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Republic of Cameroon

Joint Staff Advisory Note on the Poverty Reduction Strategy Paper Third Annual Progress Report

Prepared by the Staffs of the
International Monetary Fund and the International Development Association

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I. Overview

1. **In February 2006, the authorities submitted their Third Annual Progress Report (hereafter, "the Report") covering PRSP implementation during 2005.** It covers a period of improved fiscal performance and accelerated implementation of structural reforms but a deceleration of economic growth. As in the Second Annual Progress Report (APR), this Report focuses on a listing of ongoing and planned actions and provides only limited analysis of results. Due to the short interval between the completion of the present Report and the Joint Staff Advisory Note (JSAN) of the Second APR, this Report does not reflect much of the advice given by staff in the last JSAN, particularly on content and focus.

2. **The staffs welcome the Report's candid review of achievements and obstacles in the implementation of the PRSP since January 2005 in a crisper and more focused fashion than the previous APR.** The staffs suggest that the next APR, which would probably come after the completion point under the enhanced HIPC Initiative, should focus not only on actions but on results, discuss the 2006 budget execution and the 2007 macroeconomic objectives and budget, and highlight the plans for structural and governance reforms for the post-completion point period. This JSAN is organized in eight sections. Sections II to VI cover the key priority areas of the PRSP, while section VII provides some guidance on the PRSP monitoring and section VIII concludes.

II. Enhancing Macroeconomic and Fiscal Management

3. **The Report highlights the substantial improvement of the fiscal position and the strengthening of fiscal management in 2005.** The staffs acknowledge that fiscal policy implementation and performance strengthened substantially in 2005, accompanied by better

management of budget execution. The overall fiscal balance is estimated to have improved by about 3.8 percentage points of GDP in 2005, with an increase in oil and non-oil revenue and control over current spending. Also, for the first time in several years, domestically-financed investment reached its target although foreign-financed investment again fell short reportedly because of insufficient domestic counterpart funds. Tax administration was strengthened; fiscal reporting improved; direct spending by the national oil company (SNH) on behalf of the government was phased out; and quasi-fiscal losses at the public refinery (SONARA) were avoided by a combination of increases in fuel prices and transparent subsidy payments. The staffs believe that efforts need to continue to make the government budget a more effective instrument for accelerating growth and poverty reduction:

- **Budget preparation.** The staffs commend the recent acceleration in the development of sector strategies and Medium Term Expenditure Frameworks (MTEFs). In 2005, new strategies were adopted in a number of areas including telecoms, public works, social development and tourism, while the education and rural sector strategies were updated. The 2006 budget is broadly consistent with the PRSP priorities. The staffs recommend that sector MTEFs in all priority sectors be linked to a global MTEF as they become available and integrated into the annual budget, thereby helping to further improve the alignment of future budgets with the PRSP.

- **Revenue and expenditure.** The authorities need to continue strengthening tax and customs administration, including through consolidating progress at the large taxpayer unit, increasing taxation of the informal sector, and introducing the Automated System for Customs Data. The authorities also need to continue increasing the execution rate of investment projects, including by further improving investment planning and project selection. The strengthening of payroll management should also be a priority, given the substantial shortcomings that have become apparent in recent months.

- The staffs note a need for improving **budget effectiveness**, by further modernizing budget implementation procedures, improving the accounting and financial reporting systems, as well as strengthening the financial oversight framework and capacity.

4. **The Report did not address a few key issues regarding budget execution and policy, including:**

- an assessment of the quality of the 2005 investment;

- a deeper discussion of issues related to the use of interim HIPC debt relief even if the rate of spending of HIPC resources accelerated in 2005; and

- an in-depth discussion of 2006 macroeconomic policy intentions and the budget.

5. **The Report indicates a number of actions taken to improve procurement within the framework provided by the Procurement Code adopted in 2004.** These include the adoption and publication of the implementation decree of the Code in June 2005, its dissemination in the

provinces, the preparation and dissemination of the manual for bids, and the launching of the audit of public contracts executed in 2004. Other important actions, not discussed in the Report, include the adoption of standard bidding documents to be used by all contracting entities, and the adoption of an action plan to strengthen the implementation of the Code over the next three years. A recent joint World Bank/government review of procurement operations in 2005 concluded that the foundations of the system are in place, but implementation remains weak, hence the adoption of this action plan. The actions include the implementation of (i) a capacity building program; (ii) contract administration and dispute resolution provisions; (iii) ethics and anti-corruption measures to enforce compliance with the Code; and (iv) a monitoring and evaluation component for an annual assessment of the performance of the procurement system. The staffs encourage the government to swiftly implement this action plan.

III. STRENGTHENING GOVERNANCE

6. **The Report indicates that the government has implemented actions to improve governance and strengthen transparency and accountability across the public administration.** The government adopted an updated national governance program in November 2005 and prepared a priority implementation plan, with emphasis on delivering results. The staffs note that the newly adopted governance priority action plan aims at consolidating ongoing efforts to strengthen the judiciary system, fight corruption, and improve transparency and accountability in public finance management. A number of other actions were taken in 2005. In the judicial sector, magistrates were recruited and trained, measures against money laundering have been taken, and a new penal procedures code, aimed at improving the delivery of judicial services and the protection of human rights, was promulgated in July 2005. The external audit body for public finance (*Chambre des Comptes*) became functional in early 2006 but needs to be strengthened. The staffs recommend that its mandate be expanded to be in line with the International Organization of Supreme Audit Institutions (INTOSAI) norms.

7. **The Report reflects recent actions on decentralization and local development.** However, the Report would have benefited from laying out the rationale of and the implementation strategy for decentralization. Also, the Report could have discussed some critical constraints on implementation, namely weak coordination mechanisms at the national and sub-national levels, as well as between administrations at these levels, the government and development partners; lack of an organizational framework for the elected local government and communal staff; and weak operational, financial and management capacities of municipalities. The staffs note that the authorities have prepared and are implementing an action plan based on the recommendations of the audit report of the FEICOM (the special fund for the financing of local governments) and urge the authorities to separate FEICOM's functions as a municipal bank from its role in public contract management.

8. **Staffs reiterate the importance of financial and other sanctions against transgressions of the laws and regulations and welcome the government's recent and significant efforts in this area**. The staffs welcome the actions discussed in the Report aimed at enforcing the rule of law and reducing corruption, including the wider use of sanctions. The Report indicates that forestry titles were withdrawn from three private operators who failed to pay their deposits. It also notes that regular consultations have been taking place between the

Ministries of Forestry, Finance and Justice for improving the monitoring of litigation cases. To enhance such monitoring, the staffs recommend that the software designed to supervise litigation cases should be made fully operational within the three above mentioned ministries. The staffs welcome the recent measures to clean the payroll and to sanction cases of misconduct in the judiciary and procurement operations and to crack down on corrupt public officers. The staffs encourage the authorities to continue these efforts in a manner consistent with the due process of the law.

9. **Despite recent steps, governance remains weak.** Transparency International's Corruption Perception Index for Cameroon in 2005 remains very low at 2.2 (on a scale of 0 to 10, with a higher number indicating better governance), although this is an improvement over the 2.0 rating reached in 2000. The staffs welcome recent actions on corruption, but urge the authorities to apply anticorruption laws systematically. Steps are urgently needed to strengthen the judiciary, including through the provision of sufficient budget allocations and the recruitment and training of more qualified personnel.

IV. CONSOLIDATING GROWTH AND THE DIVERSIFICATION OF THE ECONOMY

10. **The Report duly notes the slowdown of economic activity in 2005, with a decline of GDP growth from 3.7 percent in 2004 to 2.6 percent in 2005.** It ascribes the growth deceleration mainly to the compression of households' purchasing power following the 2005 increase in VAT and excise tax rates. The staffs are of the view that the slowdown is also due to supply shocks (e.g., contraction of agro-industry and forestry production), as well as lower-than-programmed public investment. Against this background, the staffs call on the authorities to redouble their efforts to remove the impediments to public and private investment.

11. **While the Report does not include updated medium-term macroeconomic projections, the framework contained in the authorities' Second Annual Progress report of September 2005 remains broadly appropriate.** The medium-term macroeconomic outlook has not changed fundamentally in recent months, in spite of a moderate upward revision of oil output and oil exports projections for 2007 and later.

12. **The Report indicates a number of actions taken by the authorities to strengthen private sector development,** including the creation of public/private partnerships in the energy and agro-industry sectors and negotiations with the international conglomerate, ALCAN, for the expansion of the aluminum production. The staffs encourage the government to conduct supply chain analysis of potential growth areas (agro-industry; manufacturing; financial services; information technology; oil, gas, mining and petrochemicals with specific analysis of the scope of bauxite and aluminum activities; transport services; and tourism) to gauge the scope for economic diversification. More generally, the staffs encourage the government to use the findings of the ongoing investment climate assessment survey (ICA) and the Reports on the Observance of Standards and Codes (ROSC) to develop policies and actions aimed at improving the business environment. The survey will examine impediments to private sector activities stemming from the taxation and trade regime, red tape, time needed to obtain a license and start a business, labor issues (costs, labor laws and training), collateral, arbitration, and status of the judicial system. Without prejudging the results of the survey, the staffs agree with the Report's

view that weak governance and the poor state of basic infrastructure weigh heavily on the business environment.

13. **The government has updated its rural strategy and elaborated a MTEF for the Ministry of Agriculture and Rural Development**. The Report highlights some actions taken in 2005 to train targeted rural communities in technological innovations and to strengthen the capacity of private operators in the production of selected crops. These actions, undertaken on a pilot basis, have shown some success and support from the donor community would be sought to scale them up, with the involvement of rural producer associations.

14. **The Report notes a number of actions taken in 2005 to deepen financial intermediation,** including the launching of activities at the Douala Stock Exchange through the quotation of negotiable government securities and bonds issued by the Urban Community of Douala; the production of initial studies on the creation of a private agriculture bank; and the elimination of 182 microfinance establishments that did not comply with COBAC rules. The staffs welcome the favorable opinion given by the COBAC to 232 compliant microfinance establishments as well as the closure of non-compliant microfinance institutions and encourage the authorities to maintain an effective regulation and supervision of the microfinance sector. However, the staffs note that in light of CEMAC's project to create a regional stock exchange in Libreville, the establishment of a stock exchange in parallel in Douala could pose challenges for the development of one or both of them. The staffs note that the proposed agricultural bank is to be established with private capital and, given the poor record of such specialized institutions in the past, urge the authorities to proceed with caution in supporting this institution.

15. **The Report indicates that the government is committed to continue the reforms of the forestry sector with the support of its development partners.** The Report highlights the efforts made by the government to strengthen implementation of forestry reforms, and the recent support provided by development partners to support the implementation of these reforms. The staffs welcome these developments. However, they remain concerned that in the absence of strong supervision of tight enforcement of the forestry regulations, community forests and small logging permits may be used to serve vested interests and fuel illegal logging, to the detriment of local communities. The staffs recommend that the government review and clarify all aspects related to the award and use of community forests and small logging permits.

16. **With regard to infrastructure, the Report notes that the government is giving high priority to physical infrastructure including strengthening service delivery by key utilities.** The staffs are encouraged by signs that the restructuring and privatization of public enterprises involved in the provision of infrastructure called for in the last JSAN has gained momentum in 2005, and that the government is committed to increase public investments in infrastructure including through Public Private Partnerships (PPP) for infrastructure. The staffs recommend that the government begin an in-depth discussion of PPP models and approaches. The Report highlights a number of actions underway in the infrastructure sector:

- **In the transport sector,** like the previous APR, this focus of the report is mostly on the road sector, with little if no consideration to the other transport modes. **On roads**, the Report reflects well the government's actions: adoption of a road strategy and

MTEF, with increased amounts to maintenance and investment funding for the sector in line with the commitments made with the donor community. **On ports,** an independent evaluation of port reform will be undertaken in the first half of 2006 to assess the actual gains of the reform and prepare follow-up actions to strengthen the implementation of the overall port reform. **On air transport,** the staffs note that progress in the preparation of the scission/liquidation/privatization of the national air carrier CAMAIR remains satisfactory. The authorities have started to implement the strategy as per the recommendations of the strategic option report prepared with the assistance of the International Finance Corporation.

- **Regarding electricity**, the government is putting in place the conditions for strengthening the electricity sector. The government has renegotiated the concession agreement with the private operator, adopted the National Energy and Poverty Reduction Action plan and nearly finalized the 2006-30 least cost sector investment plan. The staffs encourage the authorities to restructure and strengthen the capacity of the regulatory agency and to assess in a transparent manner the financially sustainable sector investment needs.

- **In the telecommunication sector, preparations for the privatization of CAMTEL are proceeding.** The authorities have launched the prequalification process in 2006. The staffs recommend that the redeployment of CAMTEL's civil servants and the finalization a comprehensive financial restructuring package be addressed before the end of the bidding process period. However, in early 2006, the staffs have been informed about the authorities' decision to create an asset holding company. The staffs have expressed serious concern about this proposal which risks jeopardizing the success of the transaction and strongly recommend the authorities to maintain the privatization framework as initially envisaged in the strategy adopted in December 2005. The staffs also encourage the authorities to restructure and strengthen the capacity of the telecommunications sector regulatory agency.

- **In the postal sector**, the staffs note that the government, while engaged in the restructuring of CAMPOST, has yet to finalize the sector policy and the selection of the CAMPOST management contract team. The staffs also encourage the government to quickly complete the liberalization and regulation strategy for the postal sector, in particular to define the government's objective relative to the universal service obligation.

V. ENHANCING SOCIAL SERVICES DELIVERY TO IMPROVE STANDARDS LIVING CONDITIONS

17. **In the education sector, the Report noted a number of performance improvements.** Among the achievements are increases in the ratio of enrolled girls to boys, gross enrollments in basic and secondary education, and success rates in national exams at secondary levels, and progress in the efforts to decentralize the management of teachers. In addition, the Report emphasizes significant investments in education facilities at the basic, secondary and technical levels. The staffs note that there have also been significant institutional reforms aimed at improving the governance of tertiary education. However, key indicators of performance in the

education sector have not improved as quickly as envisaged by the PRSP; for instance, the completion rate of basic education has remained unchanged at 56 percent since 2001, reflecting the persistence of high repetition rates, which have remained around 25 percent of total basic and secondary education enrollment. The recent adoption of modern assessment procedures is expected to help reduce repetition in primary education. The staffs remain concerned about the government's intention to convert 1,700 contractual teachers into regular civil service positions without a clear policy framework for dealing with the 12,000 remaining contractual teachers. The staffs recommend that this question be addressed in the education strategy document under preparation. This strategy should be discussed with the donors, and presented to the Education Fast Track Initiative to raise funds before the end of the first half of calendar year 2006.

18. **With respect to health services delivery, the Report provides a balanced picture of recent progress in implementing the government's health sector strategy, with specific details on achievements of different programs.** The Report also assesses progress made in implementing some previous recommendations such as expanding the contracting of NGOs (e.g., for HIV prevention) and lowering the cost of treatment for AIDS patients. The staffs recommend that the government intensify the measures to redress inequities in access to health services during the next year by: (i) better targeting of underserved areas better; (ii) further rationalizing the system of user fees and drug policies; (iii) expanding risk sharing mechanisms; and (iv) continuing to assign more personnel to rural areas. The staffs also suggest that a broad-based consultative process be launched on a sector-wide approach (SWAP) for the health sector to guide the implementation of the government's health strategy and ensure the coordination and alignment of donor assistance.

19. **The Report indicates that substantial progress has been made in the provision of potable water to households, with access rates increasing over the 2001-05 period.** The staffs welcome this progress and urge the government to sustain its efforts to make further improvement in this important area. The Report notes that the government has made progress in the establishment of the public private partnership to manage the provision of water services. The staffs consider that the government has put in place proper institutional arrangements. The asset holding company, CAMWATER, will be in charge of carrying investment responsibilities whereas the private partner will operate the facilities and deliver services under the lease contract. In this regard, the staffs note that substantial commitments have been obtained from donors to help fund the investment and the capacity strengthening programs once the concession arrangement becomes operational.

VI. FOSTERING REGIONAL INTEGRATION

20. **The Report's description of progress in fostering regional integration agenda in the Central African Economic and Monetary Community (CEMAC) could have been more nuanced.** The Report notes a number of steps taken to support regional integration, including compliance with the multilateral surveillance criteria and Cameroon's support for connecting the CEMAC road network, electricity grids, and telecoms networks; however, these regional connections remain at an early stage. The Report also notes that the common external tariff has been reduced to four categories with a maximum of rate of 20 percent. The staffs are of the view that this action is still under discussion at the regional level and urge the authorities to move

forward on this measure, which has long been advocated by the staff of the Bank and the Fund. Further, the Report provides a preliminary analysis of the impact on the Cameroonian economy of the forthcoming Economic Partnership Agreement (EPA) between the EU and the CEMAC. The assessment focuses on the potential adverse impact on Cameroonian industry and government revenue of lower import tariffs. A future analysis could be deepened to consider the benefits of this reform. The staffs urge the Cameroonian authorities to capitalize on its leadership position to further advance regional trade integration.

VII. Institutional and Statistical PRSP Monitoring

21. **The government is taking a number of actions to strengthen PRSP implementation**. First, it is committed to generalize the use the MTEF in the 2007 budget preparation to enhance PRSP implementation. Second it is organizing regular consultations with private sector and civil society and is preparing a national workshop on the economy ("*états généraux*"), scheduled during the first semester of 2006, to launch the debate on the post completion point growth strategy as a higher volume of resources would be made available through the HIPC and MDRI initiative. Third, it has enhanced its leadership in aligning and harmonizing donor support on PRSP pillars on the basis of the Paris Declaration on Aid Effectiveness. To this effect, the government plans to develop a new partnership framework based on the ongoing independent aid assessment. These various inputs along with the newly adopted or revised sector strategies would serve as critical input in the formulation of the second PRSP.

22. **The staffs commend the efforts to assess poverty and living conditions based on information provided by the recent survey on employment and the informal sector (EESI).** Though a recent household survey is not available, the Report tries to assess changes in household income based on GDP growth, the level of public wages and trends in the prices of important agricultural goods. To gauge progress in living conditions, the Report also draws on the recent Demographic and Health Survey (DHS) and EESI to assess changes in access to housing, services (water, electricity, cooking gas) and ownership of durable goods (bicycles, radio, television). Finally, the Report tries to characterize urban poverty in the presence of a growing trend towards urbanization.

23. **The staffs welcome ongoing efforts to strengthen the program of statistical surveys and participatory monitoring mechanisms**. The Report presents a comprehensive program of statistical surveys and participatory monitoring mechanisms. The staffs welcome the ongoing study on the formulation of a formal methodology for participatory monitoring and hope that this study will develop a variety of instruments that will improve and facilitate monitoring, strengthen ownership and widen participation.

VIII. Conclusion

24. **Progress in PRSP implementation accelerated somewhat in 2005 as the government intensified its efforts in a number of areas, including fiscal policy, governance, structural reforms, and social policies.** Prospects for 2006 are encouraging provided the government continues to build on the progress made in 2005 and strengthens implementation to achieve more tangible results on the ground. In particular, the staffs note the critical importance of the following issues: (i) the elaboration and implementation of a public financial management action

plan, in concert with the donor public finance platform; (ii) the implementation of the National Governance Action plan; (iii) the acceleration of public enterprise restructuring/privatization program; (iv) the improvement in the execution of public investments, and (iv) the strengthening of the provision of basic social services through better targeting of actions and expenditure and the implementation of the improved evaluation methods in primary education for sustained reduction of repetition rates.

Issues for Discussion by the Board

- Concerted efforts were made in 2005 to improve Cameroon's fiscal position, in sharp contrast with the slippages registered in 2004. Learning from this experience, the priority in the fiscal area going forward is further strengthening tax and customs administrations, improving the accounting and financial reporting systems, and reinforcing the financial oversight framework and capacity. Directors might wish to discuss this challenge and provide further guidance on what needs to be done to prevent fiscal slippages from reoccurring.

- Improving governance is one of the pillars of the PRSP and arguably the most critical challenge facing Cameroon. The government has recently started to crack down on corruption—by sacking, indicting, and imprisoning senior public officials—indicating its intention to move ahead faster in this area. The government has stressed its commitment to enhance and sustain these efforts in the post-HIPC completion point period. Directors might wish to discuss this challenge and provide further guidance to the efforts to improve governance in Cameroon.

- Cameroon's relationship with the donor community has been weak and the government is working to strengthen this relationship and build a partnership for development. An independent body is in the process of developing a partnership framework for consideration by the government and the donors. Directors might wish to provide insights into this process.