

INTERNATIONAL MONETARY FUND
AND
INTERNATIONAL DEVELOPMENT ASSOCIATION

REPUBLIC OF SENEGAL

**POVERTY REDUCTION STRATEGY PAPER— SECOND ANNUAL PROGRESS REPORT
JOINT STAFF ADVISORY NOTE**

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and the International Development Association

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I. OVERVIEW

1. **Senegal's poverty reduction strategy paper (PRSP), covering 2003–05, was distributed to the Executive Boards of IDA and the IMF in October 2002, after endorsement by the Presidential Council in July 2002.**¹ The joint staff assessment concluded that Senegal's PRSP provided an adequate framework for fighting poverty and endorsed its four pillars: (i) wealth creation; (ii) capacity building and the provision of basic social services; (iii) improving the living conditions of vulnerable groups; and (iv) monitoring and evaluation.² The PRSP was welcomed by the Executive Boards in December 2002. Senegal's first annual PRSP Progress Report³ was reviewed in a joint staff advisory note in December 2004.⁴

2. **Senegal's second annual PRSP Progress Report (hereafter the Report) covers the implementation of the PRSP during 2004 and examines prospects for 2005.** The staffs note that the authorities made some progress in addressing some of the major

¹ www.imf.org, www.worldbank.org: Senegal–Poverty Reduction Strategy Paper, 2002.

² www.imf.org, www.worldbank.org: Senegal–Poverty Reduction Strategy Paper–Joint Staff Assessment, December 2, 2002.

³ www.imf.org, www.worldbank.org: Senegal–Poverty Reduction Strategy Paper Progress Report, March 2004.

⁴ www.imf.org, www.worldbank.org: Senegal–Poverty Reduction Strategy Paper–Annual Progress Report Joint Staff Advisory Note, December 6, 2004.

methodological shortcomings that were identified in the first JSAN: (i) they developed a detailed analysis of the linkages between the allocation of resources within the budget and the PRSP priority sectors; (ii) they identified and used a series of quantitative indicators to monitor progress over time; and (iii) they strengthened the participatory process with donors, civil society, local governments, and the private sector, most notably during the evaluation and preparation of the Report.

3. **The Report acknowledges the uneven implementation of the PRSP in 2004 and highlights persistent weaknesses in key areas.** It takes note of the progress realized in strengthening the first pillar with appropriate macroeconomic policies, improvements in the investment climate through tax, regulatory and administrative reforms, and structural reforms in the groundnut sector. Yet, it also recognizes that further progress is needed to foster a sustained rise in private investment and exports. Concerning the second pillar, the Report points to progress in health and education, but at a pace (especially in health) that might not be sufficient to attain the MDGs. The authorities also emphasize their need to consolidate fiscal transparency as well as strengthen internal and external budgetary controls. Regarding the protection of vulnerable groups, they report that increasing funds were allocated to support children and women but that there were gaps in programs supporting handicapped and elderly as well as the development of infrastructure benefiting the poorest segments of the population. The authorities have started to address these deficiencies in the course of 2005, paving the way to a new three-year PRSP to be ready in early 2006.

II. PROGRESS WITH POVERTY REDUCTION POLICIES AND PROGRAMS

A. Macroeconomic Policies

4. **The Report indicates that the authorities continued to implement appropriate macroeconomic policies in 2004.** Despite rising petroleum prices and the adverse consequences of the locust invasion, the government maintained its focus on enhancing revenue mobilization and a tight control on current expenditure, while allowing for further increases in capital and pro-poor spending. Supported by this fiscal stimulus and a moderate easing of monetary conditions by the Central Bank of West African States, real GDP growth exceeded 6 percent, with the telecommunication and construction sectors as best performers. Inflation remained subdued, with the annual average CPI rising by about 0.5 percent. In spite of the increase in the price of oil, the external current account deficit (including grants) stabilized at about 6.7 percent of GDP, as private remittances grew.

5. **The fiscal stance remained consistent with the authorities' goal of preserving debt sustainability even though the overall fiscal deficit increased to 3.3 percent of GDP in 2004.** This fiscal weakening reflected mainly an increase in capital expenditure and a deterioration of the balance of selected public sector entities. Capital spending financed externally, in particular, increased by about 0.7 percent of GDP, as donors simplified disbursement procedures and a number of projects reached peak activity.

6. **Looking forward, it is crucial to achieve better public expenditure management to ensure the efficiency of additional investment spending.** Further

increases in capital outlays (which have grown from 7 percent of GDP in 2001 to more than 10 percent of GDP in 2004) need to be accompanied by better investment planning, evaluation—including thorough feasibility analysis for large projects—and monitoring to raise the productivity of investment. Stricter enforcement of procurement rules, including by autonomous expenditure-executing agencies, is also necessary to improve the efficiency of public spending.

7. **The next PRSP should continue to be based on realistic growth assumptions.** Based on the IMF staff estimates, the growth performance expected for 2003–05 (about 5.9 percent on average) under current policies will fall short of the middle-case growth PRSP scenario of the 2002 PRSP (6.5 percent on average over the same period) and the trend growth of about 7 percent needed to reach the Millennium Development Goal (MDG) of halving poverty by 2015. In response, the authorities have launched an accelerated growth strategy, which aims at increasing annual real GDP growth beyond 7 percent (see paragraph on policies to promote wealth creation). Until this strategy starts to bear fruit, the staffs recommend that the authorities continue to program their financial policies based on more conservative growth scenarios, and maintain their efforts to mobilize domestic resources at a level consistent with their medium-term priority investment program.

B. Poverty Reduction

8. **While updated poverty data are not available in the Report, there are indications that poverty continued to decline in 2004.**⁵ In the absence of new household surveys, the government estimates that the incidence of poverty was reduced from about 57 percent in 2001 to 54 percent in 2004.⁶ However, the Report does not fully spell out the policy implications of the concentration of poverty in rural areas, which may require greater financial resources for local governments to carry out in full the functions for which they have been made responsible by law since 1996. The mechanics for transferring resources from the central government to local governments is inefficient and needs to be made simpler and more predictable. Also, significant training and capacity building at the local levels will be required so that the central government will feel confident that the transferred financial resources will be well used. Lastly, an effort should be made to enhance the development of new private activities in the regions, especially small and medium firms, through improved access to credit and commercial information.

⁵ The most recent comprehensive analysis of poverty in Senegal—based on data from the household survey of 2001/02—suggested that the share of the population living in poverty decreased from 67.9 percent in 1994 (61.4 percent of households) to 57.1 percent in 2001 (48.5 percent of households). (See IMF Country Report No. 05/114, page 51 and IMF Country Report No. 05/115, paragraph 13).

⁶ Poverty indicators are projected according to estimated elasticity parameters and the observed growth of real GDP per capita. The projection assumes constant elasticity of poverty reduction to growth and inequalities since 1994.

C. Sectoral Policies

Policies to promote wealth creation

9. **Building on recommendations from the Presidential Investors' Councils, the authorities have improved the business environment by streamlining regulations concerning business registration and taxation.** The National Assembly adopted reforms that simplify the corporate income tax and investment codes in January 2004. The tax basis was widened by abolishing several tax exemptions, and for small enterprises a single tax was introduced to replace the income tax, the value-added tax, patent contributions, and social security charges. The new investment code streamlined the system of investment incentives and broadened the scope of sectors eligible to these incentives to take account of PRSP priorities.

10. **The Report notes that, in its effort to promote wealth creation, the government achieved significant progress in the groundnut and electricity sectors.** After two failed privatization attempts in 1995 and 1999, in March 2005 the authorities sold the groundnut processing and vegetable oil refining company (SONACOS) to the only bidder that made an offer. The government also suspended an import tariff on refined vegetable oil, in order to foster competition in the sector and reduce the price of a key staple for the poor. In the electricity sector, the government concluded the process of selecting a private independent producer (PIP) to increase generation capacity by 60MW (equivalent to about 13 percent). The contract was signed in February 2005 and the increase in production capacity is expected to come on stream in the latter half of 2006. The report, however, does not fully spell out the implications of these reforms for poverty, which should be encouraged in the next PRSP and progress reports.

11. **The Report emphasizes the growing attention paid to the PRSP first pillar by the government, and in particular, the development of an Accelerated Growth Strategy (AGS).** To accelerate growth, the government has selected five clusters with substantial growth potential, labor intensity, and external competitiveness: agriculture and agro-industries, fishing and fishing industries, tourism-art crafts and cultural industries, textile and clothing industries, and electronic customer support (ECS) services. The strategy consists of identifying growth constraints and implementing action plans to address them in close collaboration with enterprises active in each sector. The government adopted a roadmap describing the institutional framework and the timetable for the steps needed to allow implementation of the AGS by early 2006.

12. **Raising economic growth to a higher sustained level will require further progress with policies associated to the first PRSP pillar.** Such an effort is vital to boost private sector activities, investment and exports, and reduce the vulnerability of the Senegalese economy to external shocks. Further reforms are required in the electricity sector such as applying the new formula for setting electricity prices, which better reflects SENELEC's cost structure. The decision to cut electricity prices by 5 percent, in October 2004 in spite of the sharp rise in oil prices, weakened SENELEC's financial performance, thereby reducing the attractiveness of this key sector to potential investors. There is also a need to improve policies toward small groundnut producer—who are among

the poorest groups in Senegal—with a view to reducing their vulnerability to external shocks. The next PRSP should also discuss how the large infrastructure projects (*les grands travaux du Chef de l'État* such as the new airport and the Dakar-Thiès Highway), if found viable, will contribute to promote economic growth and equity in Senegal. The government needs to finalize its new AGS, not only by identifying a set of actions to be implemented at the sectoral level, but even more by making a further effort to address transversal issues that were identified by the Presidential Investor Council as structural impediments to private sector development. These include problems in the areas of justice, financing, administrative barriers, and labor skills, which are viewed as major obstacles by both local and foreign investors. Finally, attention should be given to actions aimed at facilitating procedures for realization of collateral that will be key to foster the contribution of banks to private sector development.

Policies to promote capacity building and basic social services

13. **Promoting capacity building has received increased attention from the Senegalese government, as it was well covered by the budget allocation in 2004.** The authorities have continued to implement their recruitment of 15,000 civil servants and launched a new remuneration strategy. They pursued the execution of two action plans supporting public expenditure management reforms (following recommendations of the Country Financial Accountability Assessment—CFAA and the Country Procurement Assessment Review—CPAR) that included the adoption of a new budget nomenclature, the simplification of expenditure channels through computerization, the improvement of cash and debt management, and the revision of the legal framework surrounding procurement and public-private partnerships (a new BOT law was adopted in April 2004). Following spending irregularities in 2003, which came to light in June 2004,⁷ the authorities have, in consultation with the World Bank and the IMF, adopted a series of measures aimed at improving procurement practices, including curtailing the use of emergency procedures (without competitive tender), and a revision of procurement laws with a view to removing loopholes which facilitated these spending irregularities. The implementation of these measures has not been fully satisfactory, notably in view of the recent steep increase in single tender contracts. A new procurement Code is expected to be adopted by end 2006.

14. **The allocation of spending toward social sectors continued to improve as both the combined shares of education and health expenditures in total public expenditures (33 percent) and in GDP (8 percent) increased (by about 10 percent) in 2004.** There is nonetheless room to improve budget alignment with the PRSP as only about two thirds of the actions identified in the PRSP were reflected in the 2004 budget. The report showed that progress occurred in the education sector with an increase in gross enrollment in primary schools from 77 percent in 2003 to 80 percent in 2004, and the construction of 1,103 new classrooms. Similarly, in the health sector, positive results were achieved such an increase in the DTC3 immunization coverage from 59 percent in 2003 to 75 percent in 2004, higher

⁷ These irregularities and the remedial actions implemented by the authorities are described in the Joint Staff Advisory Note (JSAN) on the first PRSP progress report (see IMF Country Report No. 05/115, paragraph 10).

primary care consultations (up by 8.7 percent between 2003 and 2004), and in the number of births assisted by trained personnel (from 54 percent in 2002 to 59 percent in 2004).

15. **The staffs welcome the attention given by the Report to the second PRSP pillar, but note that the government should address three major issues. First, there is a need to strengthen budgetary reforms and fiscal transparency.** In particular, significant upgrading is still required in the area of internal and external controls of budget execution—in particular timely ex post control by the audit court—and state-owned enterprises. There is also a need to develop the budget on a programmatic basis, which has been postponed to the 2006 budget law, prepare the Consolidated Investment Budget and the 3-year investment program using an economic classification of expenditures, and ensure consistency between the table of government financial operations (TOFE) and the budget. Moreover the risks to public finances associated with large infrastructure projects need to be fully reflected in fiscal accounts. Improvement in expenditure tracking is also necessary to ensure that budget lines are spent as intended. The authorities should continue their efforts in these crucial areas as they should lead to higher transparency, more financial resources, and a better allocation of spending, both at the central and local government levels.

16. **Second, there is a lack of progress in the implementation of the decentralization strategy, which contributes to the weak delivery of basic public services in remote areas.** Although the legal decentralization framework was adopted in 1996, the central government has been transferring only limited and declining financial resources to local governments (transfers declined from FCFA 17 billion in 2003 to FCFA 14 billion in 2004). Not only are these transfers insufficient to match increasing decentralized spending responsibilities, but they also continue to be based on complex and erratic allocation rules. The next PRSP should devote increasing attention to the implementation of the decentralization strategy, including the much-anticipated decentralization of the execution of the Consolidated Investment Budget and the rationalization of financial transfers through the adoption of clear and predictable rules. The PRSP should also emphasize the need for enhanced capacity building at the local level as a prerequisite for successful decentralization.

17. **Finally, the government should accelerate the pace of reforms in education and health so that these two sectors can reach their MDGs.** Although these two sectors benefited from substantial financial resources, the share of the budget devoted to health (around 8 percent in 2004) remained below the 9.8 percent objective called for in the PRSP. Concurrently, the government should continue to improve access and utilization of basic health services through the strengthening of outreach activities, the implementation of its infrastructure development plan, and the implementation of the regulatory and legal frameworks for private health service provision and funding. It should also reinforce priority actions in the areas of the prevention of infectious diseases and the utilization of reproductive health services. In addition, it is recommended to better coordinating cross-sectoral activities, such as access to drinking water and sanitation that have a significant impact on health. In the education sector, there is a need to improve quality and performance of secondary education.

Policies to improve the living conditions of vulnerable groups

18. **Vulnerable groups are numerous and diverse in Senegal, including children, handicapped, elderly, and refugees.** The PRSP emphasized the need to improve the lives of vulnerable groups and prescribed actions to ensure that these groups do benefit from wealth creation and access to social services.

19. **As noted in the Report, this PRSP pillar received uneven attention from the Senegalese government in 2004.** The lack of emphasis is reflected in the relatively weak allocation of budgeted resources to vulnerable groups, most notably handicapped and elderly groups, and to the development of infrastructure benefiting the poorest segments of the population. There is also the absence of specific monitoring indicators for this pillar in the list presented in the Report. On the basis of this diagnostic, the government has committed to develop a global and coordinated strategy for national social protection in 2005. This strategy should include a new priority action plan for the short and medium terms, a better identification of the most groups most exposed to major risks and catastrophes as well as a series of monitoring indicators. It has also announced its intent to launch a programmatic budgeting approach, which should help improve the efficiency of public spending in these social sectors.

III. MONITORING AND EVALUATION

20. **The government has placed evaluation and monitoring of its performance at the center of the PRSP.** During the course of 2004, the authorities reinforced the PRSP institutional framework, notably at the regional level, and sought to increase the participation of several stakeholders in the evaluation and the preparation of the Report. Yet, the Steering Committee, chaired by the Minister of Economy and Finance, only met once in June 2004, which is not enough to play its supervising and coordinating role. There is also a need to increase the participation of top government officials in the regular supervision and evaluation of the PRSP to foster ownership and momentum.

21. **Progress was realized with the finalization of a set of PRSP monitoring indicators through an intense dialogue with development partners operating in the country.** These indicators have been used to evaluate the implementation of the PRSP in 2004. Yet, coverage remains incomplete since: (i) statistical data are still missing in key areas such as rural roads and procurement; and (ii) there has been no specific indicator selected for monitoring progress in the living condition of the most vulnerable groups. The next PRSP should also indicate how the government intends to improve its capacity to monitor and analyze poverty determinants and outcomes across the country for the period after the latest national survey was carried out (2001/2002). Improving such capacity will enhance the government's effort to implement its PRSP agenda over the next few years.

IV. CONCLUSION

22. **Bank and Fund staffs believe that Senegal's second PRSP Progress Report provides a balanced assessment of the second year implementation of the PRSP.** The Report is comprehensive, highlights the risks ahead, and points to areas for further improvements. Significant progress has been achieved in strengthening the evaluation and monitoring process through (i) a detailed analysis of the budgetary alignment with PRSP priorities and (ii) the development of quantitative indicators.

23. **The Report, nonetheless, recognizes a few areas where gaps remain in the implementation of the PRSP, and these should form the agenda for further work.** The staffs recommend that special attention during the next twelve months be given to: (i) the promotion of the private sector, through alleviation of administrative barriers, measures to address other transversal issues such as corruption, and justice, and the finalization of the Accelerated Growth Strategy that should help improve the investment environment and enhance private activities in key export sectors; (ii) the remedial actions to address weaknesses in public financial management and fiscal transparency such as the strengthening of the General Audit Court, the adoption of the new Procurement Code, and stricter enforcement of procurement rules; (iii) the improvement in the efficiency of public investment spending, notably through the preparation of investment budgets and programs using an economic classification of expenditures, better evaluation systems for priority projects (notably in infrastructure), and improved internal and external controls; (iv) the alleviation of rural poverty by consolidating the decentralization of resources to local governments; developing a better articulation of measures aimed at improving the living conditions of vulnerable groups living in rural areas, and implementing the new agricultural strategy aimed at promoting and diversifying new activities in the regions; (v) the finalization and adoption of a new National Social Protection program to help target and coordinate actions aimed at improving the protection of vulnerable groups; and (vi) the identification of factors constraining the absorptive capacity in both public and private sectors, and thereby facilitate the execution of poverty reducing programs.

24. **Recent economic developments have confirmed that the main risks for the successful implementation of the PRSP include both exogenous shocks—such as the locust invasion, the sharp increase in oil prices and the recent flood in the Dakar region—and endogenous difficulties in implementing structural reforms.** The first risk could be mitigated through the authorities' continued efforts to diversify the economy and the financial assistance of donors, if needed. The second risk needs to be tackled through sustained efforts to strengthen public financial management, including in particular fiscal transparency and procurement practices, at the central and local government levels, and complete reforms in the electricity sector as well as the groundnut sector.