from the natural disasters, and strong demand for Malagasy textiles from abroad.

The severe drought in the first few months of the year affected agricultural activities and reduced hydroelectric power supply. Output for key staples such as rice fell, contributing to higher inflation and an increase in food imports. And in March 2017, Madagascar experienced its most severe cyclone in 13 years, where losses were estimated at US$ 400 million, equivalent to approximately 4 percent of GDP.

These weather events have highlighted again Madagascar's vulnerability to climatic shocks as well as its ability to act swiftly when disasters strike. The Central Bank has continued to control inflation by tightening liquidity operations and increasing the policy rate. The budget has been recast to incorporate emergency-related spending.

In this edition's Special Focus Section, we discuss how Madagascar's institutional environment is evolving, which the World Bank measures through the Country Policy and Institutional Assessment. We are pleased to share that since the return to constitutional order in 2014, we have noted a gradual improvement in the quality of Malagasy institutions, notably in the areas of social protection and budgetary management.

This improvement to the institutional environment is critical given the opportunities and challenges that lie ahead. Following a successful Donors and Investors Conference in December 2016, US$6.4 billion was pledged by development partners for the 2017-2020 period, including US$2.1 billion of undisbursed commitments and US$4.3 billion in new commitments. The private sector also announced US$3.5 billion worth of investment projects. In total, external financing is expected to increase to an annual average of 16.7 percent of GDP over 2017-2021, assuming a steady scale-up. Building strong institutions is key for ensuring these resources are used well.

We maintain a positive medium-term growth outlook, provided that the momentum for implementing key reforms continues. In particular, efforts should continue to focus on improving the performance of state-owned enterprises, which pose a significant drain on public resources, strengthening the business environment, and curbing corruption.

We hope that you enjoy reading this edition of the Economic Update.

Coralie Gevers
Country Manager, Madagascar and Comoros
World Bank

ACKNOWLEDGEMENTS

This edition of the Madagascar Economic Update was prepared by a team led by Natasha Sharma (Senior Economist, GMF13). The team included Faniry Razafimanantsoa (Economist, GMF13) and lead author of the special focus section on the evolution of Malagasy institutions, Prisca Mamitiana (Consultant, GMF13), and Bonde Raharinoasy (Team Assistant, AFMMG). The discussion on the economic losses from tropical cyclone ENAWO is based on a paper led by Michel Matera (Senior Urban and Disaster Risk Management Specialist, GSU13).

The team is grateful for the support provided by Carolin Geginat (Program Leader, AFCS2). The team is thankful to Christian Yves Gonzalez (OPSCE) for reviewing the special focus section. The report was prepared under the overall guidance and supervision of Mark Lundell (Country Director, AFCS2), Coralie Gevers (Country Manager, AFCS2) and Mathew Verghis (Practice Manager, GMF13). The team would also like to express gratitude to Norosoa Rakotomena for translation activities, Cybil Maradza for design work and Dia Styvanley (AFREC) for communications support.

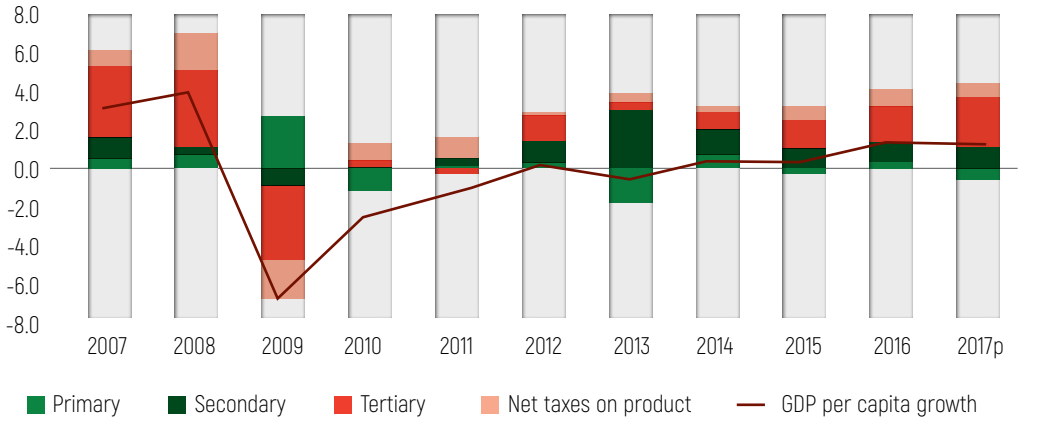
PART ONE

RECENT ECONOMIC DEVELOPMENTS

The Real Sector

1. Economic growth in 2017 is estimated at 4.1 percent despite two natural disasters. This growth rate follows the same trend as 2016. The current growth is favorable in comparison with the average for the last ten years up to 2016, which includes the political crisis period 2009-13, when real GDP expanded by 2.7 percent a year on average. The most important growth driver is the tertiary sector, supported by public works and related activities such as trade, services and transport. The expansion of public works activities partly reflects emergency construction works in response to the severe grade 4 cyclone ENAWO that hit Madagascar in March 2017. The secondary sector is expected to continue expanding, as textiles exports are forecast to remain strong following the reinstatement of eligibility to the African Growth and Opportunities Act (AGOA).[1] However, agricultural activities are expected to contract by nearly 6 percent, following the effects of the cyclone.

F1 **Figure 1: Sectoral contributions to growth by sector (%), 2007 - 2017**



Source: National Institute of Statistics and World Bank staff calculations, June 2017

2. These recent economic developments are expected to put GDP per capita growth on a positive trajectory. GDP per capita growth is estimated at 1.3 percent in 2017, and is expected to increase over the medium-term, suggesting that economic growth is keeping up with population growth. However, the contraction in the agricultural sector may contribute to an increase in the depth of poverty as consumption levels decline for those who are already poor. The Government is pursuing an expansionary fiscal policy to support the planned scale-up in public investments, which explains the expected deficit of the current account balance. A summary of selected macroeconomic data is provided in Table 1.

Growth continues a **positive trend** in 2017

[1] AGOA is a United States Trade Act that enhances market access for countries in SSA, which improve the rule of law, human rights, and respect for core labor standards. Madagascar lost AGOA eligibility in 2009 following the political crisis and regained it in 2014 after the return to constitutional order.

T1 **Table 1:** Selected Macroeconomic Data

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	Actuals			Est	Projections					
Real sector										
GDP (billions of ariary)	23,397	25,775	28,585	31,769	35,751	40,493	45,653	51,042	56,633	62,571
Real GDP growth	2.3	3.3	3.1	4.2	4.1	5.1	5.6	5.4	5.2	5.0
GDP per capita (USD)	462.5	452.8	402.1	401.4	447.6	479.0	501.2	525.4	548.1	569.0
GDP per capita growth	-0.5	0.5	0.3	1.4	1.3	2.3	2.8	2.6	2.4	2.2
Unemployement rate (ILO definition)	1.3	1.4	1.8	2.1	...	...	...	...	...	...
GDP deflator (annual % change)	5.1	6.6	7.6	6.7	8.1	7.8	6.8	6.1	5.5	5.2
Inflation, consumer prices (annual %, end of year)	6.3	6.0	7.6	7.0	8.0	7.9	6.2	5.7	5.4	5.0
Public Finance (%GDP)										
Revenues, excluding Grants	9.6	10.1	10.4	11.2	11.7	12.1	12.1	12.5	13.0	13.3
o/w: Tax Revenues	9.3	9.9	10.1	10.9	11.4	11.9	11.9	12.3	12.8	13.1
Grants	1.3	2.3	1.5	3.5	3.2	3.0	3.1	1.9	1.8	1.6
Total spending (commitment basis)	14.9	14.7	15.1	16.0	18.4	18.0	20.2	19.6	19.3	19.0
o/w: Capital spending	3.1	3.9	3.5	5.2	6.3	8.1	10.5	10.2	9.8	9.1
Overall balance (cash basis)	-2.0	-2.4	-3.7	-2.0	-4.3	-3.5	-5.2	-5.3	-4.7	-4.1
Total public debt	33.9	34.7	41.3	38.4	36.2	36.2	37.2	39.8	41.9	43.4
Monetary accounts (annual % change)										
Money Supply (M2)	9.0	9.8	15.8	21.4	18.5	13.1	15.0	16.1	16.4	14.7
Net Foreign Assets	-12.7	17.3	20.9	37.4	10.9	12.9	14.9	16.2	16.7	13.0
Net Domestic Assets	8.0	8.3	11.4	10.8	22.9	12.2	13.3	14.0	14.4	14.3
o/w: Credit to the Private Sector	16.7	18.4	16.5	8.2	12.8	16.9	15.1	14.7	14.4	14.0
External sector (%GDP)										
Exports of goods	18.1	20.6	21.0	21.6	20.8	20.2	20.7	21.5	22.2	22.6
Imports of goods	30.7	30.2	28.7	28.6	31.0	30.1	31.3	31.7	31.9	32.2
Current account balance	-5.9	-0.3	-1.9	0.6	-3.4	-4.1	-4.3	-4.1	-4.3	-4.4
Foreign Direct Investment	5.2	2.9	4.5	4.5	3.6	3.4	3.4	3.4	3.4	3.5
Overall Balance	0.7	0.2	1.0	2.9	0.8	0.6	1.0	1.3	1.4	1.1
Foreign Reserves (months of imports)	2.2	2.5	2.9	3.9	3.7	4.0	4.2	4.3	4.4	4.4
External debt	43.8	45.0	48.6	45.4	45.3	45.6	45.7	44.9	44.0	43.1
Terms of Trade (percent change)	-0.1	-0.7	1.2	23.2	-6.9	2.5	-3.1	0.3	-0.9	-0.8
Exchange Rate LCU/USD(average)	2,207	2,415	2,934	3177						

Source: Malagasy authorities, IMF and WB Staff calculations, October 2017

3. The economy has been affected by two major natural disasters in 2017. Madagascar suffered from a serious drought in late 2016 and early 2017, affecting an estimated 1.14 million people. Agricultural activities suffered, where rice output, the country's main staple, is estimated to have fallen by 20 percent. Hydroelectric power supply was also affected and the electricity and water state-owned enterprise, JIRAMA, needed higher subsidies. The worst cyclone in 13 years hit Madagascar in March 2017, imposing costs estimated at US$400 million (around 4 percent of GDP), of which approximately one-third fell on the public sector and two-thirds on households and the private sector. The economic costs of Cyclone ENAWO are discussed in Box 1.

B1 Box 1: Counting the Costs – The Economic Impacts of Cyclone ENAWO

Madagascar is vulnerable to natural hazards and has the greatest exposures to cyclones in Africa.[2] Between 1982 and 2015, over 2,200 disasters were recorded in Madagascar, including cyclones, flooding, and droughts. A probabilistic assessment of Madagascar's disaster risks estimates that the annual average cost of damages from weather shocks, just on infrastructure alone exceeds US$100 million per year[3] of which US$87 million is the impact from cyclones, largely due to strong winds.

**In March 2017, cyclone ENAWO hit Madagascar, imposing costs estimated at US$400 million.**[4] Cyclone ENAWO was the strongest of its kind in 13 years, and is estimated to have impacted over 295,000 people in 58 out of 114 districts. Over 83,100 houses were damaged, 3,900 classrooms destroyed and 1,300 water points polluted.[5] By using a quantitative risk modelling approach, it was possible to estimate losses resulting from direct damages to buildings and infrastructure to be around US$ 200 million. An agriculture sector model was developed to assess agricultural losses, which were estimated at US$207 million, largely due to the destruction of vanilla plantations worth US$164 million.

The North-Eastern part of Madagascar was the most affected region. The cyclone has been felt differently in each region. In the North-Eastern part of the country, damages resulted mainly from strong winds reaching up to 230km/hour and flooding. While the strength of the wind abated as the cyclone crossed the island, the abundant rainfall caused floods all over the country. In some of the communities located in the North, half of all houses have been destroyed. It is estimated that one third of vanilla production has been ruined, also contributing to recent price dynamics (see Box 2).

The authorities recast the 2017 budget to help offset the damage from the recent shocks. The cyclone hit Madagascar whilst the country was still responding to the effects of the El Niño related drought in the South of the country. In response to these two major natural disasters, the Government approved a revised budget law in June 2017 to include an additional US$50 million for reconstruction efforts. Of this, US$35 million was channeled for emergency relief-related expenditures, targeted to different sectors (Figure 2). Following ENAWO, the budget transfer for the National Bureau for Disaster and Risk Management was increased by US$ 2 million. The World Bank also activated the IDA Immediate Response Mechanism (IRM) for an amount of US$ 13 million.[6]

[2] USAID (2016). Risk Profile of Climatic Change in Madagascar

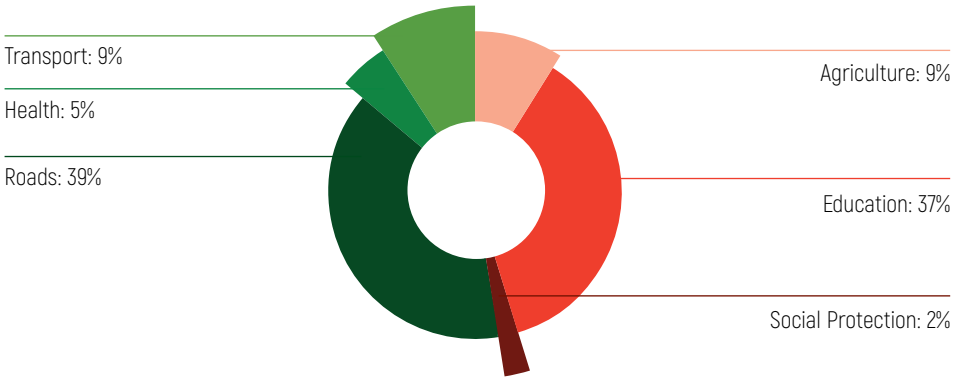
[3] Madagascar Disaster Risk Profile, SWIO-RAFI, GFDRR and World Bank (2016)

[4] Estimation of economic losses from Tropical Cyclone Enawo, World Bank (2017)

[5] Madagascar: Cyclone Enawo. Situation report No.2, National Bureau for Risks and Disasters Management and United Nations Office for Disaster Risk Reduction (2017)

[6] The Immediate Response Mechanism allows IDA countries to rapidly access up to 5 percent of their undisbursed IDA investment project balances following a crisis. The Immediate Response Mechanism (IRM) complements longer-term emergency response tools available to IDA countries, such as the Crisis Response Window, offering them financial support within weeks rather than months of an emergency.

F2 **Figure 2: Sectoral Distribution of Emergency Relief-Related Expenditure by the Government**



Source: MFB

Madagascar has a well-established institutional framework for managing natural disasters, as evidenced in the preparation for ENAWO. The management and mitigation of disaster risks is one of the key components of the National Development Strategy. Building on the lessons learned over the past years, the National Disaster Risk Management (DRM) Policy was updated in 2016, followed by the elaboration of the National DRM Strategy 2016-2030, which emphasizes prevention and mitigation measures. As the country prepared for ENAWO, an early warning system was activated, with regular communication through different channels. The National Weather Services (*Direction Générale de la Météorologie*) also provided regular updates on the trajectory of ENAWO.

Nevertheless, there is significant scope to further strengthen the institutional framework for disaster risk management. Madagascar is making progress to improve its institutional framework in line with the Sendai Framework for Disaster Risk reduction 2015-2030, which specifies the work that is required from different sectors and actors to reduce disaster losses. The previously used Hyogo Framework for Action (HFA) 2015 National Progress Report pointed to several areas requiring improvement such as: (i) technical capacity; (ii) financing of recovery schemes and social safety nets for resilience; (iii) mainstreaming disasters risks reduction in public investment management; and (iv) establishment of emergency funds to support response, recovery and preparedness measures. Strengthening these areas is important given that Madagascar's exposure to natural disasters is on an upward trend: episodes of cyclones, flooding and drought have increased three-fold in the last 20 years.[7]

Source: Estimation of Economic Losses from Tropical Cyclone ENAWO, World Bank, March 2017

4. The agricultural sector continues to be characterized by vulnerability to climatic conditions and low levels of productivity. Following the effects of the drought in the first half of 2017 and cyclone ENAWO, growth of the agricultural sector is expected to slow down by almost 6 percent compared with the previous year. The severity of the climatic effects on agricultural contribution to growth has been partly offset by the surge in vanilla prices (Box 2). Nevertheless, despite engaging approximately 80 percent of the population, low productivity and unfavorable climatic conditions jeopardize food security. However, cattle, fishing and forestry are expected to grow compared with the previous year, where the latter is also expected to positively contribute to GDP growth.

5. Industrial production is expected to continue to pick up in 2017, driven by growth in industrial processing zones and agro-industry. In 2017, industrial processing zones are expected to grow by 13 percent, largely reflecting the increase in textiles exports, which is supported by stronger

[7] USAID (2016). Risk Profile of Climatic Change in Madagascar

growth in Madagascar's main trading partners, France and the United States. In the first six months of 2017, earnings from exports to France was already two thirds of total earnings in 2016; and export earnings to the United States from January to June 2017 was nearly equivalent to the total value in 2016. Agro-industry is also expected to grow by 10 percent, largely due to sugar processing. A more buoyant growth of 9.5 percent is expected in the extractive industries, as nickel prices improve slightly. Looking ahead, there is significant potential for the mining sector to contribute further to growth as nickel prices are projected to grow over the medium-term, with anticipated increase in demand from China.[8]

6. Services related activities are expected to be on an upward trend in 2017. Construction related activities are expected to increase by 10.5 percent compared with 2016, reflecting a scale-up of both public and private investment. Transport related services are also expanding particularly for goods and travel related services. Data for the first semester of this year indicate a 4.1 percent rise in the number of foreign visitors to Madagascar, compared with the same period last year. Other services such as trade, banking and telecommunications are also expected to increase, indicating a rise in private sector related activities.

B2 **Box 2: What's your flavor? Why vanilla market dynamics are keeping costs high**

Vanilla prices are soaring, by an estimated 240 percent between 2015 and 2016. At an average price of around US$400 per kilo,[9] vanilla is the second most expensive spice trading on the global market, after saffron.[10] Vanilla is used by large food processing firms and industries as a key ingredient for various products, including beverages, food, and pharmaceuticals. But the cost of vanilla has been sky rocketing, from around US$73 a kilo in 2015 to over US$250 a kilo in 2016.

Madagascar is the world's leading vanilla producer. Between 2005 and 2014, annual world vanilla production almost doubled from 4,900 tons to 8,500 tons. Madagascar is the world's major producer, accounting for nearly half of global output in 2014. This market dominance is likely to continue since vanilla production requires specific climatic conditions and is extremely labor-intensive.

Vanilla is processed outside of Madagascar, where the behavior of intermediaries is affecting supply and pushing up prices. Madagascar exports vanilla pods, which are processed by firms, primarily based in France, Germany, and Canada. There is limited market information on prices, producers and suppliers across the value chain. Taking advantage of this opaqueness, 'intermediaries' working for large processing firms are reported to be hoarding vanilla, to reduce supply and obtain more favorable prices.

Global supply has been further suppressed by adverse climatic conditions. Since 2015 higher vanilla prices have encouraged new cultivators in Madagascar, but there has been insufficient time for crops to harvest given that two to five years are needed for orchids to bloom. Cyclone ENAWO is estimated to have destroyed 15 percent of vanilla crops, putting pressure on world production.

Despite high prices, global demand for vanilla remains strong. As vanilla prices fell around the mid-2000s, manufacturers increasingly used vanilla in product development for high end goods. This decision proved popular amongst consumers and led to some giant food companies abandoning the use of artificial vanillin flavor, despite trading at a far more competitive US$10-20 per kilo.

The effects of higher vanilla prices on the Malagasy economy have been mixed. Strong vanilla prices have contributed to favorable export earnings. Once poor farmers have become rapidly wealthy, although insecurity in producing areas has mounted. However, the price surge has amounted to an economic shock that is being carefully managed. Since vanilla cultivators largely operate outside of the banking network, currency in circulation has soared, contributing to inflationary effects. The appreciation of the Ariary has coincided with the start of the vanilla export season, and the generation of higher export earnings. The Central Bank is responding to these effects through managing liquidity operations.

The price surge is expected to last in the short term. While vanilla prices have increased, major manufacturers

[8] Commodity Markets Outlook, World Bank, April 2017

[9] Average export price in July 2017 as reported by the Malagasy Customs

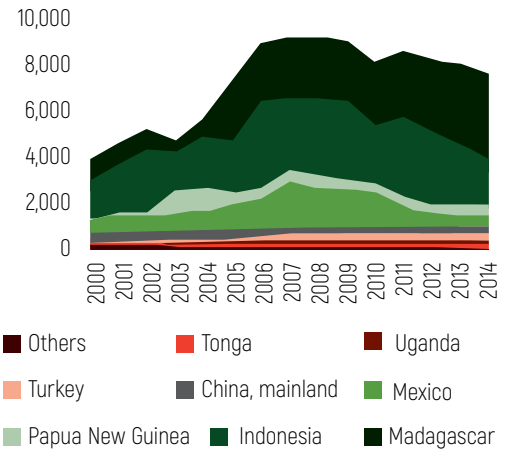
[10] The price for saffron can exceed US$10,000 per kilo.

have expressed commitment to keep using natural vanilla, reflecting consumer preferences. Activities of intermediaries are likely to continue contributing to high prices, at least until all stocks that are being purchased at a high price are sold.

Over the medium-term, downward pressures are expected to weigh in. The last time there was a vanilla price hike, from 2002 to 2004, the market experienced a dramatic drop, where prices fell to the tune of 45 percent. While large firms continue to express a commitment to using vanilla, the high prices are unlikely to be sustained. Firms are increasingly marketing alternative high end products with natural flavors. New cultivators that started planting in 2015 are likely to contribute to improved supply, although this will inevitably take time to bear fruit.

F3 **Figure 3: Madagascar's production share has been steadily increasing**

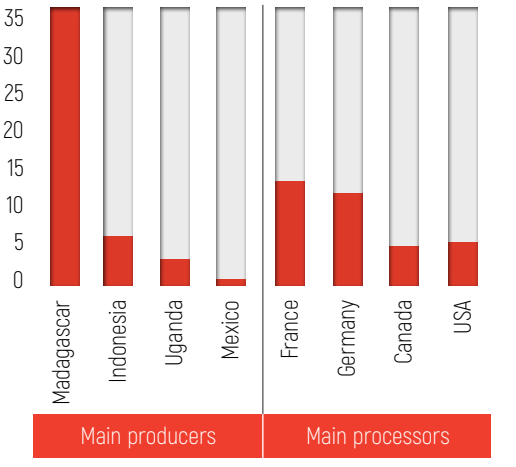
Vanilla production (tons)



Source: FAOStats

F4 **Figure 4: Vanilla is processed in Europe and N. America**

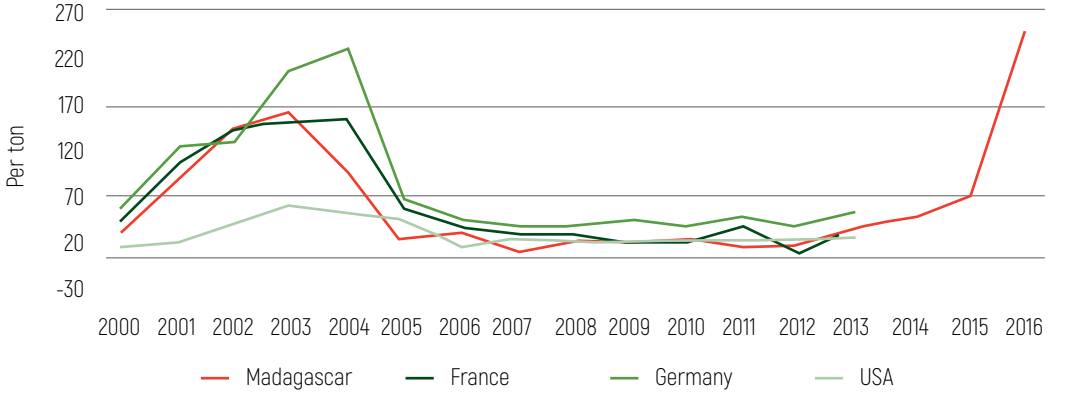
Vanilla export average between 2000-2013 (in %of US$ nominal value of World export)



Source: FAOStats

F5 **Figure 5: Vanilla prices have surged in recent years**

Vanilla prices in US$1000 (2000 base year)



Source: Madagascar Customs Directorate, FAOSTAT[11]

[11] Data are available up to 2013 for France, Germany, and the USA..

The External Sector

7. The projected scaling-up of investment is expected to weaken the current account balance.[12] Madagascar runs a structural current account deficit, but 2016 was an exception, with the current account recording a small surplus of 0.6 percent of GDP, reflecting an increase in vanilla export prices, higher textile exports, and a decline in mining-related imports. Going forward, the current account balance is expected to fall back into deficit, at around 3.4 percent of GDP in 2017. The current account deficit is primarily expected to be financed by external financing of public sector investment and foreign direct investment.

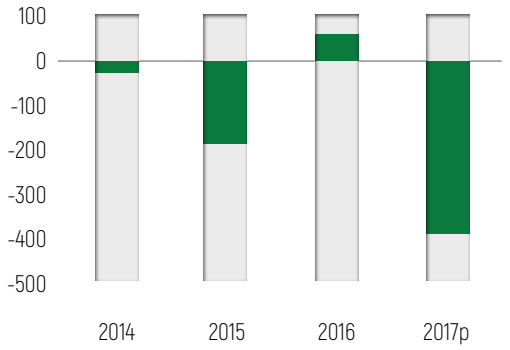
8. Even though exports continue to perform well, the rise in imports is leading to a trade deficit[13](Figure 9). Exports continue to perform well, mainly due to extraordinarily high vanilla prices and a well-performing textiles industry (Figure 8). However, as expected, the value of imports is rising to support the scale-up of public investment activities, which is projected to increase from 5.2 percent of GDP in 2016 to 10.5 percent of GDP in 2019. Notably, the value of equipment imported by the end of September 2017 is equal to the total value in 2016. While the total value of rice imports continues to be small relative to total imports, the value of rice imports in the first few months of 2017 have exceeded the total value of rice imports in 2016, as domestic production was affected by the severe drought (Figure 7).

Rice imports have surged as domestic production has **fallen**

9. Levels of international reserves remain adequate. The spike in vanilla prices led to unbanked vanilla producers holding significant amounts of currency outside of the formal banking network, which drained liquidity. In response, the Central Bank purchased foreign currency to increase bank liquidity and meet the demand for local currency. Official reserves rose close to four months of import cover at end-2016. While reserves are likely to reduce to the equivalent of 3.7 months of imports in 2017, the level remains reasonable (Figure 10).

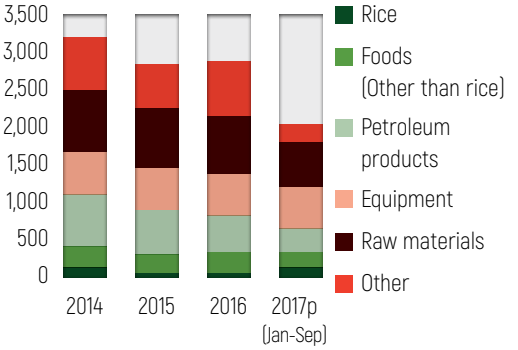
F6 **Figure 6: The current account balance is projected to come under pressure in 2017**

Current account balance, 2014-17 (USD millions)



F7 **Figure 7: Imports of equipment are rising with the scale-up in investments**

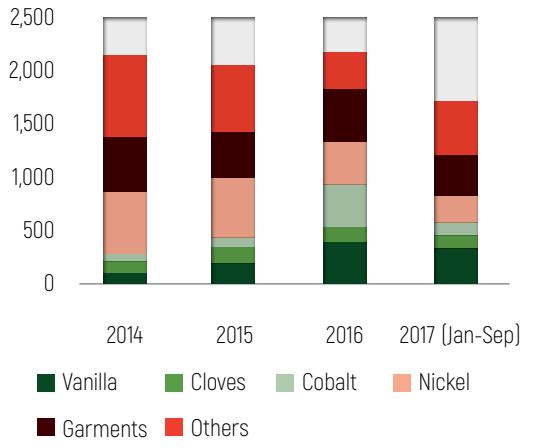
Goods imports, 2014-2017 (USD millions)



[12] The *current* account is the trade balance plus the net amount received for domestically-owned factors of production used abroad.
[13] The *trade* balance has a narrower definition than the current account balance and refers to the amount a country receives for the export of goods and services minus the amount it pays for its import of goods and services.

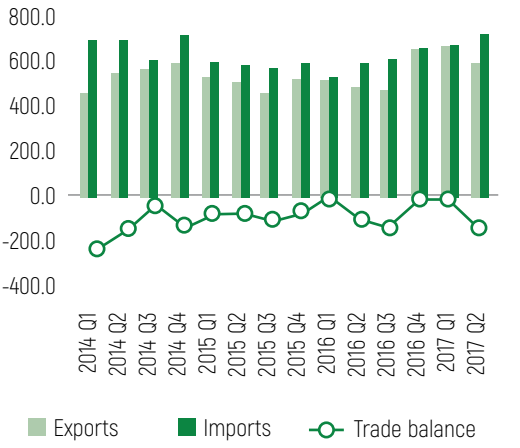
F8 Figure 8: High vanilla prices and textiles means that exports also continue to perform well

Goods exports, 2014-17 (USD millions)



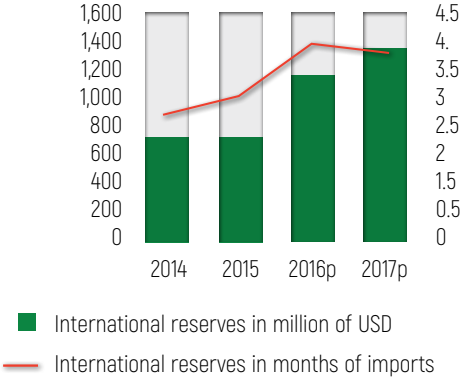
F9 Figure 9: The trade balance in 2017 is running a structural deficit

Exports and imports, 2014-17 (USD millions)



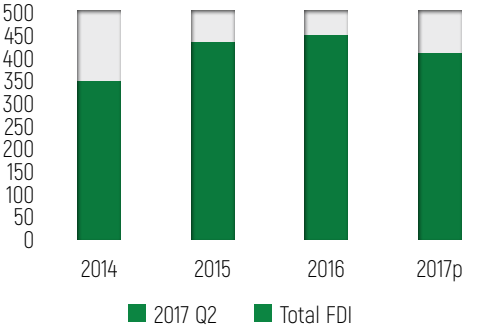
F10 Figure 10: Levels of international reserves remain adequate

2014 - 17 (US$ millions) and reserves in months of imports



F11 Figure 11: FDI flows are projected to slightly decline

(USD millions)



Source: MFB, CBM, IMF and World Bank staff

T2 **Table 2: Balance of Payments (in US$ millions)**[14]

	2014	2015	2016	2017 (Jan-Jun)
1 – Current transactions	-33.6	-184.1	75.1	17.8
1.1 Goods and services	-467.7	-337.9	-208.3	-107.6
o/w Trade balance	-546.7	-328.9	-264.3	-145.0
Exports FOB	2194.3	2047.0	2165.1	1270.0
Imports FOB	-2741.0	-2375.8	-2429.4	-1415.0
Services nets	78.9	-9.0	56.1	37.4
1.2 Income	-299.2	-376.1	-407.7	-173.5
1.3 Current transfers	733.3	529.9	691.2	298.9
2 – Capital and financial account	56.0	283.9	218.1	-79.5
2.1 Capital account	158.0	130.3	272.3	67.5
2.2 Financial account	-84.7	120.6	-13.1	-147.0
2.3 Errors and omissions	-17.3	33.0	-41.2	-10.1
3 – Overall balance	22.4	99.8	293.2	-71.7

Source: CBM, IMF and WB staff estimates

Monetary Policy

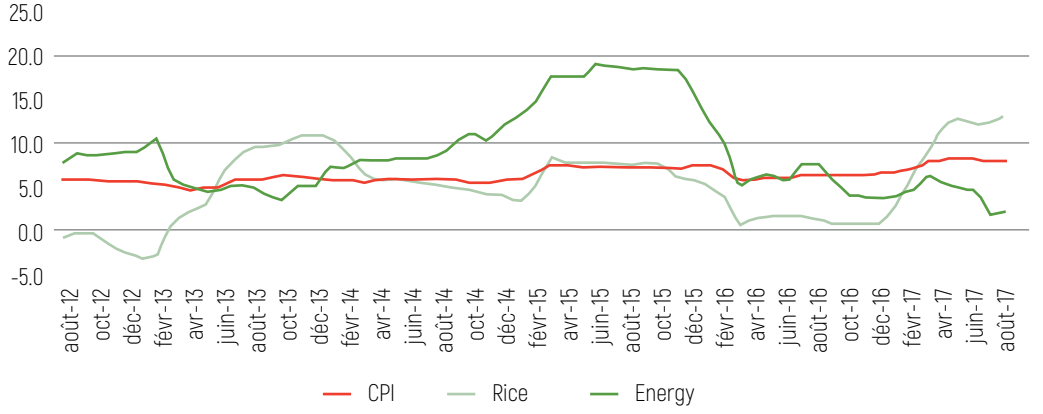
10. Inflation has increased but remains under control. Inflation accelerated from 7.0 percent at end-2016 to a peak of 8.6 percent in May 2017, with food (especially rice) and housing (rents) as main drivers, and then started to decelerate reaching 8.2 percent in August 2017. The Central Bank reacted by tightening monetary policy and by raising the policy rate from 8.3 to 9 percent in May 2017, the highest level since October 2015.

11. The Ariary has been appreciating (Figure 13). From January to September 2017, the Ariary depreciated in nominal terms by 2.4 percent against the Euro and appreciated by 9.5 percent against the US dollar, although there was a slight moderation since August. The appreciation of the Ariary may affect the competitiveness of Malagasy exports, although international demand for vanilla remains strong. Notably, the appreciation in the Ariary coincides with the production of the vanilla production season in May and June of 2017, where the increase in foreign exchange earnings is likely to have contributed to the volatility of the exchange rate.

[14] FOB refers to 'free on board,' a trade term that indicates whether the seller or the buyer has liability for goods that are damaged or destroyed during shipment between the two parties.

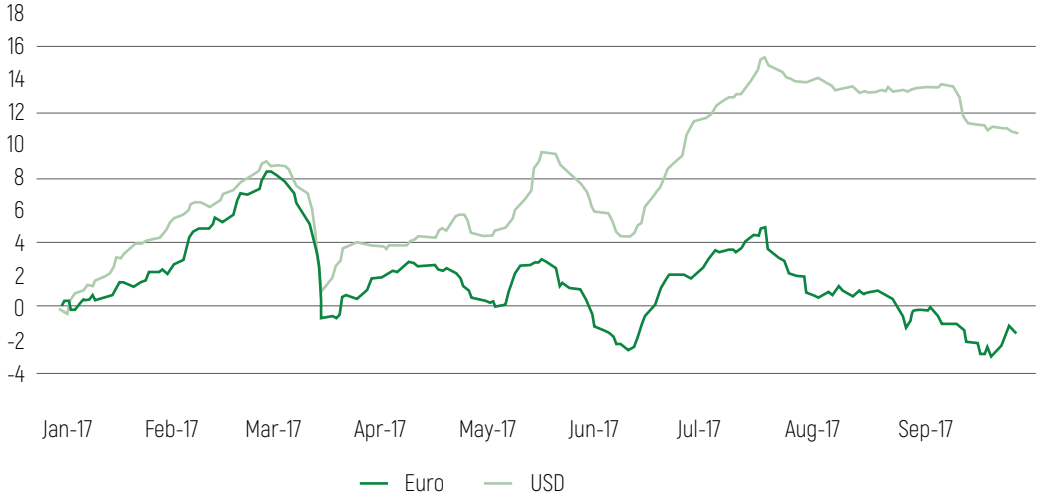
F12 **Figure 12: Inflation is on an upward trend, with prices for rice increasing**

Consumer Price Indices (Annual variation in percentage)



F13 **Figure 13: The Ariary has been appreciating, particularly against the US$**

Percentage change in the exchange rate since January 2017

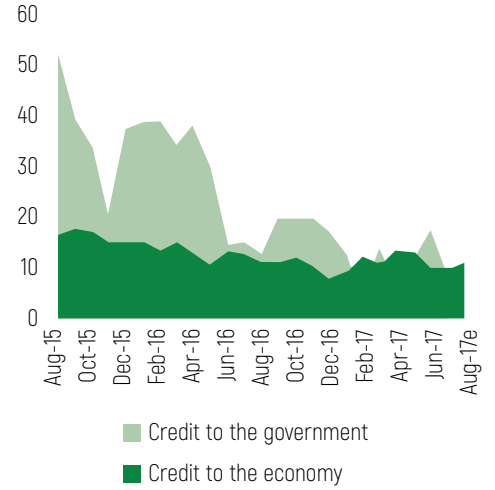


Source: INSTAT, the CBM and WB staff calculations

12. Lending to the private sector has generally been stable. In the first half of 2017, lending activities to the economy were generally stable, while lending to the Government declined (Figure 14). Available data for 2017 shows that loans are generally short term in nature (Figure 16). Interest rates offered by major banks continue to be considerably higher than the Central Bank's policy rate (Figure 15). Several factors influence commercial banking rates including risk levels, cost of operations and cost of financing.

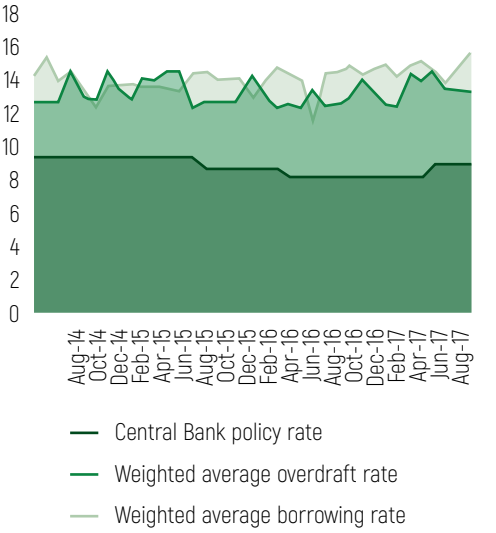
F14 Figure 14: Lending to the Private Sector is generally stable, while lending to the government has slowed

Annual variation in percentage



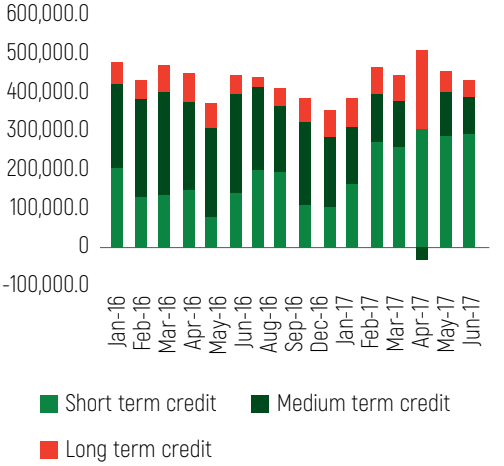
F15 Figure 15: The increase in the Central Bank's policy rate has resulted in a reduced gap with commercial bank rates

Percentage



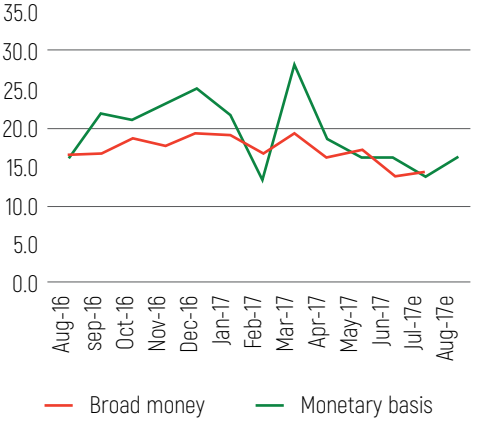
F16 Figure 16: In the first half of 2017, credit has largely been short-term in nature

Annual variation (Millions of MGA)



F17 Figure 17: Tightening of monetary policy has resulted in a more recent reduction of the monetary base

Percentage change [15]



Source: CBM

[15] Broad money is a measure of money supply that includes more than just physical money such as currency and coins but also demand deposits at commercial banks, and any monies held in easily accessible accounts.

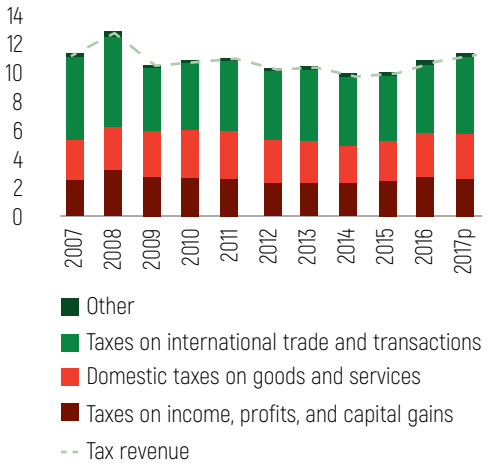
Fiscal Policy

13. In June 2017, the authorities recast the budget as spending priorities changed in light of the recent shocks to the economy. Total revenues and grants are projected to increase from 13.9 percent of GDP in the original budget law to 15.2 percent of GDP in the revised one. However, most recent estimations suggest that total revenues and grants will reach 15.0 percent of GDP 2017. The revised budget law increases expenditures from 18.3 percent of GDP to 20.3 percent of GDP, although updated estimations suggest expenditures will reach 18.4 percent of GDP. The current estimates reflect the slower than expected disbursement of external financing of capital expenditures (grants and loans). Overall, the fiscal deficit is now projected at 4.3 percent of GDP, up from 2 percent of GDP in 2016.[16]

14. The higher resource envelope presented in the revised budget partly reflects progress in implementing tax administration reforms. Madagascar's tax revenues are among the lowest in the world as a share of GDP, estimated at 10.9 percent of GDP in 2016, well below the 16.8 percent average for Sub-Saharan Africa (SSA) (Figure 19). However, there have been improvements. Between 2015 and 2016 tax revenues increased by 0.5 percent of GDP and are expected to reach 11.4 percent of GDP in 2017 (Figure 18). These reforms are largely due to the reinforcement of controls, and greater collaboration between tax and customs directorates.

F18 **Figure 18: Tax administration reforms are starting to yield higher revenues**

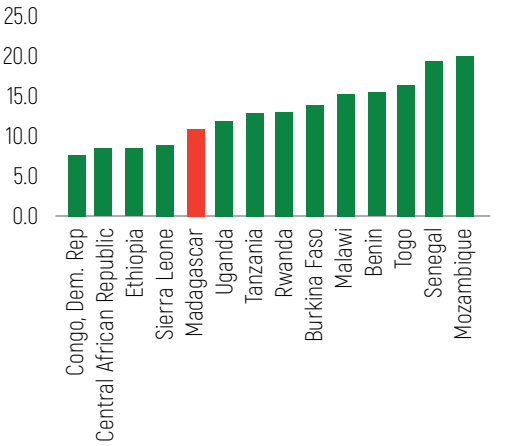
Tax as a percentage of GDP



Source: MFB

F19 **Figure 19: Compared to peer countries, tax revenue collection is relatively low**

Tax as a percentage of GDP (average 2004-2014)



Source: World Development Indicators

15. Higher expenditures in the revised budget are in part driven by one-off transfers to state-owned enterprises. Current expenditures are expected to increase from 10.8 percent of GDP in 2016 to 12.2 percent of GDP in 2017. This rise in current spending is largely driven by higher transfers to state-owned enterprises. The subsidy to JIRAMA increased from US$74 million to US$133 million, as the drought affected hydro-generation capabilities and resulted in JIRAMA purchasing more expensive diesel to run generators. A one-off transfer to Air Madagascar (the under-performing national airlines company) was approved, to the tune of US$89 million, to cover debt obligations as part of restructuring efforts to improve operational performance. Both these large state-owned enterprises are implementing governance reforms, which are expected to result in a significant reduction in transfers over the medium-term. In addition, the Government is making efforts to reduce other selected transfers, notably to the Pension Fund and the continued elimination of fuel subsidies (Figure 20). These efforts to improve the composition of public spending is expected to result in higher spending on social priority sectors (Figure 21).

[16] The financing deficit is calculated on a cash basis and considers the Government's float and arrears repayments.

Figure 20: Spending on selected transfers and subsidies is projected to decline

Selected transfers and subsidies as a percentage of total expenditures and net lending[17]

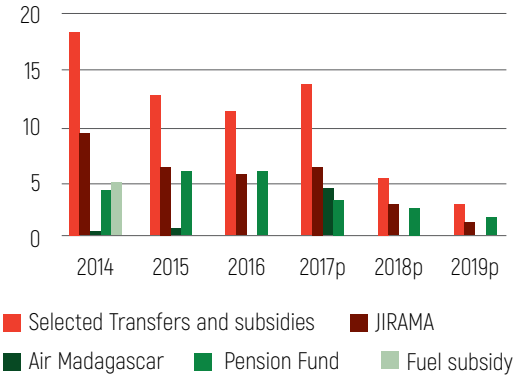
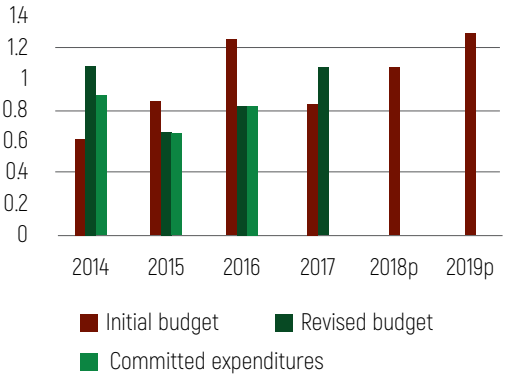


Figure 21: Spending on social priority sectors is expected to increase in the 2017 Revised Budget[18]

Percentage of GDP



Source: MFB, IMF projections

Capital expenditures have **increased** in response to the damage from the cyclone

16. Capital expenditures are projected to increase, largely to respond to the shocks. Capital expenditures are expected to increase from 5.2 percent of GDP in 2016 to 6.3 percent of GDP in 2017. This increase is largely underpinned by higher foreign financing as the government secured exceptional financing from partners to help finance the costs of the natural disasters. Domestically financed capital expenditures are also expected to increase from 1.2 percent of GDP in 2016 to 2.0 percent in 2017. Part of these resources will be channeled to new projects for emergency related expenditures in sectors such as water, roads, transport, agriculture, social protection, health and education.

[17] Selected transfers and subsidies are those destined for JIRAMA, Air Madagascar, the Pension Fund and fuel subsidies.

[18] Social priority expenditures are defined as spending on health, education, water and population sectors excluding salaries and externally financed investments.

T3 **Table 3: Fiscal Operations of the Central Government (% GDP)**

% GDP	2014 Actuals	2015 Actuals	2016 Estimates	2017 Initial Budget Law (LFI)	2017 Revised Budget Law (LFR)	2017 Current projection (Oct 2017)
Total revenue and grants	12.4	11.8	14.7	13.9	15.2	15.0
Total revenue	10.1	10.4	11.2	11.2	11.6	11.7
Tax revenue	9.9	10.1	10.9	11.0	11.4	11.4
Non-tax revenue	0.2	0.3	0.3	0.2	0.2	0.3
Grants	2.3	1.5	3.4	2.7	3.5	3.2
Total expenditure	14.7	15.1	16.0	18.3	20.3	18.4
Current expenditure	10.8	11.7	10.8	10.3	12.0	12.2
Wages and salaries	5.6	5.5	5.6	5.6	5.5	5.8
Interest payments	0.6	0.8	0.9	0.9	0.9	0.8
Goods and services	0.9	0.5	0.6	0.8	0.9	0.9
Transfers and subsidies	3.2	3.4	3.1	2.7	4.0	4.0
Treasury operations (net)	0.6	1.4	0.6	0.2	0.6	0.6
Capital expenditure	3.9	3.5	5.2	8.0	8.3	6.3
Domestic financed	1.2	1.0	1.2	1.9	2.3	2.0
Foreign financed	2.8	2.5	4.0	6.1	6.0	4.2
Overall balance (commitment basis)	-2.3	-3.3	-1.3	-4.4	-5.1	-3.5
Float (variation of accounts payable, + = increase)	0.6	0.1	0.5	0.0	-0.2	-0.2
Variation of domestic arrears (+ = increase)	-0.7	-0.5	-1.2	-0.7	-0.7	-0.7
Overall balance (including grants, cash basis)	-2.4	-3.7	-2.1	-5.1	-6.0	-4.3
Total financing	2.4	3.7	2.1	4.7	6.0	4.3
Foreign borrowing (residency principle)	1.2	2.2	0.7	3.6	4.0	2.3
Domestic borrowing (residency principle)	1.2	2.0	1.4	1.1	2.0	2.1

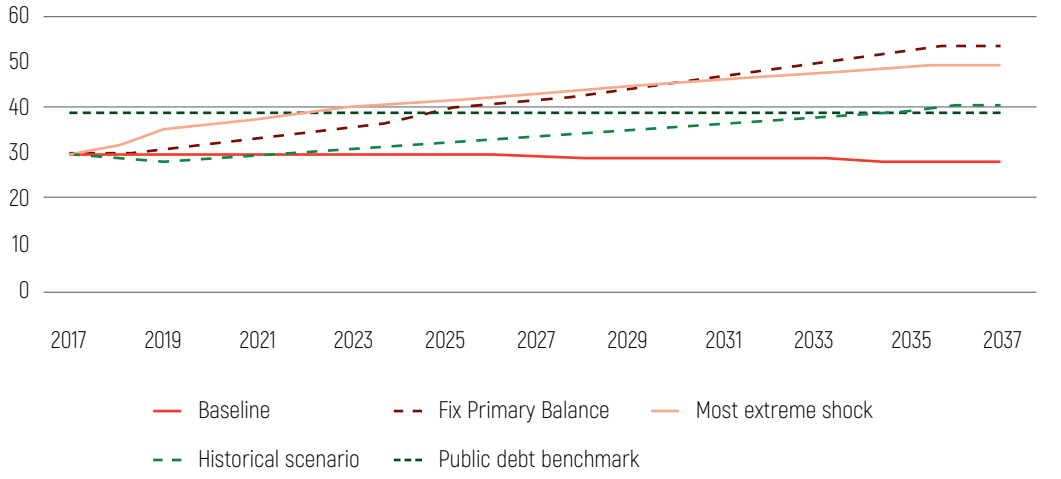
Source: Malagasy authorities, IMF and World Bank staff projections, October 2017

17. Following the increase in public revenue projection, the fiscal deficit is predicted to be lower at 4.3 percent of GDP, compared with 5.1 percent in the initial budget. Current projections point to 2.3 percent of GDP to be financed through foreign borrowing and 2 percent from domestic borrowing. External financing is largely on concessional terms. However, like previous years, there is the intention to contract a commercial loan with a

partial guarantee from the African Development Bank, of the value of US$40 million in the revised 2017 budget.[19] The IMF increased financing by US$43million to help offset pressures on the balance of payments from the shocks.[20]

18. Despite the increase in foreign borrowing, the level of external debt distress remains moderate.[21] According to the joint IMF-WB Debt Sustainability Analysis undertaken in June 2017, the present value of debt-to-GDP ratio stood at 29.1 percent in 2017. Debt dynamics are assessed to have improved since the previous DSA undertaken in July 2016 due to more favorable financing assumptions following the Donors and Investors Conference in December 2016. The present value of debt-to-GDP ratio is expected to stay steady at around 29 percent over the medium-term. Under the baseline scenario all indicators remain below debt burden thresholds. Stress tests indicate that debt sustainability is vulnerable to shocks, poor revenue collection, and contingent liabilities associated with state-owned enterprises (SOEs).[22]

F22 **Figure 22: Present Value of Debt-to-GDP Ratio**



Source: Joint IMF-WB DSA, June 2017

[19] Disbursement is expected at the start of 2018. In 2016 the AfDB agreed to provide a partial credit guarantee for a loan of US$55m from Deutsche Bank to cover the financing gap, but disbursement was delayed to June 2017.

[20] Madagascar has an Extended Credit Facility arrangement with the IMF, where member countries can request augmentation of access of quota when there are shocks. The IMF Executive Board approved a disbursement of $86 million, including an augmentation of $42 million, at its meeting on June 28, 2017.

[21] The Debt Sustainability Analysis assesses the risk of external debt distress. To assess debt sustainability, debt burden indicators are compared to indicative thresholds over a 20-year projection period. A debt-burden indicator that exceeds its indicative threshold suggests a risk of experiencing some form of debt difficulty. A moderate level of debt distress indicates that debt burden indicators are below the thresholds in the baseline scenario, but stress tests indicate that thresholds could be breached if there are external shocks or abrupt changes in macroeconomic policies.

[22] The latest available Debt Sustainability Analysis estimates JIRAMA's long term and short term debt to be around 5.5 percent of GDP and another 1 percent for a possible recapitalization of the Caisse d'epargne, the Madagascar Savings Fund.

PART TWO

Economic Outlook

19. The medium-term economic growth outlook is positive. Based on current projections, economic growth is estimated to reach 5.1 percent of GDP in 2018, and then average 5.3 percent over the 2019 to 2022 period. The intensification of public works activities is expected to be a key growth driver, which may also spur activity in related sectors. The tourism sector could also become an important contributor to growth, particularly if foreseen improvements to the national airline, Air Madagascar, materialize as planned. The energy sub-sector is projected to grow at an average of 10.5 percent over the 2018-2022 period, as private production expands and provided governance reforms for JIRAMA start to bear fruit.

20. Public finances are expected to continue readjusting to support the implementation of the National Development Plan. The scale-up of public investment activities is expected to result in higher imports, thereby contributing to a widening of the current account deficit. The deficit is largely expected to be financed by foreign direct investment and external financing of the public sector, which is projected to gradually increase. Over the medium term, both higher revenues and expenditures are expected. Increased revenues should be supported by continuous efforts to improve tax administration as well as higher grants following the Donors and Investors Conference. Expenditures are expected to reach an average of 19.5 percent of GDP over the medium term. As transfers and subsidies to non-priority areas reduce, higher expenditures are expected to be channeled to social priority sectors and public investments.

21. However, this growth outlook is subject to a commitment to maintaining political stability and continuing with important reforms. As the country prepares for elections at the end of 2018 / early 2019, for the first time in Madagascar's history there is the possibility that a Head of State will start and end a constitutional term following a democratic process. Such an achievement would bode extremely well for Madagascar's political processes and would support the nascent growth momentum, particularly through encouraging foreign investment. However, as election promises are made it will be critical to continue focusing on reforms that deliver results, by supporting the productivity and recovery of key sectors such as agriculture, energy and tourism, that have significant potential to stimulate growth and create jobs.

PART THREE

ASSESSING CHANGES TO MADAGASCAR'S INSTITUTIONS AND POLICY ENVIRONMENT

Since the return to constitutional order in 2014, there has been a steady improvement in the quality of Malagasy institutions. Specifically, the institutional environment for social protection, and the quality of budgetary management has improved. The World Bank measures the quality of policies and institutions through an instrument called the Country Policy Institutional Assessment. The evidence shows that countries with stronger institutions are likely to have better development outcomes. There is scope to further enhance the quality of Malagasy institutions, particularly in the areas of property rights, and transparency and accountability in the public sector.

1. Countries with stronger institutional environments are associated with having better development outcomes.[23] Countries with stronger institutions, particularly in areas such as property rights and a better regulatory environment, are more likely to encourage private sector development and growth. Stronger budgetary institutions are also more likely to encourage the effective allocation of resources in line with priorities outlined in a national development strategy paper. Furthermore, strong institutions are important for being able to effectively manage overseas development assistance and public debt.[24]

2. The World Bank has a diagnostic tool called the Country Policy and Institutional Assessment (CPIA) to assess the quality of a country's policies and institutional arrangements. The CPIA has 16 criteria that aim to measure the extent to which a country's policy and institutional frameworks supports sustainable growth and poverty reduction. The CPIA covers (A) Economic Management, (B) Structural Policies, (C) Policies for Social Inclusion/Equity, and (D) Public Sector Management and Institutions. The CPIA results in a score, which is published annually on the World Bank's website.[25] Further information on the CPIA is explained in Box 3.

3. Low-income countries that have made improvements to their institutional environments, as measured by the CPIA, have also shown progress in delivering development outcomes. Low-income countries that have made improvements to their CPIA scores (as shown through a positive change in the CPIA score) have also seen improvements in their human development outcomes. Similarly, low-income countries with stronger CPIA scores are generally assessed to have a stronger regulatory performance for doing business, as indicated by the distance to frontier measures.[26] To a certain extent, this finding reflects that the Doing Business survey is used to inform certain aspects of the CPIA score.

CPIA assesses the quality of a country's **policies** and **institutional arrangements**.

[23] This assertion is supported by a rich literature, which includes Acemoglu, D. and Robinson, J. 'The Role of Institutions in Growth and Development,' Commission on Growth and Development, Working Paper No. 10 and Evans, W.; Ferguson, C. Governance, institutions, growth and poverty reduction: a literature review. UK Department for International Development (DFID), London, UK (2013)

[24] See for example Dollar and Burnside (2000). Aid, Policies and Growth."

[25] http://databank.worldbank.org/data/reports.aspx?source=country-policy-and-institutional-assessment

[26] The distance to frontier score helps assess the absolute level of regulatory performance over time. It measures the distance of each economy to the "frontier," which represents the best performance observed on each of the indicators across all economies in the Doing Business sample since 2005.

Figure 23: Countries that improve the CPIA score also see advances in their human development index

Average 2010-2015 for countries with GNI per capita between 500 and 2300 $2011PPP

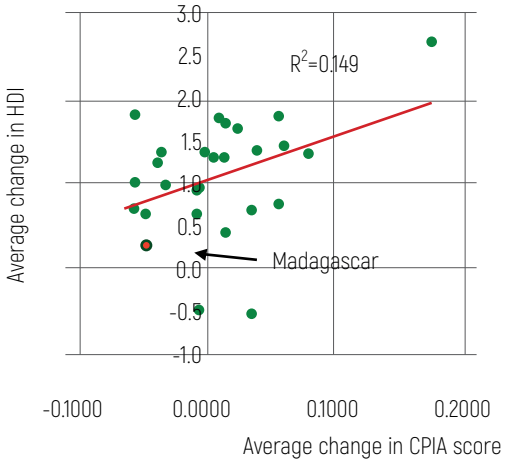
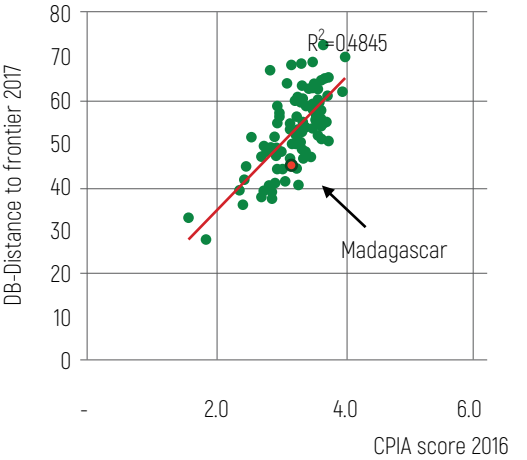


Figure 24: In general, countries with higher CPIA scores have better regulatory environments for doing business

Low income countries



Source: World Bank

Box 3: What is the CPIA and how is it used?

The CPIA criteria in table 4 are ranked with a score of 1 (low)) to 6 (high) to produce an overall CPIA score, which is used in different ways. Firstly, the CPIA score is used to inform how International Development Association (IDA) resources are allocated to different countries. Generally, countries with stronger performance are rewarded by receiving higher IDA allocations. Secondly, the CPIA score is one of the factors the World Bank uses to consider whether a country's institutional environment is fragile, along with the presence of a peacekeeping or political / peace building mission. Thirdly, the CPIA is used to determine a country's risk of debt distress. Countries that have weaker institutions have a lower debt burden threshold, reflecting a lower capacity to repay debt.

Table 4: CPIA criteria

Cluster	Criteria
Cluster A. Economic management	· Monetary and Exchange Rate Policies · Fiscal Policy · Debt Policy and Management
Cluster B. Structural Policies	· Trade · Financial Sector · Business Regulatory Environment

Cluster	Criteria
Cluster C. Policies for Social Inclusion/Equity	· Gender Equality · Equity of Public Resource Use · Building Human Resources · Social Protection and Labor · Policies and Institutions for Environmental Sustainability
Cluster D. Public Sector Management and Institutions	· Property Rights and Rule-based Governance · Quality of Budgetary and Financial Management · Efficiency of Revenue Mobilization · Quality of Public Administration · Transparency, Accountability, and Corruption in the Public Sector

Source: World Bank

The quality of Madagascar's institutions today

4. The quality of Madagascar's institutions has been progressively improving since 2014, as demonstrated by an increase in the CPIA score. The CPIA score increased from 3.0 in 2013, when the country's performance was at its lowest, to 3.2 in 2016.[27] Notably, improvements were made in the areas of Social Protection, and the Quality of Budgetary and Financial Management. These two criteria both gained 1 point between 2014 and 2016. Four other criteria also contributed to the overall improvement in the CPIA score, gaining 0.5 points each, including: (i) Building Human Resources; (ii) Debt Policy and Management, (iii) Transparency, Accountability, and Corruption in the Public Sector, and (iv) Gender Equality. Table 5 shows some of the reforms committed under these criteria.

5. Improvements to the institutional framework for social protection have stimulated the expansion of the social safety net programs. While the Government has had social protection policies since the 2000s, social protection programs were generally uncoordinated among several ministries and institutions.[28] In recognition of these challenges, the Government approved its first National Social Protection Policy in 2015. This framework has formed the basis for strengthening the role of the Ministry of Population, and Social Protection and Women Protection.

6. The Quality of Budgetary and Financial Management has improved through better access to information. During the political crisis period between 2009 and 2013, there was no national development plan, which constrained the ability to link the budget to development priorities. In addition, weak and unpredictable public resources led to discrepancies between the approved budget and execution. Furthermore, the country has always recorded delays in approving its Public Audited Financial Statement, even before the 2009 political crisis. These shortcomings have constrained the policy orientation of the budget and the credibility of the budget. With relative political stability since 2014, the country embarked on strengthening the budget process and budget management transparency. For the first time, the 2015 Public Audited Financial Statement was published in line with the limits provided in the law.

[27] See World Bank (2014). Madagascar. Economic Update for a review of CPIA trend between 2009 and 2013

[28] World Bank (2012). Madagascar. Three Years into the Crisis: An Assessment of Vulnerability and Social Policies and Prospects for the Future

T5 **Table 5: Improvements in selected CPIA criteria**

Criteria	Evolution
Social Protection and Labor	· Development and expansion of safety net programs · Improvement in the targeting mechanism · Development of the urgency response to the drought in the South in 2016
Quality of Budgetary and Financial Management	· Explicit links between the investment budget and the National Development Plan since 2016 · Publication of Citizen Budgets since 2015 · Adequate regulation rate for priority spending execution · Reduction in delays in approving Public Audited Financial Statements · Publication of the Public Report on the Accounting Court
Building Human Resources	· Adoption of the Health Sector Development Plan (2015-2019) and the National Strategy for Universal Health Coverage · Enhancement of the monitoring and evaluation mechanism for the public health sector
Debt Policy and Management	· Adoption of the law on public debt and the Debt Strategies · Improvement in the system of database management for public debt and publication of debt statistics
Transparency, Accountability, and Corruption in the Public Sector	· Update of the anti-corruption law and strategy · Participation of Civil Society in the budget preparation discussion · Development of Participatory Budgeting at municipality level
Gender Equality	· Revision of the law on Nationality Code recognizing women's capacity to transmit nationality to their children · Increase in the number of women accessing microfinance

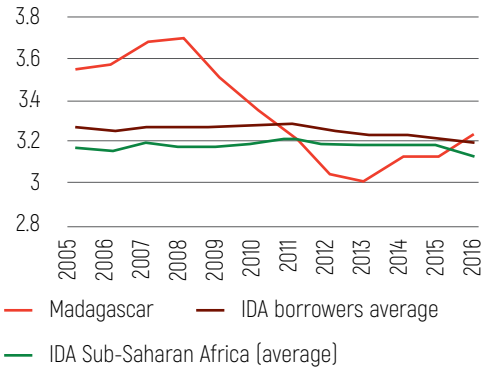
The potential to further improve the institutional environment

7. Prior to the 2009 political crisis, Madagascar was assessed as having stronger policies and institutions compared with the current situation. In 2007 and 2008, Madagascar's overall CPIA score stood at 3.7, compared with today's 3.2.[29] During the political crisis period, the CPIA score steadily declined, where the quality of public sector management and institutions notably worsened.

While Madagascar's CPIA score of 3.2 compares favorably with the Sub-Saharan African average of 3.1, it is still far behind some of the best performers. Madagascar's current performance suggests that there is further scope to enhance its policy and institutional environment, in line with its previous performance.

F25 **Figure 25: After a decline during the political crisis period, Madagascar's CPIA score is higher than the average for IDA countries**

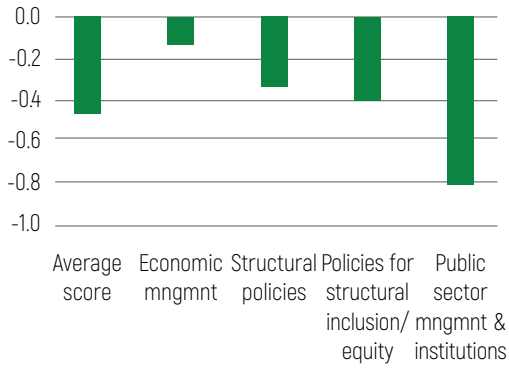
CPIA score



Source: World Bank

F26 **Figure 26: The quality of Public Sector Management and Institutions indicators worsened between 2008 and 2016**

Change in CPIA score

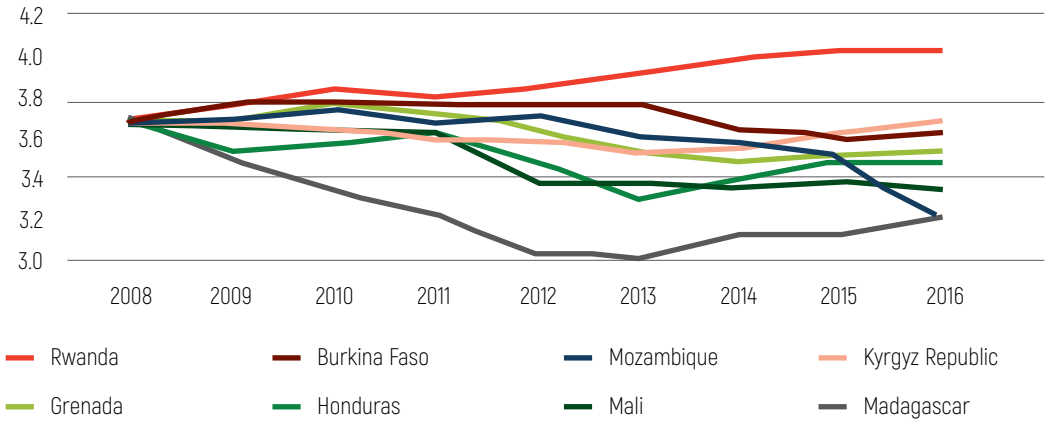


8. Lessons from other countries highlights that strong institutions go hand in hand with political stability, sound economic management, and ownership for implementing and sustaining reforms. Since the CPIA provides an indication of important gaps in policy areas, it can help governments prioritize actions in the development of a reform program. It also allows for monitoring progress over time and comparison with other countries. In 2008 several countries had the same CPIA score of 3.7 (Figure 27). Countries that experienced political instability such as Madagascar and Mali saw a deterioration in their score. In Mozambique, the debt crisis and economic governance concerns led to a sharp deterioration in the score. Rwanda, on the other hand has been able to gradually sustain and improve its CPIA score, supported by strong ownership of the reform process (see Box 4).

While Madagascar's CPIA score of **3.2 marks** an improvement, it is still far behind the best performers

[29] The scores might not be fully comparable due to the revision of criteria in 2011.

Figure 27: CPIA score in Madagascar and other countries with same score in 2008



Source: World Development Indicators

Box 4: How Rwanda improved its policies and institutions

With a score of 4, Rwanda has the highest CPIA performance compared with all low-income countries in 2016, and has recorded a continuous improvement since 2013. This strong performance is driven by a continuous commitment to institutional reform and strong leadership. Furthermore, the deepening of the dialogue between the World Bank team and the Rwandese government has helped to inform a reform action plan, which focuses on key areas for improvement identified in the CPIA. The process followed in Rwanda is described below:

1. Strong communication with the Government: this stage consists of sensitizing stakeholders from the government, mainly those at technical level, on the CPIA process and the criteria.

2. Formulating a joint working group on the assessment: an official representative from the Government, appointed by Permanent Secretaries of ministries and public agencies, is named as a focal point for each indicator. The representative is responsible for providing the required information and verifying the assessment conducted by the World Bank team.

3. Learning from previous experiences: the team learns from the comments provided during the internal review of the assessment by the Bank, to identify gaps in the institutional environment.

4. Sharing the results: once the assessment process is completed, the results are shared with the Government, to inform monitoring and the development of further reform efforts.

There are three important lessons learned: (i) using the CPIA as the basis for policy discussions, (ii) maintaining strong information; and (iii) starting the process of collecting data early to allow sufficient time for information exchanges.

9. Madagascar made significant progress in promoting ownership of institutional reforms, which is informed by the CPIA. In Madagascar, since 2015 a technical inter-ministerial team has been formed, to consult stakeholders on the CPIA process. The Ministry of Economy and Plan and the Ministry of Finance and Budget monitors the CPIA score for Madagascar. Stakeholders such as civil society, the private sector and research centers have been sensitized about the CPIA through workshops. The committee is also responsible for explaining how the CPIA score is used to inform resource allocation, the debt sustainability threshold, the identification of reforms relevant for the CPIA from the government's development program, and the monitoring of their implementation. The committee is the focal point for the consultations during the annual assessment by the World Bank team.

10. The Government's technical inter-ministerial committee and the World Bank have used the CPIA to jointly identify several areas for reform. Over the short to medium term, aspects of the institutional and policy framework that could be strengthened include:

- Strengthen anti-corruption efforts by (i) ensuring that all public officers declare the assets they own to the High Constitutional Court, as required by the law; (ii) enforcing sanctions related to violations found by the Committee on Budgetary and Financial Discipline.
- Improve Government's openness, transparency and accountability to citizens by (i) endorsing the Open Government Declaration; and (ii) improving budget transparency through making detailed expenditure data available and publishing the budgets of public entities.
- Increase tax revenues through: (i) cancelling tax exemptions that do not have positive net socio-economic impacts; and (ii) implementing the Tax Identification Number.
- Improve the planning of resources to key sectors in line with the National Development Plan through developing a medium-term expenditure framework.
- Enhance the performance and stability of the financial sector by: (i) passing a Credit Bureau Information Law to enable financial institutions to assess debitor's risk levels; (ii) passing a revised law on Microfinance to promote the stability of microfinance institutions.
- Further strengthen the institutional framework for social protection to avoid duplication of beneficiaries and improve targeting through establishing a registry of vulnerable households under the non-contributory social protection regime.

11. Over the medium-term, further efforts could be directed to improve public sector management and the quality of institutions. Three out of five criteria under cluster D are rated at 2.5, showing almost no progress for several years: (i) Property Rights and Rule-based Governance, (ii) Quality of Public Administration, and (iii) Transparency, Accountability, and Corruption in the Public Sector. These criteria cover several aspects of governance and institutions that are fundamental to promote growth and poverty reduction. The low scores are explained by: weak enforcement of laws and policies, perceived low quality of the legal and judicial system, high cost of access to appropriate judicial support by the poorest, modest capacity in human resource management in the public sector (competitive recruitment, performance-based promotion, incentives, sanction, etc.), low levels of accountability of the executive and inefficient control by existing bodies, and the absence of sanctions for mismanagement of public resources.

T6 **Table 6: Madagascar's CPIA Summary Table**

	Madagascar	Average SSA IDA countries
Cluster A. Economic management		
Monetary and Exchange Rate Policies	3.5	3.3
Fiscal Policy	3.0	3.0
Debt Policy and Management	4.0	3.2
Average [1]/	**3.7**	**3.2**
Cluster B. Structural Policies		
Trade	4.0	3.6
Financial Sector	2.5	2.8
Business Regulatory Environment	3.0	3.1
Average [1]/	**3.2**	**3.3**
Cluster C. Policies for Social Inclusion/Equity		
Gender Equality	4.0	3.2
Equity of Public Resource Use	3.0	3.3
Building Human Resources	3.5	3.6
Social Protection and Labor	3.0	3.0
Policies and Institutions for Environmental Sustainability	3.0	3.2
Average [1]/	**3.3**	**3.2**
Cluster D. Public Sector Management and Institutions		
Property Rights and Rule-based Governance	2.5	2.8
Quality of Budgetary and Financial Management	3.0	3.1
Efficiency of Revenue Mobilization	3.5	3.4
Quality of Public Administration	2.5	2.9
Transparency, Accountability, and Corruption in the Public Sector	2.5	2.7
Average [1]/	**2.8**	**3.0**
CPIA overall score[2]/	**3.2**	**3.1**

[1]/each criteria have the same weight for the calculation of cluster average

[2]/the overall score is the average of the 4 cluster's score

REFERENCES

- Acemoglu, D., and Robinson, J. (2008). 'The Role of Institutions in Growth and Development'. Working Paper No.10, Commission on Growth and Development, World Bank, Washington, DC
- Bureau National de Gestion des Risques et Catastrophes (2017). 'Point de situation ENAWO. BNGRC, Antananarivo, Madagascar
- Burnside, C., and Dollar, D. (2000).'Aid, Policies and Growth'. American Economic Review, Vol.90, No.4,pp. 847-868
- Evans, W., and Ferguson, C. (2013). 'Governance, institutions, growth and poverty reduction: a literature review'. UK Department for International Development. London, UK
- Global Facility for Disaster Reduction and Recovery, United Nations office for Disaster Risk Reduction, World Bank (2011). 'Disaster risk management programs for priority countries'. Second edition, GFDRR, Washington DC
- Ishira, Y. (2015). 'Rwanda experience: country policy and institutional assessment (CPIA)'. Macroeconomics and Fiscal Management practice notes, No.7. World Bank, Washington, DC
- Kraay, A., and Vikram, N. (2004). 'When Is External Debt Sustainable'. Policy Research Working Paper No.3200. World Bank, Washington, DC
- Maplecroft (2010). Climate Change Vulnerability Index 2011. <http,//www.washingtonpost.com/wp-srv/nation/green/pdfs/ClimateChangeVulnerabilityIndex2011.pdf> (accessed August 2017)
- South West Indian Ocean Risk Assessment and Financing Initiative, Global Facility for Disaster Reduction and Recovery, and World Bank (2016). 'Madagascar Disaster Risk Profile'. World Bank, Washington, DC
- United States Agency for International Development (2016). 'Profil du risque de changement climatique Madagascar'. USAID, Washington, DC
- World Bank (2012). 'Madagascar- Three Years into the Crisis: An Assessment of Vulnerability and Social Policies and Prospects for the Future', Volume2. Background Papers. World Bank, Washington, DC
- World Bank (2014). 'Madagascar- Economic Update'. World Bank, Washington, DC
- World Bank (2017). 'Commodity Markets Outlook'. World Bank, Washington, DC
- World Bank (2017). 'Estimation of economic losses from Tropical Cyclone ENAWO'. World Bank, Washington, DC