An Emerging Senegal: Safeguards for Promoting Investment in African Sovereign Debt

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A traditionally stable economic and political environment, together with favorable regimes for business and transport activities, make Senegal one of Africa's exemplary democracies and one of the African countries which most strongly promotes foreign investment, thereby attracting more and more global investors.

On June 24, 2015, the Senegalese government approved the "*Plan Sénégal Émergent*" (ESP), which includes a series of economic amendments and structural reforms designed to attract foreign investment and increase private investment. In particular, the ESP contains amendments aimed at fostering growth in the energy, education, agriculture and transportation sectors.

All told, the ESP includes 27 priority projects and 17 economic reforms intended to reinforce the enabling environment for private sector investment. Among these various reforms, the authors highlight here the one contained in Senegal's Investment Code, which apply to investments over XOF 100 million (mainly production, processing, industrial, tourism, agricultural and complex trade civil code) and provide basic guarantees for equal treatment of foreign investors and repatriation of profit and capital as follows:

1. Tax incentives include a three-year exemption on customs duties for capital goods imports and VAT exemption on production and purchase of local products and services.
2. Exemption from the Minimum Personal Income Tax and from the Business License Tax is granted to investors that use local resources for at least 65 per cent of their total inputs within a fiscal year.
3. Companies located in less industrialized areas of Senegal benefit from exemption of the lump-sum payroll tax of three per cent, with the exemption running from five to 12 years, depending on the location of the investment.
4. Several reforms to make it easier for investors to acquire and register property, maximizing procedures and reducing associated costs for property registration, were carried out. As stated previously, Senegal's Investment Code includes guarantees for equal treatment of foreign investors, including the right to acquire and dispose of property.

Relatedly, the authors have observed an increasing interest in Senegal from Spanish investors, especially from those that have been granted export credit in connection with exports to Senegal in project finance transactions, as well as those that have directly financed the Senegalese government (0.10% of Spanish exports are destined for Senegal, and Spain is the top importer of Senegalese exports in the EU). In addition, one of the major reasons for growing Spanish investment in Senegal is the country's favorable geographic position, given Senegal's proximity to continental Spain and the Canary Islands.

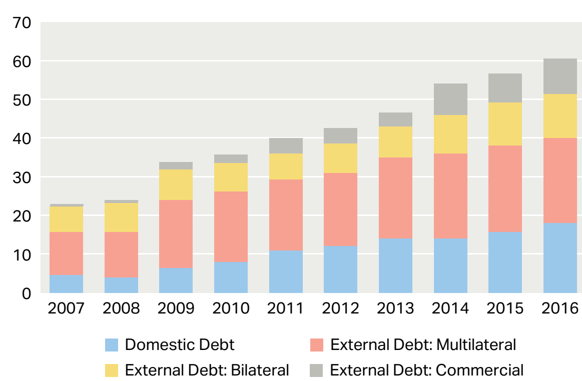
The Senegalese government's measures aimed at attracting foreign investment and the subsequent increase in Senegal's public debt levels raise important questions as to whether and how the country's debt may be restructured in the future. Upon examination of the changing makeup of Senegal's creditor constituencies and the debt restructuring mechanisms used in the past, the authors believe that Senegal may need to find new and different avenues for debt relief in the coming years.

Senegal's Creditors

Historically, African countries, and Senegal in particular, have mostly borrowed from multilateral institutions—primarily the World Bank, the African Development Bank (AFDB) and the International Monetary Fund (IMF)—and, to a lesser extent, from bilateral lenders belonging to the Paris Club. The Paris Club, formed in 1956, is an informal group of creditor governments from major industrialized countries that meets with debtor countries in Paris on a monthly basis in order to agree to the terms and conditions of the potential restructuring of their debts.

As reflected in the table below, even though the majority of Senegal's external debt is still owed to multilateral institutions, the percentage of multilateral debt relative to other types has decreased over the last decade, while bilateral debt levels have largely remained stable. The reason for this is that recently, loans extended by the World Bank, the AFDB and the IMF have been too small or restrictive in comparison with the country's demand (i.e., either not sufficient to fund many of the big infrastructure projects or subject to strict borrowing limits), which has resulted in the World Bank, the AFDB and the IMF being unable to provide the volume (or kind) of financing that Senegal needs. Additionally, indebtedness owed by Senegal to certain non-Paris Club creditors is increasing. The rise in these new debts, owed to individual creditors who are not included in the Paris Club, has reduced the importance of the Paris Club creditors.

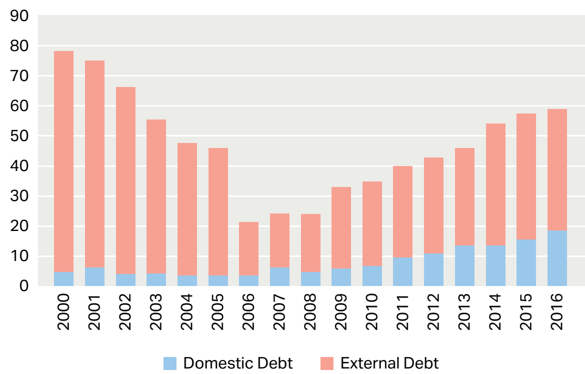
Figure 1: Senegal: Public Debt, 2007–16
(Per cent of GDP)



Source: Table published by IMF in 2017

Over roughly the same period during which Senegal has become less reliant on multilateral institutions and Paris Club members, public debt levels and borrowing costs in Senegal have been increasing. Senegal's ratio of public debt over GDP increased from 20.9% in 2006 to 59.3% in 2016.

Senegal: Public Debt as share of GDP



Source: Table published by IMF in 2017

Debt Restructuring

As discussed above, although Senegal has historically borrowed heavily from multilateral institutions and, to a lesser extent, from bilateral lenders belonging to the Paris Club, due to Senegal's new and evolving financing needs, debts owed to non-Paris Club individual creditors have been increasing.

Senegal's wide variety of creditors in recent years and its external debt burden has meant that investors' attention has been drawn to the way in which Senegal's debt has been restructured on several occasions in the past so as to evaluate potential future restructuring alternatives.

First, in 1996, the IMF and the World Bank, as the largest creditors of most countries, introduced the HIPC Initiative (Heavily Indebted Poor Countries) "*with the aim of ensuring that no poor country faces a debt burden it cannot manage*".[1]

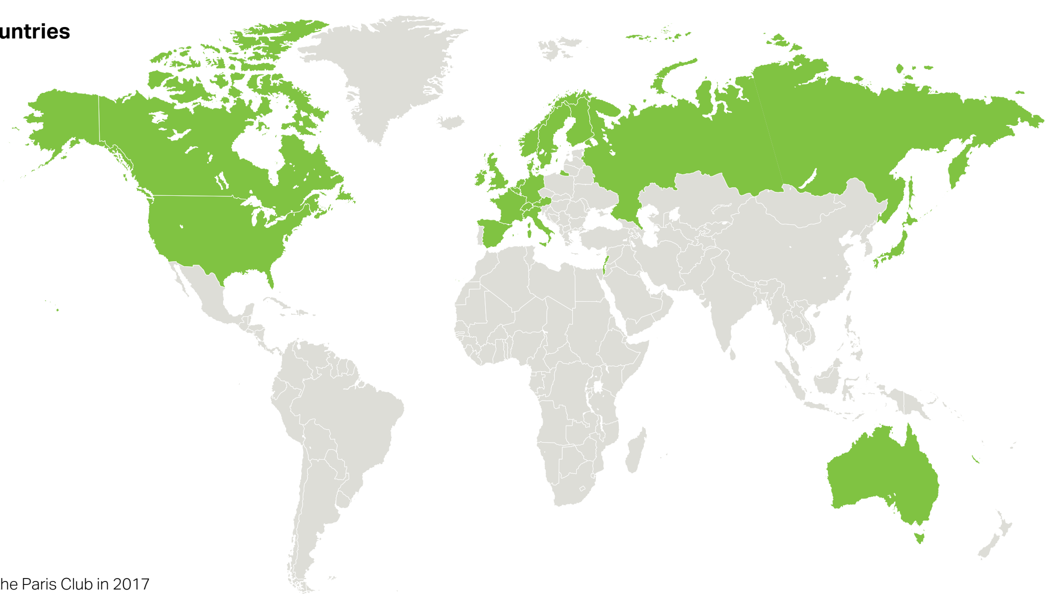
Under the HIPC Initiative, if a country wished to qualify for debt relief, it had to comply with certain economic and structural reform programs and poverty reduction strategies. Initially, debt relief was conditional on countries opening up their economies and reducing the state's role in the economy (e.g., dismantling of government-owned monopolies).

As low-income countries required greater levels of debt relief, in late 2005, a new programme, the Multilateral Debt Relief Initiative (MDRI) (which provided full debt relief to countries that successfully complied with the HIPC Initiative requirements) was approved. Against this backdrop, in June 2005, the IMF, the International Development Association of the World Bank and the African Development Fund agreed to write off 100% of their debt claims on all countries that had reached, or will eventually reach, the completion point under the enhanced HIPC Initiative. Consequently, as of January 2006, twenty countries, including Senegal, were eligible for immediate MDRI relief.

Second, in addition to the HIPC Initiative and the MDRI, the Paris Club also worked closely with the IMF and the World Bank regarding debt relief. For many years, the Paris Club has been an important place for Senegal in terms of restructuring sovereign debt owed to bilateral creditors. It was the top forum for Senegal to restructure its sovereign debt, which it did on several occasions (in 1981, 1982, 1983, 1985, 1986, 1987, 1989, 1990, 1991, 1994, 1995, 1998, 2000 and 2004).

Senegal's last debt restructuring with the Paris Club took place on 9 June 2004. By the end of 2002, Senegal's total public debt amounted to approximately USD2,538 million in net present value, while the debt owed to Paris Club creditors amounted to approximately USD586 million in net present value. In

The 20 Paris Club Countries



Source: Graphic published by the Paris Club in 2017 the 2004 restructuring, and given Senegal's commitment to carrying out the economic and structural reforms previously proposed by the HIPC Initiative, the Paris Club members agreed to write off USD94 million in net present value terms, relying on Senegal's commitment to continue modernizing its economy in a manner consistent with the HIPC Initiative. Additionally, most creditors belonging to the Paris Club also committed to granting additional debt relief to Senegal on a bilateral basis.

The HIPC Initiative and MDRI are nearly complete, with 36 countries (including Senegal, as noted above) having reached the completion point under the HIPC Initiative. However, since Senegal's last debt restructuring, the composition of its creditors has changed. As a result of the rise in bilateral lending by entities other than multilateral institutions and Paris Club members (most significantly China, Kuwait, Brazil, Russia, India and South Africa), the importance of the Paris Club as it exists today as the chosen forum for Senegal's debt restructuring has been significantly reduced.

The emergence of these new bilateral lenders in Senegal's borrowing arrangements raises some doubts regarding the mechanisms which will be used in the future by these non-Paris Club countries when facing future defaults in view of the need to restructure Senegal's debt. Perhaps these new bilateral creditors will join the Paris Club, widening the club's membership, or they could build a separate international club governed by their own rules.

CIGI papers from 2014 regarding African perspectives on sovereign debt restructuring expressed concern about the *"uncoordinated, protracted and ultimately costly sovereign debt restructurings on the African continent. The lack of contemporary framework for restructuring debt owed to the multilaterals is one worry; another is the absence of adequate rules and procedures for restructuring private held sovereign bonds"*.

In view of the foregoing, it seems clear to the authors that (i) the debts written off under the HIPC Initiative and MDRI were one-off, which means that these lenders are unlikely to settle future sovereign debt crises in the same manner, and (ii) the new composition of Senegal's creditors implies that the importance of the Paris Club will be reduced and that a new mechanism for debt restructuring in Senegal will emerge.

Overview: Senegal Debt Relief Committed and Delivered by Paris Club Official Bilateral Creditors
(USD (millions), in year-end 2015 present value terms)

HIPC Initiative Assistance Committed	HIPC Initiative Assistance Provided	Debt Relief Beyond HIPC Initiative Provided	Total Debt Relief Provided	Deb Relief Provided to Debt Relief Committed (%)
179.8	179.8	442.7	622.5	346.2

Based on table published by IMF in 2017

Emerging Senegal Plan

In light of the above, and given Senegal's economic growth during the past years, Senegal's government approved the ESP in 2015. The ESP, a strategic plan designed by Senegal's government in cooperation with the World Bank, establishes the framework for Senegal's mid- and long-term economic and social policy, which can be summarized in one phrase: "*An emerging Senegal in 2035, providing a cohesive society under the rule of law*".[2]

Strategic Goals of the Emerging Senegal Plan

The strategic goals of the Emerging Senegal Plan, which is being carried out through private investment, are based on three pillars:

1. Prompting a structural transformation of Senegal's economy (i.e., the automation of administrative procedures, setting up of incentives and simplified tax and legal devices, and promoting high impact investments, among other initiatives);
2. Improvement to the well-being of the population; and
3. Promoting good governance practices by reinforcing security, stability, governance, protection of rights and liberties and the consolidation of the rule of law.

The aim of Senegal's government is for Senegal to improve its ranking (147th out of 190 countries) in the 2017 Doing Business report issued by the World Bank, which will significantly increase Senegal's attractiveness in the eyes of investors.

In December 2017, the Executive Board of the IMF completed the fifth review of Senegal's economic performance and highlighted that "*Senegal's macroeconomic situation is stable. [...] the outlook for the Senegalese economy remains on the whole positive [...].*"[3] Additionally, several measures contemplated by the ESP have improved and will continue to improve the well-being of Senegal's population. Such measures include:

Key measures implemented (or to be implemented) by the ESP aimed at improving the well-being of Senegal's population

— Public infrastructure projects have made Senegal´s rural regions, where more than 70 per cent of Senegal's population lives, more connected both digitally and physically.

— Dakar's citizens no longer experience the water and power cuts that threaten many cities in West Africa.

— Development of the agricultural sector has included important measures to promote better utilization of water (more land is being irrigated allowing the planting of basic food such as rice) and improved seed quality.

— Senegal is building a new city near the airport called "Diamniadio", with special economic zones, a free-trade area, a tech city, research centres and a medical campus.

— Adoption of a regulation prior to the IMF's Executive Board's sixth review, making it possible for medium-sized enterprises to file and pay taxes online in 2018.

In light of these statements, it would be easy to conclude that performance under the ESP has been broadly positive. Yet Senegal still faces great problems as it seeks to improve the living standard of the nearly half of its population who live below the poverty line, which means that further efforts under the ESP are needed.

Conclusion

Senegal's strategic geographical position, its steady and increasingly competitive economic and political environment, along with its latest taxation amendments to promote business and transport activities, make Senegal an attractive opportunity for foreign investors looking for new countries in which to maximize their investments. However, Senegal's variety of lenders and increasing reliance on bilateral financing outside of historically familiar frameworks raise the question of how its sovereign debt may be restructured going forward.

Traditionally, there have always been suitable mechanisms for dealing with defaults and restructuring in an orderly, timely and fair manner (such as the HIPC Initiative, the MDRI and the Paris Club). Up to now, Senegal has mostly borrowed from multilateral creditors and, to a lesser extent, from bilateral creditors belonging to the Paris Club. However, even though multilateral lenders are still Senegal's largest creditors, due to the country's vastly growing and evolving developmental needs, multilateral lenders are losing significance. The proportion of bilateral lenders is increasing as compared to multilateral lenders, which translates to a growing increase in non-Paris Club member lenders.

Finally, the Senegalese government's clear and firm commitment to break with the past and drive Senegal towards a new developmental trajectory and the modernization of its economy through the execution of the ESP is evidence of the commitment to turn Senegal into an emerging country by 2035. Only time will tell, but it would not be surprising for Senegal to start coming under international investors' spotlight, particularly because of its opportunities in the context of the privatization of public companies, new infrastructure, the agricultural sector and investment in technology. ■

1. IMF: *"Debt Relief Under the Heavily Indebted Poor Countries (HIPE) Initiative"*. IMF Factsheet. March 8, 2018.
2. African Development Fund: "*Senegal Local Development Reform Support Programme - Phase I*". OSGE Department. August 2016.
3. Anecdotally, Senegal's recent issuance of Eurobonds in the amount of USD1,100 million with a reasonable interest rate of 6.5%, suggests increasing confidence of global markets in the Senegalese economy.

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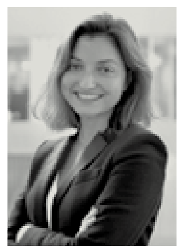

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