PROJECT INFORMATION DOCUMENT (PID)
CONCEPT STAGE

Report No.: AB2411

Project Name	CEMAC Financial Institutions Support Project
Region	AFRICA
Sector	General finance sector (100%)
Project ID	P099833
Borrower(s)	BEAC
Implementing Agency	
Environment Category	[ ] A [ ] B [X] C [X] FI [X] TBD (to be determined)
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1. Key development issues and rationale for Bank involvement

The Central African Economic and Monetary Community (CEMAC) comprising Cameroon, the Central African Republic, Chad, the Republic of Congo, Equatorial Guinea, and Gabon, is one of the oldest regional blocs in Africa and has its roots in the colonial era when the countries other than Cameroon and Equatorial Guinea were organized as a federation with a common currency, the CFA. The region is the smallest of African regional arrangements with a population of about 31 million; countries are contiguous, but forests, few natural trade routes and poor infrastructure make communications difficult. The region is well endowed with natural resources including petroleum in five of the six countries (discovered in the nineties in Equatorial Guinea and Chad). Cameroon and Gabon are the largest economies, accounting for some 64 percent of regional GDP; some 47 percent of the population lives in Cameroon. The countries rank low on the human development index (CAR 169; Chad 167; Republic of Congo 144; Cameroon 141 and Gabon 122 out of 177). The grouping is diverse, including relatively prosperous coastal economies and two poorer landlocked countries: Chad and the Central African Republic; regional texts have always recognized the importance of integration to the development of the land-locked countries.

The increase in oil prices over the recent past has made the management of liquidity in the financial system and intra-regional financial flows a central issue of economic policy. Some countries in the region are likely to generate surpluses from petroleum exports which are expected to be reinvested to promote regional development.

The integration movement dates to independence in the early sixties when the region was organized as a loose monetary association; a customs union was established in 1964, but in fact policies pursued discouraged intra-regional trade. In the 1980's, the oil price collapse, and macroeconomic imbalances led to a severe depression (per capita GDP fell by an annual average of 3.7 percent in 1985-1993), which eventually led to a 50 percent devaluation of the CFA in 1994 and the adoption of an economic reform program. Reforms included restructuring of the regional customs union (renamed the Central African Economic Union) which together with the Central African Monetary Union became CEMAC under a treaty ratified in 1999. As a result of the reforms started in 1994, the region has a less distorted trade regime than most countries in sub-Saharan Africa. The reforms also helped develop the institutional infrastructure for the Community, and the exchanges have led to a growing recognition among member countries of the advantages of integration both in terms of economic development and in their standing internationally and vis-à-vis their larger neighbors (principally Nigeria, given its recent growth, but also the Democratic Republic of Congo).

The CEMAC policy agenda calls for integration through financial sector integration; an expanded customs union; macroeconomic policy convergence and coordinated sector policies. Progress has been made in financial integration, which is critical for expanded intraregional trade and the movement of capital, including the petroleum surpluses, among countries. The CEMAC countries share (i) a Central Bank – BEAC (*Banque des Etats de l'Afrique Centrale)* the strongest regional institution, which formulates a common monetary policy, and manages the CFA, which has a fixed parity with the Euro; (ii) a banking supervision commission – COBAC (*Commission Bancaire de l'Afrique Centrale*) which is charged with regulation of banks and other deposit-taking financial institutions, including microfinance institutions, and is competently run, although quite short of resources; and (iii) a Development Bank –BDEAC *(Banque de Développement des États d'Afrique Centrale*, which has been mandated to promote regional investments and is being restructured. Regional institutions have also been established to regulate the financial market (COSUMAF) and deal with money laundering (GABAC), both of recent creation. The CEMAC countries also share a common external tariff and business laws harmonized under the OHADA initiative *(Organisation pour I' Harmonisation du Droit des Affaires).* The institutional architecture of CEMAC includes an Executive Secretariat which is relatively new and generally considered quite weak.

Progress in establishing regional financial institutions is a step in developing the financial system, which is in fact among the least developed in the world and not able to appropriately intermediate between the increased resources and the needs for increased credit, particularly for investment, in the region. According to the conclusions of the recently carried out regional FSAP, the sector is dominated by the banking sector which accounts 87 percent of assets. Credit to the private sector is only about 7 percent of GDP; there are only about 1 million bank accounts and 780, 000 clients in microfinance institutions (a penetration rate of 3 percent or 2.2 percent of the market respectively, which is very low); there is virtually no investment finance. The system is exposed to risks, in part because of the sectoral concentration of credits characteristic of the region but also because of the lack of policies to manage liquidity, a regulatory framework which is more lenient than international norms and inadequate supervision. The proposed project will help strengthen financial policies and institutions so that financial services, including those to the very poor, are expanded.

The Bank assistance strategy for the CEMAC region is outlined in a Regional Integration Assistance Strategy (RIAS) prepared in January 2003 (Report No.25328). The strategy is based on the premise that the historical and institutional base for integration that exists can lock member countries into policy reform, encourage peace within the Community and increase the presence of member governments in international negotiations. In addition, regional integration is essential for the economies of the two landlocked countries (Chad and the Central African Republic), which have among the lowest per capita income in the world. The work program in the Bank strategy has the following objectives: (i) the development of a unified financial market which is a necessary condition for integration in the region; (ii) improvements in trade facilitation and the promotion of efficient region-wide infrastructure services; and (iii) improvements in human resources through support to HIV-AIDS. An underlying theme is the need to strengthen the institutional framework for integration.

The Bank is also increasingly focusing on a regional approach to member countries' development. Forestry conservation and transport development are being dealt with on a regional basis. In the financial sector, the Bank is financing the establishment of a regional payments system, and supporting a single approach to banking restructuring and to microfinance regulation. The proposed project is part of the Bank strategy and listed as a priority in the RIAS. The Bank intends to work closely with the IMF and other donors involved in regional integration, notably the African Development Bank and the Government of France, to ensure harmonization of activities carried out under the project

2. Proposed objective(s)

The objective of the project is to improve financial integration and intermediation in the CEMAC region which will help increase economic activity and reduce poverty over time. Project outcomes will include enhanced regional integration, increased credit (particularly for investment) and deposit mobilization in the region, as well as improved governance on financial matters. Indicators will be further developed during project preparation.

3. Preliminary description

A sector investment credit is proposed. The credit would finance technical assistance, studies, training and related investments to support strengthening of institutions so that they are able to efficiently carry out their mandate. A line of credit for investments in regional projects which are too small to be financed through other means is also being considered. The preliminary project components are summarized below. The activities listed are priorities where the Bank has a comparative advantage. However, the agenda for financial sector and regional integration is very broad, and it is likely that the program to be supported by all donors will be larger. The full program including those activities financed by other donors will be included in the Project Appraisal Document.

A. Developing policies and mechanisms to better manage the regional monetary union

The project will provide assistance so that the regional authorities are in a better position to appropriately manage liquidity, carry out effective monetary policy, and improve macroeconomic management, including the ongoing effort towards reaching economic convergence. This is also central to an effective use of petroleum surpluses so that these can be channeled for investment. BEAC is a well run institution, and support will focus on areas which will enhance its ability to conduct monetary policy and ensure currency stability. The project would, inter alia, support improvements in monetary policy formulation, the establishment of the

Treasury bill market, assistance in the management of foreign exchange reserves, and regional macroeconomic management.

B. Strengthening regional institutions

The project will help strengthen regional institutions so that they can carry out their mandates of ensuring the soundness of the regional economic and financial system and promote economic development. The regulatory framework for banking institutions was updated in 2001 although some of the prudential regulations are less strict than international norms and it is difficult for a bank to in practice operate regionally which is a serious obstacle to integration. Regulations governing microfinance institutions were enacted in 2002 and while they are in line with international best practice, they have not yet been adopted because of the large number of small institutions involved renders the task complex and time-consuming. As supervision requirements have expanded without a concomitant increase in resources for recruitment and training of staff, the ability of COBAC to supervise banks and microfinance institutions is inadequate, which represents a potential threat to the already small deposit base. The project will also support the further preparation of the basic framework for a regional securities market which is in principle to be supervised by the Central African Financial Supervision Commission (COSUMAF - *Commission de Surveillance du Marché Financier de l'Afrique Centrale*), and the needed activities to develop the Regional Anti-Money Laundering capacities under the aegis of the GABAC **(***Groupe d'Action contre le Blanchiment d'Argent en Afrique Centrale*). Tighter regulation and supervision of financial institutions, markets and operations will significantly contribute to the governance improvement agenda of the countries in the sub-region.

Expansion of finance in the region will require increased knowledge of and information about clients. To this end a regional credit bureau, possibly at BEAC, would represent an important step. The project will support the establishment of such a credit bureau. The project could also provide institutional support to the Executive Secretariat of CEMAC which is charged with making the customs union effective; enforcing macro-economic policy convergence and pursuing financial sector integration. CEMAC remains weak and understaffed particularly in light of its broad mandate. The project would strengthen CEMAC and help it define a work program so that it can gradually fulfill its mandate.

C. Facilitating the financing of integration investments

The project would support the institutional strengthening of BDEAC, the regional development bank, and could finance a pilot line of Credit to support regional investments, primarily in infrastructure. BDEAC has been appointed by CEMAC countries to manage a Community Development Fund (FODEC-*Fonds de Développement de la Communauté)* and is also expected to receive substantial funding from increased petroleum revenues to finance regional infrastructure investments such as cross-border electricity supply and the construction of the regional road network. Despite progress in strengthening its financial position, BDEAC would have difficulties managing the resources that are expected to eventually flow through it, and has requested Bank assistance. The project would support the design and implementation of an institutional strengthening program, which would focus on strengthening financial management, operational practices, including project analysis, and staffing. Completion of an agreed program in the early years of project implementation would enable BDEAC to subsequently manage a pilot line of credit from the Bank, and would be a condition of disbursement of the IDA line of credit should the line of credit be included in the project.

Projects financed under the line of credit would promote economic integration among CEMAC countries. The funds would be on-lent to BDEAC; as in the case of the lines of credit to the West African Development Bank, IDA funding would be allocated only to public sector components of investment projects which require long-term financing and have high economic return. The on lending arrangements would be in line with standard practice for lines of credit.

4. Safeguard policies that might apply

If a line of credit is included in the project, the environmental assessment of investments financed.

5. Tentative financing

Source:		($m.)
BORROWER/RECIPIENT		10
INTERNATIONAL DEVELOPMENT ASSOCIATION		50
	Total	60

6. Contact point

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