OVERVIEW

In 2006, against a backdrop of robust and accelerating global economic growth, African Franc Area countries as a whole posted a slowdown in their growth rate, which slipped from 3.9% in 2005 to 3.1% in 2006. This overall result, which is barely above the rate of demographic growth, stemmed from the slackening – more pronounced in West Africa than in Central Africa – of the rate of GDP growth, which converged towards 3% in both parts of the Area. As in the previous year, both of the Franc Area's main sub-regions put in a weaker economic performance than Sub-Saharan Africa as a whole, which recorded growth of 5.5%. However, inflation remained significantly lower in the Franc Area than in Sub-Saharan Africa as a whole.

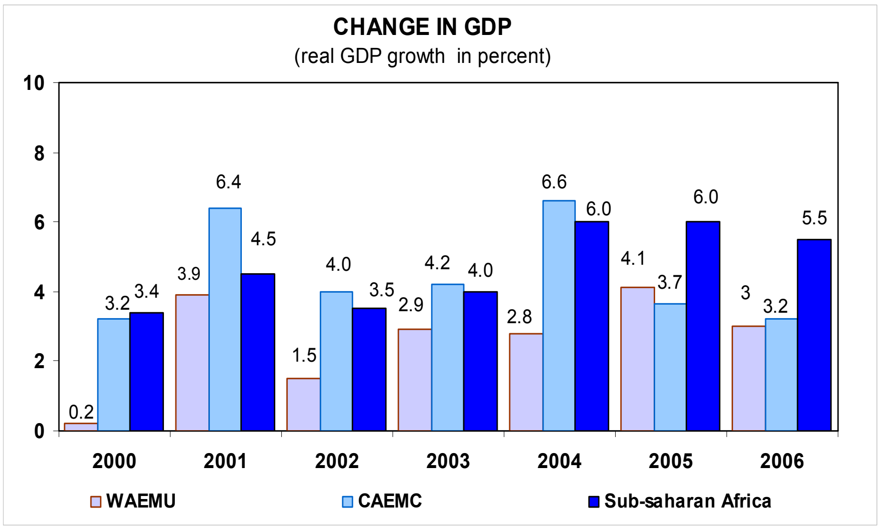
Key economic indicators

(%)

	GDP growth (%)		Inflation (%) *		Fiscal position (% of GDP) **	
	2005	2006	2005	2006	2005	2006
WAEMU	4.1	3.0	4.3	2.3	-2.8	– 2.5
CAEMC	3.7	3.2	2.9	5.3	8.8	11.7
Sub-Saharan Africa	6.0	5.5	10.6	11.8	1.5	4.1

* Change in consumer prices, as a yearly average
** On an accrual basis, including grants (but excluding MDRI)
Sources: IMF Regional Economic Outlook April 2007, central banks.

In 2006, the countries of the Central African Economic and Monetary Community (CAEMC) once again enjoyed a substantial improvement in their terms of trade thanks to the rise in oil prices. The West African Economic and Monetary Union (WAEMU) benefited from a slight upturn in its terms of trade but was hampered by the persistent socio-political uncertainty in several of its member countries.



Sources: Central banks, IMF Regional Economic Outlook April 2007.

The economic slowdown in CAEMC countries, with GDP growth of 3.2% after 3.7% in 2005, mainly reflects the fall in oil production, which was down by 3.9%. Equatorial Guinea remained the largest oil-producing country of the sub-region, with annual production of 17.1 million tonnes, ahead of Congo (13.3), Gabon (11.9), Chad (7.9) and Cameroon (4.4). These five countries account for over 11% of Africa's total oil output. In 2006, the CAEMC's reliance on the oil industry increased further, with the latter accounting for 44% of GDP, 83% of exports and 71% of tax revenues.

In the non-oil sector, commercial activities, transport and telecommunications as well as local crop and log and wood production were particularly dynamic. By contrast, the contribution of export crops to growth was negative as a result of the decline in coffee, cotton and banana harvests.

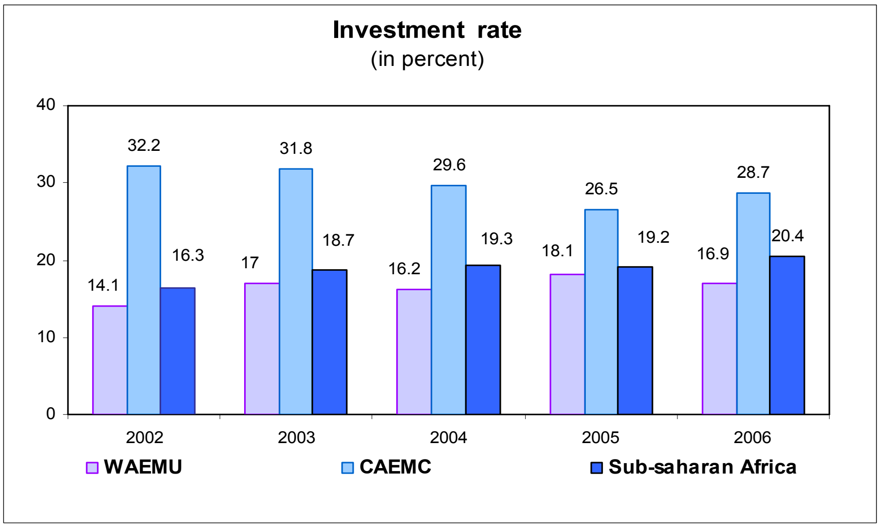
Congo and Equatorial Guinea continued to enjoy relatively sustained growth rates, although significantly lower than in 2005. Economic activity increased in Cameroon (which accounts for 36% of the CAEMC's GDP) and in the Central African Republic. Gabon posted a weak growth rate, significantly down on 2005, while the Chadian economy might be stalling or in recession.

The CAEMC's investment rate (28.7% of GDP) is higher than that of Sub-Saharan Africa as a whole (20.4%). However, investment activity is very largely determined by its oil component, which has limited medium- and long-term spillover effects on local economic development.

GDP growth in WAEMU countries shed more than a percentage point, falling from 4.1% in 2005 to 3% in 2006. In the primary sector, the slow pace of restructuring affected the financial position and economic results of agricultural sectors. There was a decline in cocoa and groundnut harvests as well as in sales of cashew nuts, and there was no increase in cotton production. In particular, the cotton sector in Franc Area countries faces asymmetrical competition from a number of industrialised countries that heavily subsidise their own producers. In the secondary sector, problems related to the supply of electricity that persist in several countries and that are gradually spreading to the whole of the sub-region have substantially disrupted productive activity. Moreover, the crisis in the phosphates and chemicals sectors (Senegal) led to very substantial falls in production. All in all, growth mainly stemmed from the increase in local crop production, the dynamism of mining activities (gold in Mali, uranium in Niger and oil in Côte d'Ivoire) and the strong performances of retail trade and mobile telephones.

In addition to cyclical factors, the still delicate socio-political environment in some countries weighs on companies' development decisions, which is reflected in the relatively low investment rate in the sub-region (16.9%). Thus, for the last six years, the WAEMU's economy has been hampered by the situation in Côte d'Ivoire (35% of the sub-region's GDP), where the growth rate fell from 1.8% in 2005 to 1.2% in 2006. During the year under review, the Union was also affected by the sharp slowdown (from 5.3% to 2.1%) of economic growth in Senegal, the sub-region's second largest economy (20% of GDP).

While the slowdown in activity was marked in Guinea-Bissau and in the WAEMU's two largest economies, a country-by-country analysis reveals relatively sustained growth dynamics (albeit less so than in 2005) in Mali, Niger and Burkina Faso. In Togo, the growth rate increased but remained below 2%.



Sources: Central banks, IMF World Economic Outlook, April 2007.

In 2006, the Comoros recorded growth of 2.4% (compared with 2.8% in 2005). This slight decline was the result of a fall in exports of the main cash-generating products and persisting socio-political uncertainty.

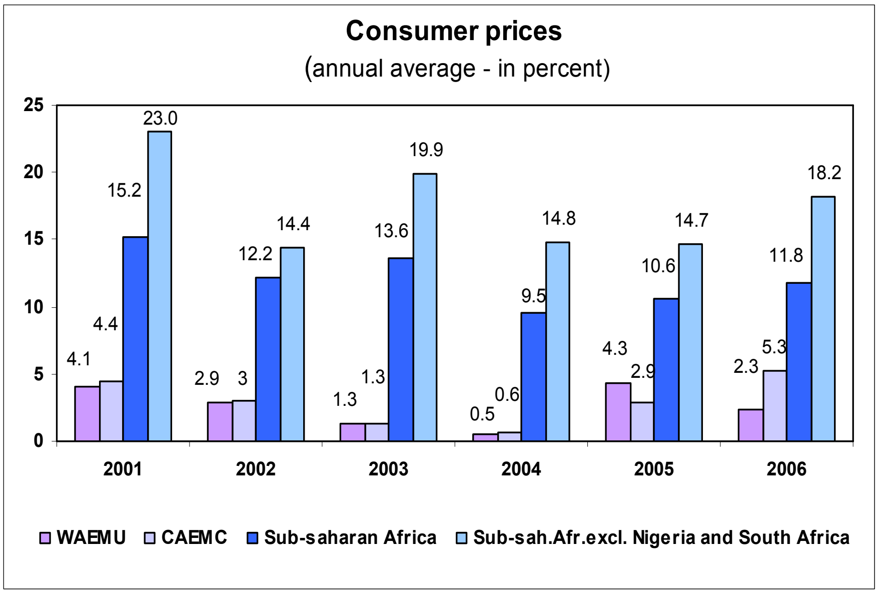
In terms of prices, 2006 was marked by contrasting developments in the two sub-regions: inflation accelerated in the CAEMC (5.3%, after 2.9% in 2005), while in the WAEMU it fell significantly (by 2.3%, after 4.3% in 2005). In Central Africa, the increase in inflation resulted primarily, to varying degrees depending on the country, from the rise in hydrocarbons prices and the insufficient supply of local crops and cereals. In addition, the monetary and fiscal environment (with ample bank liquidity and substantial oil surpluses fuelling domestic demand) is conducive to the build-up of inflationary pressures. In West Africa, the marked slowdown in price rises is attributable to the increase in local crop and cereal production in 2005–2006. This slower pace of price rises was however partly offset by the increase in the prices of fuel and transport.

In the Comoros, the good performance of local crop production did not enable inflation to be reduced, with the latter remaining above 3% (3.4% in 2006, after 3.2% in 2005).

In 2006, the Franc Area continued to post better results as regards fighting inflation than Sub-Saharan Africa as a whole, where it stood at 11.8%. The Franc Area's performance in terms of inflation is well established: between 1997 and 2006, the average annual inflation rate stood at 2.3% in the WAEMU and 2.4% in CAEMC countries, whereas it was around 12% for Sub-Saharan Africa as a whole.[1]

This lower inflation can primarily be attributed to the nominal pegging of the CFA and Comorian francs to the euro. Franc Area countries thus benefit from the low level of inflation in the euro area, which curbs the rise in the price of imports from this anchor area, and from the stability of their currency, which helps to contain the cost of their imports, notably energy imports, from the rest of the world.

[1] However, excluding Zimbabwe which has been facing hyperinflation, the inflation rate in Sub Saharan Africa was 7.2% in 2006 (source: IMF). Therefore, since 2004, the differential tended to contract, in particular for the CAEMC.



Sources: Central banks, IMF World Economic Outlook, April 2007.

Irrespective of the exchange rate regime, the quality of macroeconomic policies remains the key determinant of economic performance. In particular, the soundness and credibility of the peg of the CFA and Comorian francs to the euro benefit from the vigilant monetary policies conducted by Franc Area central banks. Sound and balanced fiscal policies are also crucial in this regard.

The Banque Centrale des États de l'Afrique de l'Ouest (BCEAO, Central Bank of West African States) has pursued its policy focused on consolidating external assets and price stability. In August 2006, against the backdrop of rising oil prices and the increase in intervention rates by the main central banks, the BCEAO raised its key interest rates by 25 basis points. Moreover, in early 2007, for the first time since 1998, it reverted to an active open market policy, with a view to steering rates on the money market.

The monetary policy of the Banque des États de l'Afrique Centrale (BEAC, Bank of Central African States) remained focused on curbing inflationary pressures and promoting sustainable growth. In 2006, the money supply in CAEMC countries expanded at a rate of 18.5% mainly on account of the sharp rise in net external assets. The BEAC thus raised its minimum reserve coefficients in Cameroon, Congo, Gabon and Equatorial Guinea. As from May 2007, it adopted an active management approach to excess liquidity by increasing the volume of liquidity withdrawals from banks, in line with their bids. In addition, following the 25 basis point cut in March 2006, the BEAC no longer altered its key rates.

In the Comoros, the money supply shrank by close to 6% in 2006 after having recorded an upward trend in 2004 and 2005. Since 1999, the key rates of the central bank have been linked to the EONIA. In 2006, the interest rate on savings accounts and passbook accounts was lowered from 3% to 2.5%.

Furthermore, the monetary authorities of the WAEMU and the CAEMC decided (respectively in 1998 and 2001) on the principle of phasing out the direct advances made by central banks to the government. In the WAEMU, this reform, which reflects the determination to increase fiscal discipline in the community, was launched in 2003 and has been accompanied by the rapid development of a regional public debt market *(see the study in part 4 of this report)*.

The budget surplus of the CAEMC (on an accrual basis, including grants) posted a further increase, rising from 8.8% of GDP in 2005 to 11.7% in 2006. This improvement is chiefly due to the surge in oil revenues, which grew by 48%.

In the WAEMU, the government deficit dipped from 2.8% of GDP in 2005 to 2.5% in 2006. This reduction is due to enhanced tax recovery, albeit strongly offset by a pronounced increase in public spending, in particular (like in the CAEMC) by often record levels of transfers to sectors experiencing difficulties and subsidies to the population. Some countries, in particular those that have not yet benefited from the debt relief and cancellation initiatives (Côte d'Ivoire, Guinea-Bissau, Togo), continued to experience cash flow pressures, which led to the accumulation of further external payment arrears.

In the Comoros, the consolidation of public finances started in 2005 was discontinued and the country recorded a budget deficit of 2.4% of GDP, after a 0.1% surplus in 2005.

Current account balance

	Current account balance (% of GDP)		Change in the terms of trade (%)	
	2005	2006	2005	2006
WAEMU	– 5.9	– 4.2	– 5.4	+ 3.4
CAEMC	+ 1.3	+ 1.6	+ 24.7	+ 18.4

Change in the terms of trade: (+) = improvement
Sources: Central banks, AFD, April 2007 Jumbo report.

As regards the external accounts *(see also, in the present report, the boxes on the Franc Area external trade over the last 10 years)*, the current account surplus of CAEMC countries posted a further rise to stand at 1.6% of GDP in 2006. Despite a 4.3% dip in export volumes, oil sales were up by 17% in value terms. The increase in the trade surplus was partly offset by the decline in the income and services balances.

In the WAEMU, external accounts also improved given that the current account deficit fell back to 4.2% of GDP. After having recorded a deficit in 2005 for the first time since 1993, the trade balance posted a small surplus as a result of the rise in oil sales in Côte d'Ivoire. The current transfers surplus increased further on the back, in particular, of higher remittances from migrant workers.

The foreign exchange reserves held by the central banks of African Franc Area countries continued to expand. They represent roughly five months of imports in the WAEMU and the CAEMC and seven months in the Comoros. The ratio of money in circulation to external assets largely exceeds the mandatory Franc Area threshold of 20%, to stand at 117% in the WAEMU, 95% in the CAEMC and 113.6% in the Comoros.

Overall, the regional convergence process is still insufficient in the Franc Area. As regards the CAEMC, the degree of compliance with the criteria of multilateral surveillance worsened significantly: at end-2006 no country met the four first-level criteria [2]. In the WAEMU, only one country (Niger) succeeded in meeting the four first-level criteria set by the Commission of WAEMU [3]. In the Comoros, none of the four first-level convergence criteria was met.

Yet, strict economic discipline goes hand in hand with sound monetary policy. Indeed, monetary integration is not sufficient to lay the foundations for optimal growth. Fiscal policies also need to be co-

2 Fiscal position, inflation rate, public debt outstanding as a percentage of GDP, change in payment arrears.

3 See previous note.

ordinated in order to ensure that national budgets are left with sufficient room for manœuvre to counter the asymmetric shocks with which the Franc Area is often faced. In this respect, African Franc Area countries are currently enjoying an environment conducive to the adoption of cautious and effective fiscal policies based, for oil producing countries, on the sustainable management of their surpluses and, for the beneficiaries of the Multilateral Debt Relief Initiative (MDRI), on the significant reduction in their external debt servicing.

Structural reforms (privatisations, transparency of public funds, restructuring of the banking system, sustainable management of natural resources, etc.) are also a means for the authorities of strengthening the growth potential of the domestic economies. Despite the progress recorded in some sectors and some countries, these reforms were, on the whole, still slow in 2006, even though there is a general consensus on the need to improve the business environment in order to encourage local and foreign investors and to enhance the Franc Area's ranking on the global scene.

In an environment still characterised by a large number of regional geopolitical uncertainties and exposed to exogenous shocks, the Franc Area mechanisms continued to act as an essential stabilising force for the cohesion of the Area. First, solidarity between Member States, via the pooling of foreign exchange reserves in each issuing area, has made it necessary to introduce multilateral surveillance which greatly encourages a rigorous management of public finances. Second, the principle of free-transferability and the unlimited currency convertibility within the Franc Area render economic and monetary trade flows all the more easy and thus act as an incentive for investment. Lastly, the contingency measures accompanying the co-operation agreements with France guarantee that monetary policy shall be conducted with the necessary vigilance with regard to the risk of inflationary pressures.

Franc Area institutions therefore provide a framework conducive to regional integration and economic development. As regards the WAEMU, the implementation of the Regional Economic Programme (2006-2010), aimed at the development of regional infrastructures and the construction of an integrated productive system, should eventually benefit economic activity and trade.

According to the BEAC, economic activity in CAEMC countries should expand significantly in 2007, with the growth rate coming close to 5%. Growth is expected to be mainly underpinned by the buoyancy of the non-oil sector. Inflationary pressures are expected to decline and the increase in consumer prices should reach 3.8%.

According to the BCEAO, economic activity in the WAEMU should grow at a relatively moderate pace (4%). Several important sectors (energy, cash crops, chemicals) experience difficulties that weigh on the activity, and need to undergo restructuring, sometimes already underway. Despite major advances, investors are still displaying a wait-and-see attitude on account of the socio-political situation in some countries. Lastly, despite the drop in the price of cereals, the inflation rate should remain above 2%.