

**WEST AFRICAN MONETARY AGENCY
(WAMA)**



ECOWAS MONETARY COOPERATION PROGRAMME

**MACROECONOMIC CONVERGENCE REPORT
2007 SENEGAL**

FREETOWN, JUNE 2008

Economic policy objectives for 2007 were centred on an economic growth rate of 5.8%. This was to be spurred on by a series of reforms in the electricity sector as well as the resumption in operations of the Société Africaine de Raffinage (SAR) and the Industries Chimiques du Sénégal (ICS). In spite of the early warning signals of inflationary pressures sensed through the surge in oil prices on the international market, the inflation rate target as of December ending 2007 was set at 3%.

Further improvement in the state of public finances was expected owing to the exceptional growth projected in budgetary revenue collection. The said growth, however, was expected to be partially whittled away by significant transfers to ailing public enterprises mainly in the energy sector. Consequently, the overall deficit excluding grants was expected to deteriorate further, rising from 6.3% of nominal GDP in 2006 to 6.8% in 2007. Overall deficit targets were originally projected at 4.8% of GDP in 2006 and 4.6% in 2007, in view of the anticipated rise in the level of grants mobilisation.

The general extent of convergence compliance was expected to improve with the projected achievement of seven (07) convergence criteria by the end of 2007.

The quest to achieve these targets yielded rather mixed results. Even though the projected growth target, of 5.8% was met, the same could not be said about general price levels which recorded sharp rises, thereby spurring on end of year inflation to 6.1% as of December ending 2007 as against 4.0% in the previous year.

1. Sector analysis

1.1 Real Sector

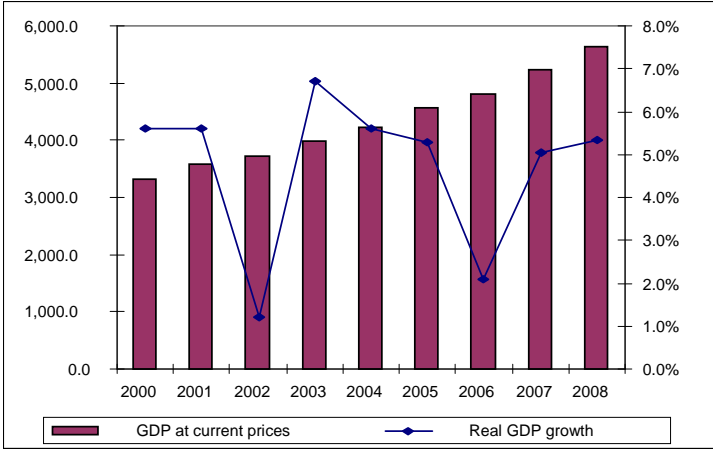
The year 2007 was marked by an accelerated economic growth. This growth was achieved thanks to the performance recorded in all sectors of the economy. In fact, in the primary sector, growth rate settled at 6.4% against a decline of 2.9% in 2006. The agricultural sector recorded a growth rate of 5.5% reflecting a recovery after the decline. This performance is attributed to the even spread of rainfall and good phytosanitary conditions. Food production grew by 7% in 2007 and industrial agriculture meant for exports expanded by 2.8% against a 7.4% and 1.6% decline respectively in 2006. With regard to the livestock sector, it advanced by 2.3% against 5.9% in 2006.

In the secondary sector, there was a 6.8% growth in 2007 against 1.7% the previous year. This outcome is linked with the resumption of production at Industries Chimiques du Senegal (ICS) and at Société Africaine de Raffinage (SAR). In fact, following the agreement between the State and the Indian partner for the recapitalisation of ICS, production increased by 12.3% against a decline of 22.1% in 2006. As regards production in other industries including SAR, the growth recorded was 2.2% despite the escalation of crude oil prices. The electricity, gas and water sub sector recorded a growth of 5.6% in 2007 against 0.3% in 2006. Growth remained vibrant in the construction and public works sector, reaching 10.0% in 2007 against 15.0% in 2006. The buoyancy observed in the construction and public works sub sector stem basically from construction activities in preparation for the 11th Summit of the Islamic Conference Organization, implementation of the Improved Urban Mobility programme and household investments in housing.

With regard to the tertiary sector, the growth rate was 5.4%, driven mainly by transport, post and telecommunications sub sectors which grew by 12.6%. Trading activities increased by 5.3% in 2007

against a decline of 0.5% in 2006 in view of the rise in the margin of primary and secondary sector products as well imports.

Graph 3.25 : Trends in Nominal GDP and Real Growth Rate



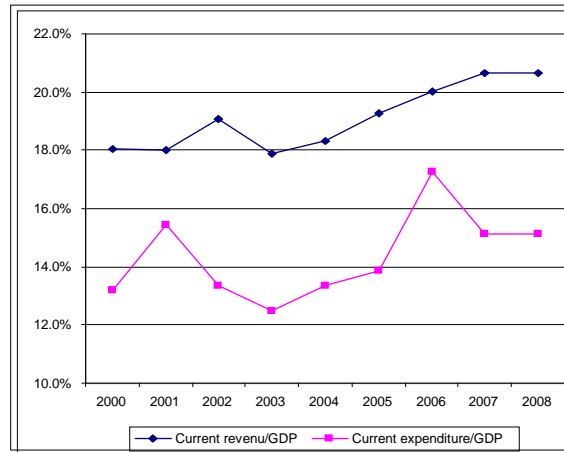
On the employment level of GDP, final consumption grew by 6.2%. The FGCF expanded by 6.8% on account of the public FCCF which went up by 12.0% and the private FGCF by 5.0%. Concerning external trade, imports and exports recorded 0.2% and 3.7% growth respectively following the resumption of production at ICS and SAR as well as the dynamism underlying the upturn in the importation of capital goods and intermediary goods.

Regarding prices, the year recorded a rise in inflationary pressures. End of period inflation at end of December stood at 6.1% against 4.0% the previous year. This inflation rate was the result of a 10% rise in “housing, water, gas, electricity and other fuel” prices and 7.3% increase in “foodstuffs and non alcoholic beverages” prices. This upward trend is due to the increase in bread and rice prices following the escalation of cereal prices especially, wheat and rice on the world market.

1.2 Public Finances

An analysis of the budget implementation statement points to a recovery in the trends of major budget indicators. Indeed, progress in the area of budgetary revenue recovery was made in tandem with a successful budget implementation strategy; this resulted in the positive outcome of major budget balance indicators. Consequently, the overall balance of financial operations dropped to -3.3% of GDP at the end of 2007 as against -6.6% in the previous year. The ratio of this balance excluding grants was -5.2% in 2007 against -7.6% in 2006

Graph 3.26: Trends in Current Revenue and Expenditure



All these developments stem from a growth of 14.0% in budget revenue which reflected in a ratio of 21.0% against 20.0% in 2006. This trend was fuelled by tax revenues which rose by 12.6% as result of the implementation of reforms aimed at widening the tax net, including measures geared towards strengthening the efficiency of tax authorities thanks to the recruiting training personnel on one hand, and strict controls and constant as well as regular monitoring carried out by the Revenue Service. Besides, the surging crude oil price, growing import of refined petroleum products and the considerable reduction in period of clearing goods, which is currently 10 days compared to 1.5 to 2 months, especially for petroleum products, also contributed to the good performance in tax revenue collection. With regard to non tax revenues, they recorded a significant growth of 44.0% due to the revaluation of operating licenses of mobile telephone companies. Grants accounted for 2.0% of GDP in 2007 against 1.5% in 2006.

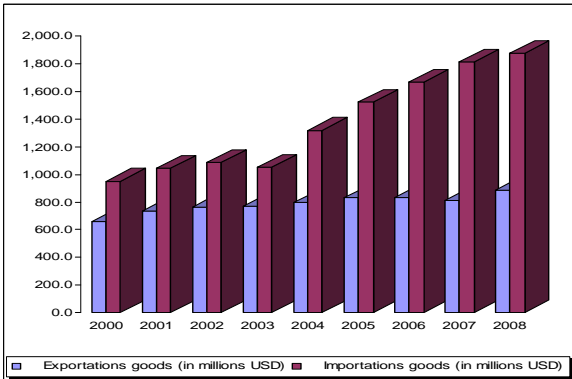
The positive outcome of budget balances is also attributed to the moderate expansion in public expenditure. Total expenditures and net borrowings in 2007 grew by only 3.3% to settle at 26.2% of GDP against 27.7% in 2006. This slow down is due to the 5.7% decline in recurrent expenditure following the 30% reduction in interest payments on public debt. On the other hand, emoluments and salaries increased by 14.8% in line with the implementation of the policy on recruitments and improvement in salary scales for civil servants. Similarly, capital expenditures went up by 0.6% on account of its internally funded component. This component grew by 16.2%, leading as at end of December to an improvement of 1.1 percentage point of the ratio in relation to tax revenues which reached 37.7%. The externally funded component reduced by 3.3%.

The reduction in interest payments on public debt is partly due to the downward trend in the total debt stocks as a result of reliefs obtained under the Multilateral Debt Relief Initiative as well as the HIPC initiative for which the completion point was achieved in April 2004. Outstanding public debt stood at 19.7% of GDP against 40.9% in 2006.

1.3 External Sector

The overall position of the balance of payments recorded at end of December 2007 a surplus of 44.0 billion against 99.0 billion in 2006. This situation is due to the firming of the surplus on the capital and financial operation account. Indeed, the current deficit widened by 18.5%, reflecting the unfavourable trend in the trade and services balance, whilst the revenue and transfers balance without counterparts improved. The trade deficit widened by 19.7% to settle at 1000.9 billion following an 8.7% growth in imports coupled with a slump of 2.4% in exports as a result of a decline in external sale of petroleum products. The increase in imports is mainly attributed to petroleum products, capital goods and intermediary goods. Services recorded a net deficit of 19.6 billion in 2007 against 18.5 billion in 2006. Revenue deficit declined due to interest payments on public debt. Net transfers stood at 216.4 billion, representing a growth of 18.0% compared to the amount recorded in 2006 in tandem with the increase in remittances of workers and public transfers. All these contributed to the worsening of the current deficit which rose from 9.4% of GDP in 2006 to 10.2% of GDP in 2007.

Graph 3.27 : Trends in Imports and Exports



The capital and financial operations account firmed by 35.6 billion as a result of inflows of resources accruing from the granting of a third mobile telephone license and the exploitation of iron ore at Faleme.

1.4 Monetary Sector

Monetary policy in UEMOA countries is a joint venture. This gives room for insignificant variations in the manipulation of instruments from one country to the other.

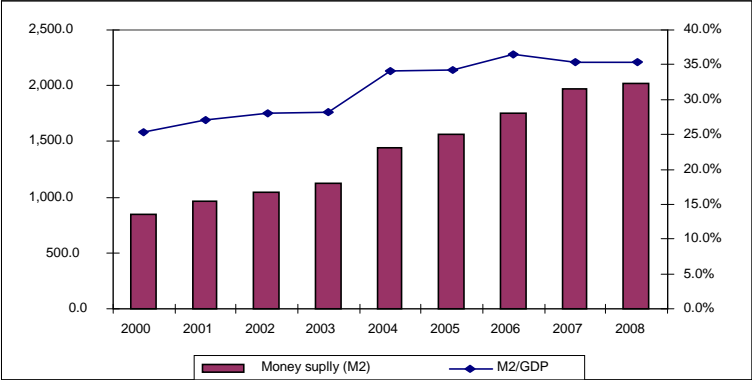
Within the Union, currency and credit management is based on interest rate policy and the mandatory reserves system. In a general context where relative price stability prevailed, the Central Bank maintained its keys rate unchanged. The pension rate remained at 4.25% and the discount rate at 4.75%. Similarly, the reserve coefficient imposed on banks and financial institutions was maintained at 9.0%. This led to increases in the main monetary aggregates.

In effect, the net creditor external position of financial institutions stood at 851.1 billion, showing an improvement of 9.2% compared to end December 2006. This result stems mainly from the 75.0 billion increase in BCEAO’s net external assets, reflecting efforts made within the framework of export earning repatriation. Outstanding internal credit recorded a 17.9% growth to settle at 1 323.5 billion at end of December 2007. The net position of government worsened by 72.9 billion in line with its growing commitments towards the banking system as a result of a relatively high level of banks’ subscriptions to instruments issued by the State on the regional financial market. Credit to the private sector went up by 10.7% to settle at 1 230.3 billion at the end of December 2007. Reflecting trends in its counterparts,

money supply grew by 2.6% to settle at 972.0 billion at end of December 2007. Deposits rose by 20.2% and cash circulation by 6.7%.

The year was marked by the persistent appreciation of the euro against the dollar. This raised the value of the CFA franc against the dollar and currencies of competitor countries linked to the dollar. However, in view of a quite favourable inflation differential, this appreciation did not affect the actual interest rate in recent years. The situation may change if prices continue to escalate.

Graph 3.28 : Trends in Money Supply



2 Performance under Macroeconomic Convergence

On the convergence front, Senegal continued to experience the negative trends that set in since 2002. After a record of eight (8) targets achieved in 2003, this performance has been eroded year after year to settle at 5 targets in 2007, being the worst since the convergence mechanism was set up in 2001. The expansion in the budget deficit was cushioned off as a result of improvements in tax revenue collection, with the ratio in relation to nominal GDP going for the first time beyond the threshold of 20% in conformity with the community basic standard. The increase in tax revenue continue to reflect in the priority accorded internally funded investments whose ratio in relation to tax revenues has followed an upward trend since 2004.

SENEGAL : CONVERGENCE POSITION	Target	2003	2004	2005	2006	2007	2008. (*)
Primary criteria							
Budget deficit/GDP	≤ 4%	3.3	5.5	4.7	7.3	5.2	6.3
Rate of inflation	≤ 5%	-1.5	1.7	1.4	4.0	6.1	2.9
Monetary financing of budget deficit /Previous year tax revenue	≤ 10%	0.0	0.0	0.0	0.0	0.0	0.0
Gross external reserves in months of imports	≥ 6	6.0	5.2	4.3	4.1	4.1	4.4
Secondary criteria							
Tax revenues/GDP	≥ 20%	17.1	17.6	18.6	19.2	20.0	20.1
Wage bill/Tax revenues	≤ 35%	30.1	29.5	30.0	31.0	31.6	30.7
Private invest./tax revenues	≥ 20%	28.1	30.0	33.7	36.6	37.7	48.1
Real interest rates	≥ 0	5.0	1.8	2.1	-0.5	-2.6	0.6
Real exchange rate stability	± 5%	2.5	0.1	-1.3	-0.6	1.1	-0.2
Total # of criteria met		8	8	7	6	5	6

Source: AMAO, BCEAO.

(*) : Annual estimates

3 Prospects for 2008

For 2008, the overall objectives remain the same as those set in 2007. This scenario takes into account the unfavourable conditions that are having a negative impact on the international economic environment. Thus, Senegal would strive to achieve in 2008 a growth rate of 6.1%, price stability and improvements in budget and current account of the balance of payments deficits.

These objectives would be achieved through increased activity in the main traditional economic sectors. The primary sector would record an average growth rate of 5.7%. This performance will be fuelled by agricultural production which would grow by 10.3% in view of the implementation of national policies aimed at improving food security, increasing rural populations' income and protecting the environment. These policies are based on orientations defined by the Government in the Return to Agriculture Plan (REVA) whose aim is develop production to cover internal demand in a sustainable manner.

In the secondary sector, economic activity would grow by 6.6% in 2008 thanks to the implementation of infrastructural investment programmes. These include the construction of a new international airport, Blaise DIAGNE, activities planned under the modernization of the container terminal of Dakar Port Authority by Dubai Ports World, the construction of toll motorway linking Dakar and Diamniadio, Urban Mobility Improvement programme, works in preparation of the 11th Summit of the Islamic Conference organization as well as improvement in the productivity and competitiveness of SME.

With regard to the tertiary sector, it would grow by 6.3% thanks to improved performances expected in the Transport and Telecommunication sub sectors which would grow by 12.0%. Trading activities would expand by 4.7% in view of adequate supplies to the markets and a recovery in industrial production.

As regards prices, inflation would be maintained below 3% as a result of adequate supply on the markets and a rigorous budget policy.

Concerning budget management, projections indicate that the strengthening of the budget framework would be pursued and this would lead to an increase in total revenues by 8.6%. This trend coupled with efforts at controlling public expenditure should have a positive impact on budget indicator, especially the related convergence criteria.

4 Conclusions and Recommendations

The generally low level of convergence is one of the major characteristics that come out the analysis of economic trends in Senegal in 2007. Though projections point to a possible improvement in the situation in 2008, the bleak world economic outlook resulting from the mortgage crisis and the persistent escalation of petroleum prices may impede the achievement of the above objectives. There is therefore the need to take appropriate measures to limit the negative impact should these unfavourable international conditions persist. In this regard, Senegalese authorities should give priority to the following measures:

- Pursuing the implementation of special programmes that will stimulate strong and sustained growth ;
- Implementing programmes designed to strengthen and diversifying exports in order to benefit from opportunities on international markets ;
- Deepening the restructuring of Industries Chimiques du Sénégal, the energy sector and groundnut sub sector ;
- Sustaining efforts to mobilize revenue and control current expenditures, especially transfers and subsidies in order to attain macroeconomic performances of the early 2000s.