Country focus

Cameroon: What next after debt relief?

A year ago, Cameroon received debt relief under two major international initiatives, clearing the way for a write-down of its external debt from about 40 percent of GDP in 2005 to 5 percent of GDP in 2006. Cameroon is now poised to make faster progress toward improving living conditions and reducing poverty. But how is this resource-rich West African country making use of the breathing space created by debt relief, and can it get onto a higher growth trajectory that would edge it closer to achieving the Millennium Development Goals (MDGs)?

Since 1994, Cameroon's economic growth has picked up, although it remains lower than required to make a significant dent in poverty. The devaluation of the CFA franc in 1994 and the accompanying macroeconomic and structural reforms since then contributed to a reversal of Cameroon's declining output. Oil revenues have helped, but the country's crude reserves are dwindling, and economic activity is hampered by weak infrastructure, limited financial intermediation, uneven implementation of structural reforms, and, more generally, an unfavorable business environment. As a result, per capita real GDP has not kept pace with that in comparator countries (see Chart 1), and progress in improving social indicators has been mixed (see Table 1).

Cameroon's debt declined under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI). HIPC debt relief cut Cameroon's debt by about $1.3 billion in net present value terms, reducing future debt service payments by about $4.9 billion. Debt relief under the MDRI amounts to a further $1.1 billion in nominal terms. The IMF provided 100 percent debt cancellation on all debt incurred before January 1, 2005, resulting in the cancellation of $255 million of its claims on Cameroon.

Debt relief has opened up new opportunities. Cameroon is using the freed-up resources to increase priority spending, including on health, education, agriculture, infrastructure

Table 1

Comparative performance

Cameroon, despite its oil and commodity resources, has not kept pace with comparable economies and it lags on social indicators.

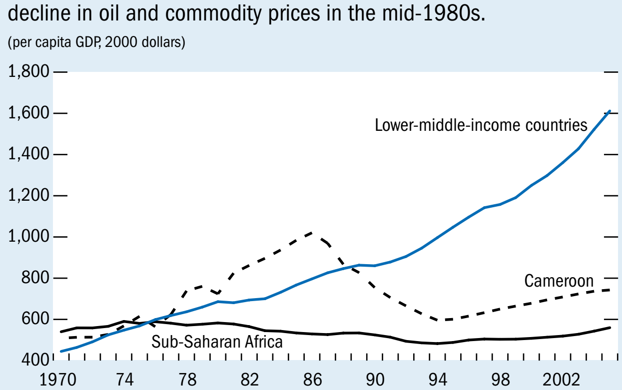
	Cameroon	LMICs[1]
	(1995–2005 average, units indicated)	
Economic indicators		
GDP per capita (constant 2000 dollars)	677.0	1,282.0
GDP per capita growth (annual percent change)	2.0	4.5
Gross domestic investment (percent of GDP)	17.9	26.1
Trade in goods (percent of GDP)	33.6	44.2
Broad money (percent of GDP)	15.2	74.8
Physical infrastructure		
Irrigated land (percent of cropland)	0.4	23.1
Paved roads (percent of total roads)	11.5	51.8
Social indicators		
Adult literacy rate[2]	64	75
Secondary school enrollment ratio[3]	30	70
Life expectancy at birth (years)	47	69

Sources: World Bank, Social Indicators Database; and Cameroonian authorities.
[1]Lower-middle-income countries.
[2]In percent of people ages 15 and above.
[3]In percent of children of secondary school age.

Chart 1

Lagging behind

Although Cameroon's per capita GDP is growing, the country has fallen behind other lower-middle-income countries since suffering a dramatic decline in oil and commodity prices in the mid-1980s.

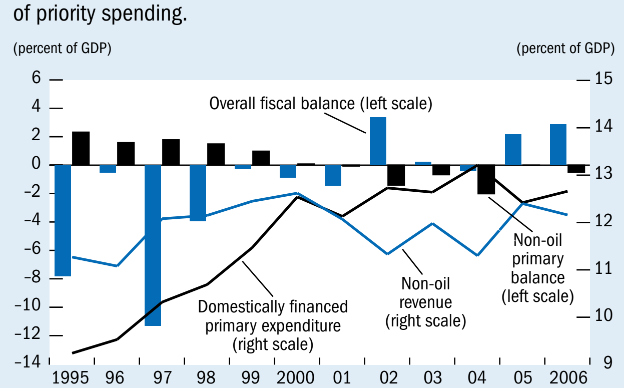


Source: World Bank, World Development Indicators Database, April 2007.

Chart 2

Fiscal challenges

With oil revenues declining over the medium term, key fiscal challenges are mobilizing non-oil revenues and raising the share of priority spending.



Sources: Cameroonian authorities; and IMF staff estimates.

development, and institution building. But expectations for a debt relief "dividend" in the form of higher current spending could undermine fiscal sustainability if not managed prudently. To build on the opportunities presented by debt relief, Cameroon will need to achieve progress in

- preserving long-term fiscal sustainability while expanding priority spending,
- broadening and deepening the financial sector,
- liberalizing trade, and
- improving the business environment by stepping up structural reforms.

Managing the "fiscal space." Although Cameroon's overall budgetary position has strengthened over the past two years, the underlying fiscal situation is less favorable. Aided by large oil revenue inflows and improved budget management, the overall fiscal balance has been in surplus. But the non-oil primary balance has deteriorated over the past decade because domestically financed primary spending has expanded faster than non-oil revenues, partly reflecting an increase in debt relief–financed priority outlays (see Chart 2). The fiscal space provided through debt relief should therefore be used prudently. How can Cameroon achieve that?

First, it needs to mobilize additional non-oil revenues over the medium term, which will be critical for preserving fiscal sustainability, given the expected decline in oil reserves and prospects for trade liberalization. But, with tax rates already high, additional revenues would need to come from a broadening of the tax base through policy and administrative measures.

Second, Cameroon should devote a larger part of public expenditures to priority outlays, taking into account its absorptive capacity. Its efforts would need to be accompanied by reforms in public expenditure management to ensure that the resources are used effectively. Measures that reduce subsidies to public enterprises—a heavy burden on the budget—and redirect those resources toward education, health, and infrastructure would also help boost the quality of spending.

Finally, to preserve its hard-won debt reduction, Cameroon needs to strengthen debt management. It should rely primarily on grants and concessional loans for the next few years to cover its financing requirements and avoid a rapid accumulation of new debt. It will need to monitor debt sustainability indicators closely to avoid a recurrence of past debt problems.

Developing the financial sector. Improved access to finance would help Cameroon diversify its economic base and achieve the more rapid sustainable growth it needs to reduce poverty. However, the country's financial system is dominated by banks that appear vulnerable to credit and interest rate shocks. Its weak judicial system, lack of adequate land and collateral registries, interest rate ceilings, and limited availability of financial and credit information further hamper bank credit. Contractual savings and capital markets are poorly developed, contributing to the scarcity of longer-term resources to finance the economy. Progress in all these areas will be needed.

Liberalizing trade. Cameroon's import tariffs are among the highest in sub-Saharan Africa, and its complex customs procedures limit trade and factor mobility. It's true that a country that reduces such trade barriers can better allocate its resources and accelerate growth. But concerns about possible revenue losses are real, especially in Cameroon, where taxes on international trade exceed 2 percent of GDP. This fiscal reliance largely explains why trade liberalization, including efforts to reduce tariff rates and harmonize regional trade rules, has not advanced very far. The best course of action would be to gradually reduce the maximum common external tariff rates applied by the CEMAC (the monetary union to which Cameroon belongs) and slowly remove obstacles to intraregional trade.

Improving the business environment. Accelerating growth would also require considerable improvement in the business environment. Available indicators of the investment climate show that Cameroon does not do well in contract enforcement, timely issuance of licenses, and cost of registering property (see Table 2). Furthermore, governance is weak and corruption perceptions are widespread. Achieving considerable improvements in all these areas will be critical if greater private investment is to be fostered. In addition, completing public enterprise reform in air transport, telecommunications, and water distribution would reduce the burden on public finances, enhance economic efficiency, and send positive signals to private investors. ■

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Table 2

Down the list

Cameroon does not rank well in the World Bank's 2006 *Doing Business* indicators. Improving the business environment is key to accelerating growth.

	Doing business (overall rank)[1]	Days to acquire licenses	Cost of registering property[2]	Days to enforce contracts
Cameroon	152	444	19	800
Indonesia	135	224	11	570
Philippines	126	197	6	600
Botswana	48	169	5	501
Mauritius	32	145	16	630
CEMAC	157	248	16	699
Sub-Saharan Africa	131	230	12	581
LMIC[3]	98	214	6	576

Source: World Bank, Doing Business Database (2006).
[1]Indicates ranking out of 175 countries (lower number = higher ranking).
[2]Percent of value.
[3]Lower-middle-income countries.