Development Cooperation addresses the Impact of the Financial and Economic Crisis in Low-Income African Countries

CASE STUDY DEMOCRATIC REPUBLIC OF THE CONGO

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**INTRODUCTION**

This report is one of three case studies developed at the request of the Belgian Directorate General for Development Cooperation in preparation of the ‘Development Cooperation Assises’, a forum of Belgian Development Cooperation policy makers and development actors, civil society/NGOs, parliamentarians and academics, that takes place in Brussels on May 5, 2009. The main theme of the Assises is: “Development Cooperation addresses the Impact of the Financial and Economic Crisis on Low-Income African Countries”. After first striking the advanced and then the emerging economies, it is increasingly being recognised that developing countries are, mainly indirectly but therefore not to a lesser extent, being hit by the worldwide crisis. The objective of this year’s Assises is therefore to explore the expected impacts in Africa’s low income countries, the population groups going to be most affected and the main channels or mechanisms through which this is going to happen. The case studies will analyse the impact of the crisis in the three Belgian partner countries and the policy responses of the government and donors in order to identify adapted policy response and priority measures.

The Democratic Republic of the Congo is situated in the centre of the African continent but is economically and regionally affiliated with Southern Africa as a member of the Southern African Development Community (SADC). Its large reserves of mineral resources notwithstanding, the vast majority of the 62 million Congolese live in extreme poverty. In 2008 it ranked 177th on the UNDP Human Development Index, in a ranking of 179 countries.

The team chosen to make this case study consists of 4 researchers from the Institute of Development Policy and Management. Danny Cassimon and Karel Verbeke bore the prime responsibility for the work; Stefaan Marysse and Robrecht Renard have provided them with complementary inputs. A review of the most relevant literature was done first, complemented with a field mission to Kinshasa, executed by Danny Cassimon and Karel Verbeke, from April 5 to April 12.

The structure of this report follows the terms of reference (TOR), added as annex 3 in the report. Section 2 provides the specific conceptual framework used for the study. It focuses not only of the different transmission mechanisms through which the current international financial and economic crisis may impact growth and poverty reduction, but also presents a framework to define and deal with crisis vulnerability. The three following sections deal with the main questions raised in the TOR for the case of DRC: section three analyses the impact of the crisis on DRC and its main transmission channels; section four deals with the reaction of the government in coping with the crisis, while section five discusses current and prospective donor reactions to help the country cope with the crisis. Section six offers some preliminary conclusions.

The opinions expressed in this report are those of the authors and do not necessarily reflect the policies or views of the DGDC. The team wishes to thank all the interviewees for their time and specifically Mr. Paul Cartier and Mr. Daniel Mukoko Samba for their assistance in the organisation of the meetings.
1. Framing the issues

1.1. How does the crisis impact poor countries and people: a conceptual framework

Figure 1 provides a possible conceptual framework that provides an overview of the different transmission channels, through which the current international financial and economic crisis could impact not only economic growth, but also poverty, well being and social exclusion in low-income countries such as DRC. The framework focuses on two layers of transmission mechanisms. The first layer depicts the different possible transmission channels through which the international shock enters the country; as such, it is linked to the performance of key items represented in the balance of payments of a country. The second layer describes the different channels through which each of these can influence income growth, and poverty.

In describing the first layer, it is useful to distinguish between four main channels. The first channel is the international trade channel, describing the (net) influence of the shock on the volume and price of both exports and imports of goods and services. The second one refers to private transfer payments, mainly that of remittances. The third one refers to international aid, in the form of grants (‘public transfers’) or concessional loans. These first three channels refer almost exclusively to the current account of the balance of payments. The fourth channel refers to the impact of the crisis on international capital flows, of both short-term and long-term flows, and be it of a debt nature (loans) or equity nature (FDI and portfolio investments). This fourth channel refers to the capital or financial account part of the balance of payments. A specific sub-channel that links both the trade and capital components refers to trade credits. As it is potentially an important subchannel in this crisis, we mention it separately.

These channels will impact the country’s economy, influencing production, consumption, and investment decisions by different actors; for this study, it is useful to decompose the economy into three main segments, being the private real sector, the public sector (including the central bank), and the private financial sector.

The second layer determines the impact of the international shocks on poverty. It describes the different transmission mechanisms through which the impact on the first layer (trade flows, aid, capital and remittances), and the reaction of different subsector actors, influences real disposable income, wealth, poverty and social exclusion. Here, we distinguish between five different channels, and their interlinkages. The first is through its effect on taxes and direct public transfers and subsidies. The second is through price changes. Here, we distinguish further between different key price variables such as interest rates, prices of goods and services (inflation), exchange rates, and wages. The third channels looks at assets. The fourth one is focusing on employment and the fifth channel deals with direct access to goods and (public) services.

In the following section, we will briefly analyse the likely relative importance of each of these transmission channels for the case of the DRC. Before we do this, it is important to make two additional remarks.

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1 Except for concessional loans.
The first one is that the direction of the impact of the international shock on the first layer of transmission mechanisms (trade, aid, capital and remittances) is not ex-ante known or negative: for most of these channels, in principle phenomena working in both directions could be at play, making the net ultimate effect uncertain both in sign and magnitude. Take the international trade channel, where the net impact largely depends on whether the country is an (net) exporter or importer of the specific goods (or services) touched by the crisis; as such, at least the net terms of trade effect is unknown ex-ante.

But this goes also for most of the other channels. Remittances might be subject to two reactions that work in opposite directions: as a result of the negative shock, senders of remittances might be negatively affected themselves and less capable of sending remittances, but on the other hand, referring to the largely countercyclical nature of remittances, remittances might increase as a reaction of the senders to the worsened situation of relatives in the recipient country. A similar dual reasoning applies to aid flows: as donor countries are confronted with a crisis in their own country, they might be tempted to reduce their aid effort, and as such, aid disbursements might be negatively affected. But on the other hand, aid ideally acts as a countercyclical financing mechanism, leading to higher flows in times of (recipient country) crisis. Although it is now known that aid, especially types of programme aid, is often pro-cyclical, countercyclical aid flows can emerge especially with respect to all kinds of ‘emergency’ aid, i.e. exceptional finance, mainly of interventions by the international financial institutions such as the IMF, the WB, and regional development banks, but also forms of exceptional, emergency crisis aid responses by bilaterals, linked to the balance of payments (BOP) support and/or types of ‘budget support’. And, finally, although private capital flows of all sorts are generally described as being highly procyclical, hinting at a decrease of these flows in times of crisis, the literature, drawing on country experiences of earlier international (financial) crises, such as the East-Asian one, documents the possibility of increased inflows during a crisis, in which foreign investors exploit the opportunity
presented by the crisis of investing in the country at bargain prices (e.g. ‘fire sale FDI, Krugman, 1998).

The second observation is that the magnitude of the impact of a shock on both layers of transmission mechanisms depends on the degree of crisis vulnerability of the country. As such, it is useful to define this crisis vulnerability in a more conceptual way, incorporating different dimensions of vulnerability, as well as providing a framework to deal with them, as in the next subsection.

1.2. Defining and dealing with crisis vulnerability

The conventional way of defining vulnerability refers to external vulnerability, as linked to the degree to which the country is integrated in the global economy (in terms of production, trade or finance). It is proxied by the vulnerability of the country to external (exogenous) shocks, linked to a trade, or external finance (aid) event, and as such largely refers to the first layer of the transmission mechanism framework of figure 1. Table 1 provides an overview of a conceptual framework to deal with external vulnerability, for different types of exogenous external shocks. The table highlights the existence of three possible ways of dealing with an external shock, i.e. prevention, insurance, and coping (see e.g. Lee et al, 2008).

<table>
<thead>
<tr>
<th>External shock</th>
<th>Prevention mechanisms</th>
<th>Insurance</th>
<th>Coping mechanisms</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Terms of) Trade</td>
<td>Diversification; countercyclical aid (and remittances)</td>
<td>Reserves hoarding; stabilization funds, SWF</td>
<td>Current account and fiscal adjustment with adjustment loans and other exceptional aid</td>
</tr>
<tr>
<td>Private Capital Flows</td>
<td>Composition of flows, DSA, capital market development, dedollarization of flows, countercyclical aid (and remittances)</td>
<td>Reserves hoarding</td>
<td>Currency and interest rate derivatives, indexed debt, external debt in local currency</td>
</tr>
<tr>
<td>Remittances</td>
<td>Migration (return) policy; diversification of household income</td>
<td>Reserves hoarding</td>
<td>Current account (macro) and household level adjustment with adjustment loans and microfinance</td>
</tr>
<tr>
<td>Aid</td>
<td>Counter-cyclical provisions in aid; multi-year donor commitments; aid contract sensitive to effects of external shocks on performance standards</td>
<td>Reserves hoarding</td>
<td>Emergency type of aid instruments</td>
</tr>
</tbody>
</table>

Source: authors’ interpretation of Lee, Perry & Birdsall (2008: table 1).

Prevention refers to ex-ante mitigation of the (BOP-)effect of a shock by diversification of exports and production (e.g. for trade shocks) or sources of external finance, or by countercyclical forms of external finance such as aid or remittances. Alternatively, also financial insurance can be used to deal with exposure to external shocks. Insuring can take the form of self-insurance, mainly through the increase of the level of international reserves or
through other mechanisms of temporarily storing windfall earnings in the good years, to use them in the bad years (as in stabilization funds, or sovereign wealth funds (SWF)); it can also be realized through market-based insurance mechanisms such as hedging (use of derivatives, indexed debt)\(^2\).

In the case of lack of prevention or insurance, the only remaining solution to deal with the shock is coping. Coping refers to country bearing the brunt of the negative shock, by adjusting to the crisis, in a BOP sense (reducing net imports, drawing down international reserves), and/or in a fiscal sense (increasing revenues, reducing expenditure), normally also resulting in a drop of country income and wealth, and an impact on poverty. Typically, in coping, the country is assisted in this adjustment process by the international community, mainly through the IFIs, through adjustment loans and other exceptional financing. These loans enable the country to reduce the current burden of the shock for the country, reducing the current negative effect on income and wealth, and as such, realize burden sharing between the country and the international community. The crucial issue here is always determining the exact burden sharing between the two parties involved, in other words: *who pays the ferryman?* Determining the exact burden sharing between the country and the international community for this crisis will be one of the elements explicitly dealt with in the DRC case study.

The previous reasoning applies for all kinds of external shocks. The main distinguishing feature of this crisis is that it is a combination of several shocks; in terms of table 1, all four potential shocks described happen simultaneously. More importantly, also sources of external finance that normally have a countercyclical potential, such as aid flows and remittances, are now also likely to be negatively affected, because donor countries themselves are affected.

In order to measure the impact on the second layer of transmission mechanisms, it is useful to go beyond the notion of ‘external’ vulnerability, highlighting aspects of vulnerability that deal more with the likely impact on household income and poverty. The framework for dealing with external vulnerability, as developed in table 1, can be extended to this level, as highlighted in table 2.

**Table 2: A framework for dealing with household level vulnerability**

<table>
<thead>
<tr>
<th>Prevention mechanisms</th>
<th>Insurance</th>
<th>Coping mechanisms</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Self-insurance</td>
<td>Market insurance</td>
</tr>
<tr>
<td>Crisis effect</td>
<td>Formal employment; diversification of household income, in informal sector; countercyclical transfers and remittances, income in dollars</td>
<td>Assets hoarding (financial and real, e.g. land, cattle)</td>
</tr>
</tbody>
</table>

Source: authors' interpretation of table 1 for household level reactions.

\(^2\) Poor developing countries would likely benefit most of market insurance instruments, as their external vulnerability is relatively high. However, they are in general not able to exploit this potential, because of the lack of development of or lack of accessibility to derivative financial instruments, or the lack of market development of appropriate financing instruments such as debt, indexed to say GDP, or the terms of trade evolution. Here lies a potential task for multilateral donors in (helping to) establish these markets (Lee et al, 2008 :4).
At the household level, again we distinguish between the same three possible ways of dealing with vulnerability, and the effects of a (negative) shock, i.e. prevention, insurance, and coping. The table provides examples of these different strategies. The same basic conclusion as for external vulnerability applies here: lacking prevention and insurance mechanisms, the basic household level reaction to a negative shock will be coping by adjusting the consumption level, or selling assets, possible smoothed by interventions by the government or donors, in the form of emergency interventions such as food-for-work programs, or individual emergency lending mechanisms, such as microfinance, if available.

In further conceptualising vulnerability, we extend our framework by drawing upon the conceptual framework designed by the World Bank (2009d) to assess and classify countries according to their relative vulnerability vis-à-vis the current international financial and economic crisis. In its framework, the World Bank looks at additional elements. The first two determine the level of poverty vulnerability, looking at the extent of decline of the growth rate, combined with the level of initial poverty of the country. If both are very high, than this points at a high level of poverty vulnerability to the crisis.

Furthermore, two additional dimensions are added in the World Bank (2009d) vulnerability framework, both linked to the capacity of governments to cope with the impact of the crisis: vulnerability is heightened when the government is limited in its capacity to cope with the crisis due to limited institutional capacity, and/or limited fiscal resources (‘fiscal space’).

For the purpose of this study, we add an additional dimension to the vulnerability framework, focusing on the relation between the donor community and the recipient government. To the extent that the donor community has realized a low level of harmonization (among donors) and alignment (with country government systems and priorities), the ability of the donor community to effectively assist the government in coping with the current crisis is also reduced, and as such this heightens vulnerability.

In dealing with the DRC case, we will deal with all six elements of this enhanced vulnerability framework.

2. The Impact of the Crisis on the DRC

In this section we apply our framework of figure 1 to the current global financial and economic crisis in DRC. First we describe the main channels through which the crisis enters the country (first layer of figure 1), followed by a description of the effects on economic sectors. Next we describe the main transmission channels through which this shock might affect growth and poverty reduction (second layer of figure 1).

Before starting the analysis, it is useful to try to relate this shock to other recent shocks that have struck the country. In fact, DRC has been hit recently by four shocks, three of them of an exogenous international nature, and one internal one. The three well-known international shocks are now commonly described as the three Fs (food, fuel and finance); the fourth, internal one re-emerged in 2008 more or less jointly with the international financial crisis with a new eruption of the conflict in the East of DRC. Where possible, the analysis will try to distinguish between the effects of the financial crisis and of these other ones.
2.1 **Main transmission channels of the global financial and economic crisis**

DRC has a very open economy, both at the current account as well as the capital account level. The level of trade openness of the economy (as measured e.g. by the sum of exports and imports over GDP) has risen steadily over recent years, and has reached 142% at the end of 2008, indicating a very high degree of openness (Ltaifa, 2009). Furthermore, the country’s exports are not diversified, being heavily concentrated on mineral exports (mainly copper, cobalt, gold and diamond, as well as crude oil), that account for about 82% of total exports in 2008. Imports are much more diversified, including also refined oil products. As such, the country’s exports depend heavily on the evolution of international commodity prices and global demand, and the country can be classified as extremely vulnerable to (terms of) trade shocks.

The country also has an open capital account regime, with no major capital account restrictions (i.e. a high *de jure* openness). However, this open capital account regime has not led to a high degree of formal *de facto* financial integration in the global financial system: formal cross-border banking links as well as private capital market transactions are limited, and the inflows of FDI are still relatively limited, despite an increase in recent years mainly linked to the development of the mineral sectors.

As a consequence, direct transmission of the global financial crisis to the DRC was very limited (see also 3.2.), but the main impact was indirect, mainly through the international trade channel. Indeed, at the outset of the recent world crisis, the DRC had been enjoying several years of substantial growth of its (mineral) exports, fuelled by growing world demand for its products and increased world prices. As highlighted in table 3, this process intensified in the first half of 2008, where prices for its mineral products, and also for some other traditional commodity export products (such as coffee, palm oil and wood) peaked, leading to a record export performance.

| Table 3: Recent evolution of DRC key export commodity prices |
|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Mineral exports | Dec ‘07 | Jul ‘08 | Nov 08 | Dec ‘08 | Jan ‘09 | Feb ‘09 | Peak |
| Crude oil ($) | 95,0 | 147,0 | 50,6 | 38,9 | 41,6 | 44,1 | 147,0 | 04/07/08 |
| Copper ($) | 5346,5 | 5477,4 | 3580,0 | 2811 | 1076,5 | 3385,0 | 8700,0 | 16/04/08 |
| Cobalt ($) | 29,4 | 38,1 | 17,0 | 16,5 | 17 | 15,0 | 47,0 | 07/03/08 |
| Gold (once) | 693,6 | 940,0 | 815,7 | 869,7 | 928,7 | 939,8 | 940,0 | 17/03/08 |
| Diamond (carat) | 22,6 | 32,1 | 16,2 | 16,2 | (8/12) | 32,1 | July 08 |

* Riggints, local currency of Kuala Lumpur: 5 riggints=1 euro
** Bdft (Board foot): 1 Bdft=2,3597 liters
Source: BCC, 2008a and 2009b

At the same time, also imports increased in recent years, fuelled by high refined oil prices, and the price increase of some imported food products such as rice. But overall, the country’s terms of trade improved continuously in recent years before the current financial shock, as highlighted in table 3.
Table 4: Terms of trade evolution of DRC (2001-2008, percentage change over previous year)

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009p</th>
</tr>
</thead>
<tbody>
<tr>
<td>Terms of trade</td>
<td>4.32</td>
<td>10.84</td>
<td>15.74</td>
<td>7.44</td>
<td>15.44</td>
<td>8.52</td>
<td>13.4</td>
<td>-2.11</td>
<td>-23.11</td>
</tr>
</tbody>
</table>


When the international financial and economic crisis struck, from September 2009 on, the effects on the prices of key DRC mineral exports were already observed rather early into the crisis, but as the crisis emerged into a truly global economic crisis, prices fell considerably, reaching their lowest value in December 2008 or January 2009, with a minor recovery for some of them (copper, crude oil) since then, as again witnessed in table 2. On the import side, the effect was mainly felt by decreased world prices of refined oil. As highlighted in table 4, this will also result in a worsening of the terms of trade, around 2% for 2008, and projected around 23% for 2009.

The impact of the crisis on DRC international trade flows, and the BOP of the country more general, is highlighted in table 5. Table 5 not only provides data on the main BOP categories, and thus main transmission channels, for 2007, 2008 and the most recent estimates for 2009, but also includes some intermediary BOP projections from the IMF, notably one before the major commodity price boom (2007), and one from September 2008, just before the international financial crisis erupted. As such, comparing these projections can provide some estimate of the impact of the boom of 2008, but, more importantly, by comparing the September 2008 estimates with the most recent data, give some idea of the magnitude of the total negative external shock due to the international financial and economic crisis.

Table 5: Balance of Payments (2007-2009), in million US$

<table>
<thead>
<tr>
<th></th>
<th>2007 (Dec 08 est. (a))</th>
<th>2007 Sept 07 proj. (b)</th>
<th>2007 Dec 08 ? proj. (c)</th>
<th>2007 Most recent est. (d)</th>
<th>2009 Sept 08 mission (e)</th>
<th>2009 Most recent proj. (f)</th>
<th>2008 effect crisis (d)-(c)</th>
<th>2009 effect crisis (f)-(e)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Account</td>
<td>-188</td>
<td>-1.168</td>
<td>-569</td>
<td>-1.783</td>
<td>-2.399</td>
<td>-2.927</td>
<td>-1.214</td>
<td>-528</td>
</tr>
<tr>
<td>Merchandise trade</td>
<td>886</td>
<td>-484</td>
<td>861</td>
<td>-125</td>
<td>-753</td>
<td>-2.073</td>
<td>-986</td>
<td>-1.320</td>
</tr>
<tr>
<td>o/w mining products</td>
<td>5.108</td>
<td>2.280</td>
<td>5.643</td>
<td>5.422</td>
<td>5.410</td>
<td>2.362</td>
<td>-221</td>
<td>-3.048</td>
</tr>
<tr>
<td>o/w related imports</td>
<td>-793</td>
<td>-491</td>
<td>-502</td>
<td>-1.109</td>
<td>-461</td>
<td>-1.237</td>
<td>-607</td>
<td>766</td>
</tr>
<tr>
<td>Services</td>
<td>-1.225</td>
<td>-734</td>
<td>-1.242</td>
<td>-1.624</td>
<td>-1.400</td>
<td>-1.253</td>
<td>382</td>
<td>-147</td>
</tr>
<tr>
<td>Income</td>
<td>-635</td>
<td>-411</td>
<td>-761</td>
<td>-1.265</td>
<td>-680</td>
<td>-680</td>
<td>504</td>
<td>0</td>
</tr>
<tr>
<td>Current Transfers</td>
<td>787</td>
<td>462</td>
<td>573</td>
<td>1.231</td>
<td>434</td>
<td>1.078</td>
<td>658</td>
<td>644</td>
</tr>
<tr>
<td>o/w official aid</td>
<td>740</td>
<td>429</td>
<td>540</td>
<td>1.019</td>
<td>415</td>
<td>954</td>
<td>479</td>
<td>539</td>
</tr>
<tr>
<td>Capital and Financial account</td>
<td>477</td>
<td>733</td>
<td>131</td>
<td>1.154</td>
<td>2.574</td>
<td>1.568</td>
<td>1.023</td>
<td>-1.006</td>
</tr>
<tr>
<td>o/w FDI</td>
<td>374</td>
<td>966</td>
<td>1.616</td>
<td>1.713</td>
<td>2.449</td>
<td>621</td>
<td>97</td>
<td>-1.828</td>
</tr>
<tr>
<td>Overall Balance</td>
<td>-307</td>
<td>-434</td>
<td>-438</td>
<td>-628</td>
<td>175</td>
<td>-1.359</td>
<td>-190</td>
<td>-1.534</td>
</tr>
</tbody>
</table>

Source: data provided by IMF and Congolese authorities.

First of all, comparing columns (b) with and (a) and (d) provides some information of the effect of the boom in 2007 and the first half of 2008. While September 2007 projections estimated exports and imports for 2008 at US$ 3 billion and US$ 3.5 billion respectively, realized figures for 2007 were already much higher (US$ 6.1 billion and US$ 5.3 billion
respectively), and this trend was continued in 2008, with exports at US$ 6.6 billion and imports at US$ 6.7 billion. Comparing (d) with (c) might also provide some idea of the cost of the crisis in 2008: exports reduced by about US$ 0.5 billion, but imports were much higher than expected (+US$ 0.5 billion), most likely due more to the crisis in the East than the financial crisis. More interestingly, comparing columns (e) and (f) provides some estimate of the financial crisis in 2009. It shows a projected huge negative impact on exports, down by about US$ 3.7 billion (US$ 3.5 billion compared to 2008 figures), due to an equivalent decrease of mineral exports; imports are projected to go down by less, estimated at about US$ 2.4 billion.

The BOP data also provide some data for other transmission mechanisms discussed in table 1. **Remittances** are not so important in the case of DRC. Official remittances declined somewhat from US$ 111.84 million in 2007 to US$ 96.86 million in 2008 (BCC data); they are projected to stay at about the same level for 2009. However, this is only capturing remittances that are channelled through the official financial system (“messageries”, such as Western Union); it is generally accepted that total remittances could be as high as five times this official figure.

The booming global demand for minerals and the consequent increase in their world price attracted large amounts of **Foreign Direct Investments** to the DRC, mainly towards the mining industry. As commodity prices declined since the second half of 2008, mining investment flows decreased significantly due to the delays or cancellation of major projects. In 2007, FDI reached US$ 1808 mln after climbing steadily for 7 years. While FDI still increased in the first half of the year, 2008 closed with a lower level of US$ 1713 mln (- 4.4%). In 2009 the IMF expects the trend of the second half of 2008 to continue, with FDI going down to a level of US$ 621 mln.

Finally, **aid** levels (in the form of grants) were much higher than projected in 2008, at around US$ 1 billion, again most likely partly due to the crisis in the East. They are projected at US$ 950 million for 2009, again higher than projected before the crisis.

Overall, the current account deficit worsened by US$ 1.2 billion, and the overall balance by about US$ 200 million for 2008; for 2009, the overall current account deficit is projected to worsen by US$ 0.5 billion, and the overall balance by about US$ 1.5 billion. Summing the imports adjustment (US$ 2.4 billion) with this overall balance gap of US$ 1.5 billion could be considered as a very rough first estimate of the balance of payments shock due to the financial crisis for 2009.

This external shock has also majorly impacted the level of international reserves. This level has been structurally low according to traditional indicators, stabilising at around one week of imports before the crisis. Figure 2 provides an overview of the most recent evolution.

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3 The Congolese central bank, BCC, could not yet provide us with estimates of actual figures for the first months of 2009.
First and foremost, the figure shows the low level of reserves, despite a major boom in export earnings in recent years, and also in 2008, which has not majorly impacted the level of reserves – again in 2008, the impact of the booming export performance in the first months of 2008 is relatively modest, with reserve levels rising to a high of US$ 270 million in April 2008. Self-insurance through some reserves hoarding has not occurred. Although this is a relative high level compared to other periods, this level equals less than two weeks of imports, much lower than the international benchmark of three months. The figure then shows the major impact of the international financial crisis: since September the foreign exchange reserves from the Central Bank have nearly evaporated. The economic crisis and the deteriorating balance of trade, mainly through lower exports, but also the increase in government expenditures that were initially financed with foreign currency have been the main reasons for this (BCC, 2009a). Reserves plunged to less than US$30 million at the beginning of March 2009, the equivalent of less than a day of imports. At mid March, the Board of the IMF decided to grant DRC access to the Rapid Access Component of the Exogenous shocks Facility and provide about US$195 million of balance of payments support to strengthen the reserves position of the Central Bank and its possibilities of intervening in the market. The disbursement of this amount is illustrated by the steep increase in the figure in March 2009 (see section 4).

We can also interpret the impact of this shock in terms of our vulnerability framework of table 1. Lacking prevention, as well as insurance, both self-insurance (as the level of reserves is very low in DRC, and heavily decreased towards the end of the year, as analysed later in this section) as well as market insurance mechanisms, coping with the crisis is the only alternative. The estimated figures of the magnitude of the shock, derived earlier, also provide some first estimate of the likely burden sharing of this adjustment cost between the country and the international community. So far, part of the adjustment cost is projected to be incurred by the country in the form of a reduction of imports (US$ 2.4 billion in 2009), and a lower
As the country cannot further reduce the current level of reserves (it should at least be US$ 200 million at the end of 2009), the total projected overall balance deficit for 2009, of US$ 1.35 billion, has to be covered by exceptional donor assistance. As will be explained in section 5 of the report, dealing with the donor response to the crisis, part of this financing is already identified, but currently, a gap of a few hundred million US$ remains. In case this exceptional assistance is not fully forthcoming, a higher share of the adjustment cost will have to be borne by the country, in the form of a larger imports reduction.

2.2 **Direct and indirect impacts on the economy of the DRC**

In this section, we provide a brief description of the impact of the current international financial and economic shock on the Congolese economy. First of all, we look separately at the real private sector, Next, we look at the impact of the crisis on the budget, and finally, on the financial sector.

2.2.1. Impact of the performance of the real economy and economic growth

Since the relative stabilisation of the country after 2002, DRC has shown a strong economic growth performance, as shown in figure 3. However, the growth is boosted by a limited number of sectors: mining, telecommunication, infrastructure and construction; and is heavily dependent on imported goods for its development.

Especially the mining sector developed considerably in recent years, driven by increased FDI in these sectors, as a reaction to increased global demand and world prices. The copper and cobalt sectors, and the mining sector in general, increased production considerably in 2007 and the beginning of 2008 as a lot of projects switched from exploration into exploitation phases. Gecamines was joined by about 200 foreign partner firms ('partenaires'), about 80 of them stock exchange listed (most of them on the Toronto stock exchange). Furthermore, some major projects were signed, including a joint venture between Gecamines and a consortium of Chinese companies, Sicomines, (linked to the development of major public infrastructure works, generally referred to as the ‘Chinese contract’).

Such a growth ‘model’, incorporating a low degree of diversification and a heavy reliance on imports even increased vulnerability to global exogenous shocks, as has been shown clearly with the impact of the economic crisis. Table 6 provides a sectoral and quarterly decomposition of the growth performance of key affected sectors. The figures show a mirror image of the BOP evolution sketched in the previous section: a huge increase in the first two quarters of 2008, followed by a severe decline in the second half of 2008 and the beginning of 2009. As a result overall growth, while strong in the first half of 2008, respectively 2.5% and 6.7% for the first two quarters, turned negative in the three subsequent quarters, with a negative growth of -1.8% for the third, -1.4% for the last quarter of 2008 and -1.3 for the first of 2009. This meant that, technically speaking, the Congolese economy entered into a recession since the end of 2008 (BCC, 2009a).

---

Originally, an overall balance surplus of US$ 175 million was projected, leading most likely to an equivalent increase in the level of international reserves.
Table 6: Sectoral and quarterly growth decomposition (2008)

<table>
<thead>
<tr>
<th></th>
<th>Overall growth</th>
<th>Mines and hydrocarbons</th>
<th>Manufacturing</th>
<th>Construction</th>
<th>Energy</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>quarterly growth rate</td>
<td>Cumulative</td>
<td>1st quarter</td>
<td>2nd quarter</td>
<td>3rd quarter</td>
<td>4th quarter</td>
</tr>
<tr>
<td>2008</td>
<td>2.5</td>
<td>2.5</td>
<td>18.3</td>
<td>0.1</td>
<td>10.8</td>
<td>3.2</td>
</tr>
<tr>
<td>1st quarter</td>
<td>6.7</td>
<td>9.4</td>
<td>3.2</td>
<td>5.5</td>
<td>8.4</td>
<td>-9.6</td>
</tr>
<tr>
<td>2nd quarter</td>
<td>-1.8</td>
<td>7.5</td>
<td>0.7</td>
<td>-6.6</td>
<td>-4.7</td>
<td>2.4</td>
</tr>
<tr>
<td>3rd quarter</td>
<td>-1.4</td>
<td>5.9</td>
<td>-12.2</td>
<td>-3.0</td>
<td>-1.4</td>
<td>-2.4</td>
</tr>
<tr>
<td>4th quarter</td>
<td>-1.3</td>
<td>-1.3</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
</tbody>
</table>

Source: BCC, 2009a; Nshue, 2009a; n.a.: not available

The negative effects on production in the mineral sector were highly visible and publicized, especially in the provinces of Katanga and Bas-Congo, with ample evidence of firms scaling down, or even temporarily stopping production (such as the diamond firm MIBA), closing down (even overnight), postponing planned production or investment plans. Also planned implementation of the Sicomines project was delayed, including for the infrastructure component (and the payment of the ‘pas-de-porte’). But, clearly, in the slipstream of this decline, sectors that are closely linked to the mineral sector, such as the service sector (including telecommunication, transport, and construction) has been severely negatively affected.

Figure 3 can also be used to give a rough estimate of the cost of the shock to the economy, as measured by the difference between projected growth rates before the crisis, and current revised growth projections. Before the crisis, economic growth was expected to increase to 10% in 2008 and 2009, even according to the latest regional economic outlook of the World Bank of October 2008; economic growth for 2008 was finally established at 5.9%. For 2009 economic projections have consecutively been revised downwards as the crisis affects the country. While the IMF expected the country to reach 4.4% in the beginning of March 2009, the most recent mission of the institution to the country revised this projection down to 2.7%. As such, the GDP cost to the country can be established at around 4.1% of 2008 GDP, and 7.3% of 2009 GDP.

Stock exchange listed firms were also more directly impacted by the severe decrease of their stock prices, in which most of them lost more than 90% of their market value.
However, this impact should not be overestimated. Overall, the DRC economy is largely informal, and as such, GDP is grossly underestimated\(^6\).

### 2.2.2. Fiscal Impact

Also the government budget has been severely impacted by the international financial and economic crisis. Before going into the detailed analysis for 2008, it is useful to describe the vulnerable nature of the budget. In general revenue mobilization is weak, and biased towards the formal business and external sector; on the expenditure side, revenues are predominantly used for wages and salaries (38% in 2008), the retrocession to the provinces and public utility companies (Régies, again about 38%), and debt service payments (17%), leaving very little if no ‘fiscal space’ for a pro-active fiscal policy and public investment, except for that created by donor projects that are included into the budget. Rather uncommon, but mirroring the economy as a whole, a large part of the revenues and expenditures are dollarized\(^7\).

Table 7 provides an overview of the evolution of the fiscal situation in 2008. In the first half of 2008, the fiscal situation of the country was under control. With a significant surplus, the country even overperformed targets agreed with the IMF within its Staff Monitored Program (SMP). The fiscal situation however deteriorated in the second half of the year. The economic crisis reduced revenues, mainly those from the mining sector and the oil producers, but most importantly the security and humanitarian problems in the east of the country put an enormous pressure on the expenditure side\(^8\). These evolutions led to fiscal deficits starting from September onwards, with a gap of US$134 million over the last months of 2008. Largely financed through monetary creation through BCC ‘avances’ (‘la planche à billets’), this impacted severely on inflation (see next section). Again, this shows the structural weakness and vulnerability of the fiscal situation. In a way, one could say that the windfall earnings

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\(^6\) A process to revise GDP calculations under way will most likely result in an estimated doubling of the official GDP figures.

\(^7\) Which does provide the government with an uncommon partial natural hedge against adverse exchange rate fluctuations, but contributes largely to the witnessed disintermediation in the foreign exchange market, and hampers the development of an active formal foreign exchange market.

\(^8\) Government expenditure for “aides, secours et indemnisations” was overexecuted by 4251% (33.724 mln FC instead of 775 mln. FC) and that for military equipment by 543% (8.921 mln. FC instead of 1.387 mln FC).
collected in the first half of the year due to the mineral boom, were not sufficient to cover the costs of the downturn later, including coping with the security shock.

Table 7: Fiscal situation 2008 (in million US$)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>1006,50</td>
<td>217,00</td>
<td>197,86</td>
<td>187,93</td>
<td>199,68</td>
<td>221,38</td>
<td>128,76</td>
<td>2159,11</td>
</tr>
<tr>
<td>o/w oil revenues</td>
<td>201,23</td>
<td>35,19</td>
<td>62,22</td>
<td>35,45</td>
<td>52,53</td>
<td>29,55</td>
<td>1,99</td>
<td>418,17</td>
</tr>
<tr>
<td>o/w mineral revenues</td>
<td>85,85</td>
<td>24,65</td>
<td>9,32</td>
<td>7,89</td>
<td>6,28</td>
<td>13,06</td>
<td>1,37</td>
<td>148,42</td>
</tr>
<tr>
<td>Expenditure</td>
<td>923,99</td>
<td>217,14</td>
<td>186,86</td>
<td>192,24</td>
<td>202,44</td>
<td>257,94</td>
<td>219,07</td>
<td>2199,69</td>
</tr>
<tr>
<td>Salaries</td>
<td>367,29</td>
<td>78,66</td>
<td>70,74</td>
<td>40,32</td>
<td>85,89</td>
<td>109,04</td>
<td>81,82</td>
<td>833,75</td>
</tr>
<tr>
<td>Retrocession</td>
<td>142,15</td>
<td>21,88</td>
<td>38,70</td>
<td>33,58</td>
<td>44,87</td>
<td>39,93</td>
<td>34,02</td>
<td>355,13</td>
</tr>
<tr>
<td>Public debt service</td>
<td>50,51</td>
<td>11,68</td>
<td>11,22</td>
<td>10,80</td>
<td>6,35</td>
<td>15,39</td>
<td>1,78</td>
<td>107,72</td>
</tr>
<tr>
<td>Other operational</td>
<td>266,53</td>
<td>70,97</td>
<td>50,25</td>
<td>91,93</td>
<td>47,03</td>
<td>62,47</td>
<td>27,51</td>
<td>616,69</td>
</tr>
<tr>
<td>Investment</td>
<td>55,35</td>
<td>31,21</td>
<td>14,38</td>
<td>10,48</td>
<td>15,33</td>
<td>17,57</td>
<td>9,56</td>
<td>153,87</td>
</tr>
<tr>
<td>Other urgent expenditures</td>
<td>20,99</td>
<td>0,00</td>
<td>0,00</td>
<td>0,00</td>
<td>9,29</td>
<td>60,01</td>
<td></td>
<td>90,29</td>
</tr>
<tr>
<td>Other expenditures</td>
<td>21,17</td>
<td>2,74</td>
<td>1,58</td>
<td>5,13</td>
<td>2,97</td>
<td>4,25</td>
<td>4,38</td>
<td>42,23</td>
</tr>
<tr>
<td>Balance</td>
<td>82,51</td>
<td>-0,14</td>
<td>11,00</td>
<td>-4,31</td>
<td>-2,75</td>
<td>-36,56</td>
<td>-90,31</td>
<td>-40,57</td>
</tr>
</tbody>
</table>

Source: Congolese authorities; exchange rate conversion based on BCC, 2009b

In the beginning of 2009 the economic recession continued to have an impact on the fiscal situation. Compared with January and February 2008, the first two months of the year showed a reduction in government revenue. As the government adjusted to the situation by revising the budget, and its expenditure and Treasury plans, moving more strictly to a cash-based budget practice, expenditures followed this reduction in revenue, which resulted in a surplus of US$9 million over the first two months. Although to a limited extent, this helps to absorb the excess liquidity created at the end of last year.

Table 8: Fiscal situation first two months of 2009 (compared to 2008 situation)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>151,95</td>
<td>134,77</td>
<td>133,01</td>
<td>123,09</td>
</tr>
<tr>
<td>o/w oil revenues</td>
<td>28,30</td>
<td>1,99</td>
<td>19,21</td>
<td>10,88</td>
</tr>
<tr>
<td>o/w mineral revenues</td>
<td>7,12</td>
<td>3,39</td>
<td>3,59</td>
<td>3,5</td>
</tr>
<tr>
<td>Expenditure</td>
<td>164,79</td>
<td>130,05</td>
<td>123,42</td>
<td>118,46</td>
</tr>
<tr>
<td>Balance</td>
<td>-12,84</td>
<td>4,72</td>
<td>9,58</td>
<td>4,63</td>
</tr>
</tbody>
</table>

Source: Congolese authorities; exchange rate based on BCC, 2009b

According to the most recent IMF projections, the current fiscal gap to be financed, after exceptional financing through the interim HIPC debt relief, is estimated at around 592 million US$, with a remaining fiscal gap still to be financed, after already identified emergency financing (World Bank, EU), of about 289 million US$.

2.2.3. IMPACT ON THE FINANCIAL SECTOR

The financial sector in DRC is heavily underdeveloped and again highly dollarized, both on the deposit as well as the credit side of the balance sheet. The system also lacks sophistication (in terms of e.g. the use of and investment in derivative instruments). Moreover, only three of the 13 banks that are currently formally licensed and operational have direct international links, i.e. Citygroup, BCDC (linked to Fortis) and Stanbic, but none of them suffered heavily
from the direct fallout of the crisis. As a consequence, the financial sector was not impacted by the international financial crisis in a direct way.

The indirect impact on the financial sector again largely mirrors developments in key affected sectors of the economy. As clients are mainly formal businesses, the increase of revenues in those sectors in recent years have increased the level of deposits and credits, including during the first half of 2008, but this has been reversed from the second half of the year on. Financial difficulties of these affected firms have also negatively affected the quality of the loan portfolio. Overall, the reduction of activity has put severe pressure on the liquidity positions of some banks, and BCC has increased the level of supervision but so far no outright rescue operations were necessary, although further caution remains warranted. In fact, unlike the Congolese authorities, the private banking sector did achieve a substantial increase in the level of foreign reserves in recent years; which self-insured the sector and managed them to deal with the crisis so far.

2.3 IMPACT ON INCOME AND POVERTY

In this section, we briefly try to describe some likely effects of the international shock on household income and poverty, by reviewing the second layer of main transmission mechanisms, as sketched in figure 1. As no formal analysis is available so far, most observations provide some preliminary, qualitative assessment only. In preparation of the second PRSP of the country, the Institut National de Statistique will do a second household survey, with support of the World Bank. This survey should provide more evidence on the microeconomic impact.

2.3.1 PRICE CHANNELS

2.3.1.1 INFLATION AND THE EXCHANGE RATE

The DRC has a largely dollar-based economy, with 85% of bank deposits denominated in dollar and 49% of the broad money. Exchange rate trends between the American dollar and the Congolese franc therefore greatly influence the country’s economic activity and inflation (AfDB and OECD, 2008). Figure 4 therefore illustrates the trends in inflation and exchange rate in a simultaneous way.

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9 Severe revealed difficulties in one bank has a large public ‘bad’ character and might easily provoke a bank run, especially in such a small market, with the level of protection of the whole system being determined largely by the situation of the ‘weakest’ bank (« weakest link technology »).
Figure 4 illustrates how the food and economic crisis has had a significant impact on inflation in the DRC and the exchange rate of the local currency with respect to the American Dollar. Inflation follows a twin peaks profile (BCC, 2008b). Between April and July 2008, inflation has known a first increase. The international food crisis (imported inflation) was one of the reasons for this higher inflation; but other important reasons have been some bottleneck problems at the Matadi port, that has distorted the production and commercialisation of certain products and the instalment of a new fiscal measure (Bivac) that lowered imports. During this first peak, changes in the exchange rate did not impact on the inflation rate.

From November 2008 onwards, a new surge of inflation came up. This time the depreciation of the local currency was one of the reasons through which inflation increased. Monetary financing of the budgetary deficit laid at the basis of the inflationary pressures through a depreciation of the exchange rate and pressure on the domestic prices. The costs for transportation, for example, have been increasing as the drop in world prices of refined oil have been more than offset by the depreciating exchange rate. The scarcity of international reserves in the Central Bank hampered the Bank’s intervention possibilities to keep the exchange rate stable.

For the whole of 2008, inflation reached 27.6%. The gliding inflation rate, counting April 2008-end March 2009, even reached 50% according to the most recent figures. According to the most recent estimates of the IMF, inflation for 2009 is projected at 27%, identical to the inflation level already reached in the first 4 months of this year. In order to make this a realistic target, this means that strict fiscal discipline must be maintained and further exchange rate depreciation must be halted.

A surge of inflation, and the danger of sliding again into hyperinflation, is a serious threat to the welfare of those that cannot protect them because they have no access to dollars, e.g. the poor. Furthermore, especially in a land such as DRC with its ‘hyperinflation’ memory, inflation surges can quickly evolve into riots and systemic crisis that could undermine the stability. However, again, one should not overestimate the direct country-wide effect of this,
as inflation discussed here is largely ‘Kinshasa’ inflation, and in other parts of the country the situation might be different. So the direct effect might be largely focusing on the capital, albeit with its potential negative systemic instability crisis effects on the whole country.

2.3.2. Employment effects

The most important direct employment effects are linked to the key affected sectors of the economy. It is extensively documented that the closing of mines resulted in massive job losses (World Bank, 2009b), not only in the formal sector, where the total employment level is limited, but especially in the informal sector, where the crisis deprived many people from exploiting new opportunities for income-generating activities in the informal sector, both within the mining sector as in derived activities. The governor of Katanga estimated the total number of losses in his province alone at 300,000, although this estimate was questioned by many of our interviewees.

2.3.3. Direct transfers, and access to public goods and services

Household income and poverty might also be affected by the direct access to transfers, or public services. Within the PRSP-process, the aim of making the budget more pro-poor was realized by identifying priority sector expenditures, and trying to protect them (‘ringfencing’) in periods of shortage of funds, e.g. in crisis. The following table 9 provides an overview of the evolution of realized pro-poor expenditures for 2008, relative to 2007.

<table>
<thead>
<tr>
<th>Functional classification</th>
<th>Nominal expenditure (mln USD)</th>
<th>% of total Expenditure</th>
<th>Nominal expenditure (mln. USD)</th>
<th>% of total Expenditure</th>
<th>Difference in % of Expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Pro-poor expenditure</td>
<td>599,08</td>
<td>33,96%</td>
<td>662,01</td>
<td>28,92%</td>
<td>-14,87%</td>
</tr>
<tr>
<td>Defence</td>
<td>5,13</td>
<td>0,29%</td>
<td>11,39</td>
<td>0,50%</td>
<td>71,09%</td>
</tr>
<tr>
<td>Order and public security</td>
<td>23,11</td>
<td>1,31%</td>
<td>24,68</td>
<td>1,08%</td>
<td>-17,71%</td>
</tr>
<tr>
<td>Economic Affairs</td>
<td>153,63</td>
<td>8,71%</td>
<td>186,34</td>
<td>8,14%</td>
<td>-6,55%</td>
</tr>
<tr>
<td>Protection of the environment, fauna and flora</td>
<td>5,42</td>
<td>0,31%</td>
<td>4,59</td>
<td>0,20%</td>
<td>-34,72%</td>
</tr>
<tr>
<td>Housing and collective equipment</td>
<td>27,29</td>
<td>1,55%</td>
<td>37,28</td>
<td>1,63%</td>
<td>5,23%</td>
</tr>
<tr>
<td>Health</td>
<td>105,56</td>
<td>5,98%</td>
<td>93,98</td>
<td>4,10%</td>
<td>-31,41%</td>
</tr>
<tr>
<td>Religion, culture, sports and leisure</td>
<td>4,80</td>
<td>0,27%</td>
<td>0,46</td>
<td>0,02%</td>
<td>-92,66%</td>
</tr>
<tr>
<td>Education</td>
<td>253,76</td>
<td>14,39%</td>
<td>278,34</td>
<td>12,16%</td>
<td>-15,50%</td>
</tr>
<tr>
<td>Social protection, social affairs</td>
<td>20,39</td>
<td>1,16%</td>
<td>24,95</td>
<td>1,09%</td>
<td>-5,70%</td>
</tr>
<tr>
<td>Total government expenditure</td>
<td>1,763,84</td>
<td>100%</td>
<td>2,289,49</td>
<td>100%</td>
<td>0,00%</td>
</tr>
</tbody>
</table>

Source: Ministère du budget (2009a)

The figures show that it has been difficult to protect the social categories of pro-poor spending in times of crisis, especially in times of conflict. Although the absolute level has increased in
2008, pro-poor spending as a % of total spending has gone down, and sectors such as health, education, and social protection saw their relative share decrease.

Again, as the government has little room for an active pro-poor policy, donor, through their projects, are largely filling the gap. But here, a major problem remains with respect to the low disbursement rates donors realize on these interventions.

2.3.4. Preliminary conclusion

Overall, experience of previous economic crisis, more specifically in Asia, have shown that poverty can increase in times of crisis, sometimes even significantly (Development Research Group, 2008 and Sumner and Wolcott, 2009). Main transmission channels have been inflation, reduced public expenditures and a reduction of GDP. As in the DRC all these transmission channels have been hit by the crisis, an increase in poverty is likely to occur. For the moment no study has been undertaken examining the impact on the poverty. Based on an estimated growth of 2.7% for 2009, an estimate that is repeatedly scaled downwards, the GDP per capita is expected to decrease as population growth was estimated at 3.2% (UNDP, 2007). Anecdotal evidence, largely collected from the Kinshasa area, suggests that the poorest are hit through the inflation that increases the cost of food directly (bread, tomatoes, onions), but also indirectly through increased transport costs. Many people have subsequently reduced the number of meals they take, to one a day or even less.

3. The government response to the crisis

Due to the severe impact of the crisis on the Congolese economy and public finances, the government has set up an inter-ministerial commission that monitors the impact of the crisis on the country and formulates appropriate policy responses for the short, medium and long term aimed at stabilising the economy and getting it back on track (World Bank, 2009b). The working group has published a note on the impact that has been updated regularly. Based on the note and other information sources, the government has already taken a number of actions.

In March 2009, the government initiated a rescue plan to tackle the effects of the international economic and financial crisis on the national economy (DRC, Commission interministrielle, 2009). Its resource envelope is estimated at US$ 695.0 million, of which US$ 325.0 million for actions in the short run and US$ 370.0 million for actions on the medium to long term (Nshue, 2009b). The main measures put forward in the plan are:

- the stabilization of the macroeconomic framework;
- lifting the obstacles to the conclusion of a PRGF-program with the IMF;
- the rapid mobilization of resources to finance the ‘5 chantiers’ identified in the country’s PRSP;
- the clearance of arrears owed to public institutions, to allow them to execute their investment programs;
- the disbursement of counterpart funds for projects co-financed by external partners;
- the reinforcement of public/private partnerships;
- the provision of legal security to investors and abolition of administrative complexities.
3.1 **SHORT-TERM MEASURES TAKEN.**

Due to their limited means, the Congolese authorities are hardly able to undertake any measures in the short term to mitigate the impact of the crisis on its citizens. The most important focus of the government in the short term should therefore be to take the necessary anticyclical measures, both fiscal and monetary, to stabilize the economy. To increase fiscal space in the short-run they rely on (additional) donor funds.

3.1.1 **FISCAL**

A already highlighted in the previous section of the report, and although the budget of the Congolese government has already significantly increased over the past years, the authorities have always been confronted with severe limits on the available fiscal space. The need for donor financing for the functioning of essential public services has therefore been high. Faced with the economic crisis, this fiscal space has been further reduced, leading to monetary financing at the end of 2008. To maintain macroeconomic stability, a necessity for growth to pick up again, and to avoid social unrest, the government has taken a number of short term measures.

Faced by the economic crisis, the budget of 2009, voted in the parliament at the end of December 2008 was revised. The budget, based on a macroeconomic framework of a 5.8% growth rate and an exchange rate of 585FC per dollar, anticipated revenues of 2,9bn FC. Adjusting to the new economic circumstances, a revised budget was worked out based on more realistic revenue and expenditure projections (World Bank, 2009a).

In the execution of its budget, the government, in agreement with the IMF, focuses on a number of key short-term measures to maintain a fiscal equilibrium and economic stability (World Bank, 2009a and IMF 2009a):

i. the budget should be executed on cash basis, targeting zero government borrowing from the Central Bank, to avoid exchange rate depreciation and inflation spirals;

ii. redirecting spending to activities that would prop up domestic demand;

As the basis from which the taxes are collected has been significantly reduced due to the economic crisis, the government has been trying to recover some of its lost taxes from other sources. Some of these propositions have shown to be more successful than others:

- During the last months, the private sector is subsequently faced with new taxes, with some critical observers describing this as fiscal harassment. While these taxes can in the short term increase revenues, in the long term it is likely to push private actors from the formal to the informal sector.

- The Impôt Professionnel sur les Rémunérations (IPR), collected from public and private enterprises, is also collected from political institutions (e.g. cabinets) since March 2009. In March, this measure allowed the government to collect FC 952 mln. Later the measure will also be applied to the provincial institutions (Ministère du budget, 2009b).

- Since the end of March 2009, passengers leaving from N’djili airport in Kinshasa are asked to pay US$50 to leave the country.

Despite these efforts, for 2009, a fiscal gap persists (estimated at US$100 mln. at the beginning of April 2009) that would necessitate further government spending cuts if not closed by additional short-term donor assistance.
3.1.2. Monetary and exchange rate

Concerning monetary policy, the authorities aim for a reduction of the excess liquidity in the economy in order to ease the pressure on the internal prices and the exchange rate. The dollarization of the economy limits however the effectiveness of the monetary policy:

- Despite the low amounts of foreign exchange reserves at the Central Bank, the Bank initially kept selling dollars to absorb the excess liquidity and to ensure the vital imports towards the country. These interventions should assure a regular and stable provision of imports, like petrol, construction products, food... Since January 2009 the Central Bank stopped these interventions as reserves were too low. After receiving the exceptional ESF balance of payment support of the IMF, the Central Bank announced on April 13 2009 that it would again start selling foreign exchange, hoping to make the local currency recover some of its lost value. The operation was announced to take place whenever the currency loses 1.5% of its value (Xinhua, 2009).
- The Central Bank also increased its central bank policy rate in three steps to absorb the excess liquidity:

<table>
<thead>
<tr>
<th>Table 10 : Policy Rate of the Central Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 2008</td>
</tr>
<tr>
<td>Policy rate</td>
</tr>
</tbody>
</table>

Source: BCC 2009a

- The sale of treasury bills is a final intervention used by the Central Bank. Despite the higher interest rate, the demand for the bills has been low due to the high inflation, limiting the actual effectiveness of this intervention mechanism.

Finally, the government should undertake every effort necessary to normalize its relation with the international financial institutions. This would not only create additional fiscal space in the country’s budget, by reducing the current debt service due to the IMF, but could also mobilize additional financing from other donors that feel now restraint as the country is not in program with the IMF. In the medium term, it could result in reaching the HIPC Initiative Completion Point, which is already floating since the country reached Decision Point in July 2003.

To achieve this, the government restarted discussions with the IMF in mid-March 2009 to conclude a new three-year program. The latest IMF-mission, residing in Kinshasa from March 16 to March 31, 2009 gave its final discharge to conclude a triennial program supported by the Poverty Reduction and Growth Facility (PRGF). Before the program could retroactively start in April 2009, a number of preconditions need to be fulfilled, more particularly on the renegotiation of the Sicomines contract. The finalization of the feasibility study on the contract might serve as an input to these discussions.

The 3-year PRGF program would, in a first phase, focus on macroeconomic stabilization. If the first review of the new program (fixed for September 2009) leads to conclusive results, the country will be able to benefit from an assistance of US$ 120.0 million balance of payments support. If the country by then also manages to achieve the remaining completion point trigger criteria (see annex 2), the DRC will also be able to reach the completion point of the HIPC Initiative in December 2009, providing access to external debt cancellation of about US$ 9 billion in net present value terms not only through the HIPC initiative, but also through its successor, the MDRI.
3.2 **Medium-term measures to be taken.**

The long-term development strategy of the Congolese Government has been formulated in a PRSP, adopted by the transitional government in July 2006: the Document de la Stratégie de Croissance et de Réduction de la Pauvreté (DSCR). After the elections, the new government endorsed it in March 2007. The strategy was finalised three years after the adoption of an interim-version and aims at contributing to political stability within the country. The strategy is based on five pillars, taking into account the specific post-conflict situation of the country:

1. Promoting good governance and consolidating peace by reinforcing the institutions,
2. Consolidating macroeconomic stability and economic growth,
3. Improving access to social services and reducing vulnerability
4. Combating HIV/AIDS
5. Supporting the community dynamics.

Based on the PRSP, the government formulates medium term programmes, the Programme d’Actions Prioritaires, of which the first ended in December 2008 and a second is being finalised.

By 2010, the government envisages the formulation of a new PRSP. To avoid the limited alignment of the first PRSP to the annual budget of the government, the new strategy should be more prioritised and should be clearly linked to Medium-Term Expenditure Frameworks (MTEFs) that are annually translated into budgets. The actual setup of 15 Thematic Groups should be used as a concertation structure between government and the different development partners, both bilateral and multilateral donors but also civil society, NGOs, syndicates, private sector representatives. To accelerate growth, most interviewees agreed that the focus of the new strategy should be on large-scale investment in the agriculture sector and an improvement of the overall business environment.

To achieve the enormous growth potentials of the country, the government should therefore increase its efficiency and lure the (foreign) private sector into investing in the country. Therefore, a number of, often ongoing, structural reforms have to be taken, or accelerated, in the medium term, including (Jahjah, 2009).

- Reform of the civil service
- Reform of the public enterprises
- Abolition of monopolies and price restrictions
- Reform of the “régies financières”
- Reform of the Central Bank
- Development of the financial sector
- Governance and transparency.

In the short run, there is however an urgent need for agreement between the government and the donor community on a limited list of key actions that are relatively easy to take, but might have a big development and reputational impact on the country. In the medium term, these critical reforms need to be further implemented, if necessary with support of the donor community.\(^{10}\)

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\(^{10}\) Often heard examples are the OHADA-agreement, the code marché public, the legalization of the mining contracts, etc...
3.3 Potential Constraints.

The success of the short and medium-term interventions and plans will be highly dependent on relieving a number of constraints (Jahjah, 2009).

- **Political constraints:** To attract foreign investors, a normalization of the security situation in the East of the country should be key. The reform programs for the civil service should be more broadly owned and the decentralization process should be further implemented.

- **Economic and fiscal constraints:** In order to restore public finances and to increase public investments, government domestic revenue mobilization will have to be increased. Donor resources are disbursed with much delay and the government budget is not aligned to the priorities formulated in the DSCR.

- **Infrastructural constraints:** Due to the different conflicts in the country over the last decade, the economic and social infrastructure of the country has totally degenerated. Absence of this infrastructure increases however the costs of doing business and limits the further development of health and education services towards the population.

- **Human constraints:** Due to the poor human capacities of the public administrations the budgets are only to a limited extent coherent with the PRSP.

- **Constraints related to statistical information:** The low quality of the country’s statistics raises problems for the monitoring and evaluation of the programs formulated by the government. In this way it is also difficult to see what impact they have on the country’s poverty level.

The most important constraints can be summarized more broadly into an institutional and governance constraint, as e.g. proxied by the World Bank governance indicators, and illustrated for the case of DRC (relative to the Sub-Sahara African average).

**Figure 5: World Bank Governance Indicators (SSA and DRC).**

![World Bank Governance Indicators](source)

The essence of the situation in DRC is described amply by the fact that this weak governance situation provokes a low level of current development and (over?)prudent behaviour of
(foreign) investors and the donor community. In order to escape from this trap, it is essential that the government can credibly show its commitment to improve its weak institutional governance situation to its development partners and the private sector, and continue to build a reputation in this field.

4. REACTION OF THE INTERNATIONAL DONOR COMMUNITY

In the recent evolution of aid to the DRC, two periods can be distinguished. During the nineties, until the beginning of the new century, the different conflicts made that structural aid was replaced by humanitarian assistance. Although to a lower extent, humanitarian programs are currently continuing, mainly in the Eastern, conflict-affected parts of the country. Since 2002 structural relations between the government and donors have been resumed. In 2002 this resulted in a new Poverty Reduction and Growth Facility programme with the IMF, bringing in also other multilaterals, and access to interim HIPC debt relief in 2003, through reaching a HIPC decision point agreement. Although the country’s performance under the PRGF program necessitated the IMF to stop its program in 2006, the structural support to the country remained important due to the relative stabilization of the political situation in the largest part of the country.

Over the last three year for which data of the DAC is available, net ODA was on average US$ 1.7bn, or 22.1% of the country’s gross national income. The bilateral share has always constituted the major part of the aid, 65% on average for the period 2005-2007. Largest bilateral donors were the United States, Belgium and the United Kingdom. Due to the low performance of the public financial system, nearly all aid to the country is given in the form of non system-aligned projects or programmes. The latest Paris Declaration survey of 2008 showed that none of the donors uses the PFM system of the recipient country and that only 1% of the aid uses the country’s procurement system. In November 2007 representatives from 15 donor countries and 10 international organizations met in Paris to discuss the progress made by the country over the last few years and its future prospects. To support the implementation of the country’s PRSP and Programme d’Actions Prioritaires (PAP), donors pledged US$ 4 billion (World Bank, 2007). A Congolese Aid Effectiveness Forum is scheduled to take place in June 2009.

4.1 CURRENT RESPONSE OF THE DONOR COMMUNITY

The way the DRC has been hit heavily by the worldwide economic crisis has brought about a number of reactions from the donor community. The different reactions taken by the donors can be grouped into two clusters, in line with the analysis of the main problems faced by the country:

- Macro-level emergency balance of payments support and budgetary support to ensure macroeconomic stability, the import of necessary goods and the functioning of minimal public services.
- Earmarked micro-level support to ensure safety nets for the population. These are mainly highly labour-intensive public works, such as road building, that tackle at the same time the pressing infrastructural constraints of the Congolese economy.
The main reactions of the multilateral donors have been:

- In March 2009, the Executive Board of the IMF approved the disbursement of US$ 195 million under the Rapid Access Component of the Exogenous Shocks Facility. This balance of payment support, already fully disbursed by the end of March, aims at rebuilding a minimal level of foreign reserves at the disposal of the BCC. At mid April, these reserves allowed the Central Bank to re-intervene in the exchange rate market.

- At the end of February 2009, the DRC was one of the first two countries benefiting from the World Bank’s IDA Financial Crisis Response Fast Track Facility. US$ 100 million was approved to assist the country on three aspects to combat the crisis. The approved project consists of three components (World Bank, 2009c):
  - US$ 58 million is reserved to ensure the availability of critical imported goods (foodstuff, construction materials, telecommunication equipment and oil products).
  - To protect the functioning of essential social services, US$ 16 million will be used to finance one month wages for primary and secondary school teachers. In a first phase up to 70% of the teachers’ salaries will be reimbursed under retroactive-financing. The balance will be released upon conclusive audit of the eligibility of salaries paid by the government.
  - To prevent the deterioration of financial situation of basic utility services, a third component will finance state water and electricity bills for US$ 26 million. During the mission, the World Bank proposed another intervention that should help the population affected in Katanga. US$ 10 million would be reserved for public work programs demanding large amounts of labour (US$ 9.5 million) and professional training for people that lost their job in the crisis (US$ 200.000). In this way 42.000 man months of labour would be created.

- The African Development Bank is currently preparing a project of US$ 95 million. The setup of the project will be similar to the one of the World Bank with different components assisting the country with a mix of balance of payments support for the import of essential goods and budgetary support to ensure essential services.

- In reaction to the food crisis, and to promote food security, the European Commission established a special credit line from which the DRC received €48 million. After the receipt of a comfort letter from the IMF and based on an audit of expenditures related to food security in the government budget, the EC is prepared to refinance these expenditures; as such this is a form of disguised, exceptional budget support. Furthermore, in a specific response to the international financial crisis and its impact on developing countries, the Commission launched a new initiative on the 8th of April 2009, announcing to set aside €500 million, to be disbursed in budgetary support to those countries most hit by the crisis. Taking into account the criteria used by the Commission to assess the vulnerability of countries (dependence on export revenues, capacity to react and dependence on external financial flows), DRC will likely be one of the recipients (European Commission, 2009). In the meantime, it has been estimated that DRC might benefit from this new budget line to the amount of about €45 million.

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11 To ensure consistency between the interventions of the World Bank and the African Development Bank, the list of critical imported goods that are eligible for financing under their interventions is likely to be harmonised.
According to the latest estimates, these multilateral efforts will not close the BOP gap, nor the remaining fiscal funding gap of US$ 100 million identified in the Congolese budget. This puts pressure on bilateral donors, including Belgium, to (partly) footing the remaining bill. If not, the remaining gap will need to be filled by the Congolese government through a further reduction in imports and other budgetary expenditures, or, a return to monetary financing, which is clearly to be avoided.

Another, highly coordinated donor intervention, albeit not as a direct response to the current crisis, refers to the amount of (interim debt relief) related to the HIPC initiative. So far, exceptional finance under the form of interim debt relief is provided by the WB and the ADB, as well as by Paris Club bilateral donors. In fact, Paris Club donors are currently going beyond interim HIPC debt relief by allowing the country not to service its debt, which is an additional form of emergency budget support.

From the side of the bilateral donors, no additional emergency support has been provided until recently. Particularly for the Belgian Cooperation, the formal dialogue and structural cooperation with the Congolese authorities, through the comité des partneraires, has been resumed very recently. From the other bilateral donors a number do not focus on specific emergency interventions, they try to enhance the implementation of their already agreed interventions.

At the end of April, at the occasion of the relaunch of the comité des parteraires, Belgium and the Congolese authorities announced agreement on the disbursement of €20 million in macroeconomic support.

4.2 How to further optimize future donor reaction?

Following the intervention of Belgium, it can be expected that a number of other donors will announce similar macroeconomic support. Besides macroeconomic support directed towards the government of the DRC, the idea of a World Bank Trust Fund is also circulating, to pay the multilateral debt that is still a significant burden for the Congolese authorities (US$ 60-65 million to the World Bank).

In case more emergency type of support is needed, a more fundamental question remains whether it is not the task of multilateral donors to fulfil this role, given also the fact that the international community at the G20 Summit in London in April agreed to a major increase in the resource envelope available to the IFIs, to help them in tackling exactly these issues12.

More general, and related to the current dominant project aid modality, donors are looking at ways to be able to accelerate aid disbursements13. One way of doing that would be to (temporarily) relax the amount of counterpart, or matching, funds that the country is supposed to provide, if the crucial bottleneck is indeed the lack of resources at the government level.

12 Again more conceptually, the emergency should be outside the government’s control. Of course, one needs to be sure that a government does not purposefully lead a country into a state-of-emergency so that it receives additional funding assistance.

13 To give an example, for the DRC, the World Bank estimates that an acceleration of the rate of disbursement by 3% of its total project portfolio, would free US$ 75-100 million on an annual basis, of which US$ 50-70 is spent on local expenditures (World Bank, 2009a).
Cost-sharing, while perhaps ideal, may be unrealistic and harmful when resources are scarce. Slowing things down further because poor governments have run out of money worsens the fiscal cycle at exactly the wrong time (Kharas, 2009)

More in the longer term, and again referring to our vulnerability framework of table 1, multilateral donors should provide more opportunities for poor countries to engage in market-based insurance and hedging facilities, including providing financing instruments with in-built hedging features.

5. Conclusion

The main transmission channel of the economic crisis on the Congolese economy has been the trade channel, in which exports of mineral products (copper, cobalt, diamond, gold) have been seriously hit. On the revenue-side of the DRC government budget, revenues have decreased as private producers of mineral exports have shut down their extractive activities due to the decreasing prices on the international markets. On the expenditure side, pressure has remained due to the security crisis in the east. Monetary financing of the expenditures resulted in inflationary pressures and a depreciating exchange rate.

To balance decreased resources with increasing budgetary needs, in the short term, the authorities aim at restoring macro-economic stability, by taking fiscal measures (cash-based budgeting, aiming at avoid new fiscal deficits), and monetary and exchange rate interventions to reduce inflation and further exchange rate depreciation. In the medium term, through negotiating a new PRGF programme with the IMF, the government aims at reaching completion point under the HIPC Initiative, and finishing a second PRSP, which would revigorate donor flows. Longer term sustainable economic growth should result from a wider diversification of the economy, with a specific focus on the agricultural sector, and an improvement of the institutional governance situation, breaking the country’s governance trap, and an improvement of the business environment. Also, a lasting solution for the crisis in the East should be achieved.

In the DRC, the main multilateral donors have reacted with emergency support mixing balance of payment and budgetary support. All donors try to support the government by executing their programmed projects which are predominantly aimed at sectors that provide social protection against the crisis. However, donors in DRC have great difficulty in getting their projects executed, experiencing very low project execution rates. In the medium term, donors should support the government in securing HIPC debt relief, and supporting the government’s programme through the new PRSP, supporting also the attempts to broaden economic growth.
References


European Commission (2009). Supporting developing countries in coping with the crisis. Communication from the commission to the European Parliament, The council, the European Economic and Social Committee and the Committee of the regions. European Commission, Brussels


## Annex 1: Agenda of the Mission and Persons Met

<table>
<thead>
<tr>
<th>Date</th>
<th>People Met</th>
<th>Function and Institution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monday April 6</td>
<td>1. Daniel Mukoko Samba, Luc Madinda Tshongu, Marceline Nkondi Nsala et Paul Cartier 2. Philippe Bronchain 3. Katrien Meersman 4. Jean-Pierre Noterman 5. Loïc Duarte et Patrick Salles</td>
<td>Directeur de Cabinet adjoint à la Primature; Premier Conseiller d’Ambassade, Ministère de la Coopération Internationale et Régionale; Economist, Banque Centrale du Congo; Ministre conseiller de coopération, Ambassade de Belgique; Attaché de coopération, Ambassade de Belgique; Attaché de coopération, Ambassade de Belgique; Conseiller Adjoint de coopération, Ambassade de France; Directeur, Agence Française de Développement RDC</td>
</tr>
<tr>
<td>Tuesday April 7</td>
<td>6. Vincent Ngonga Nzinga 7. Alexandre Nshue 8. Roger Bisimwa Namushenyi 9. Francesca Bomboko, Jocelyne Nkongolo, Fidèle Tshingombe, 10. Magloire Ntomo Nzuzi</td>
<td>Directeur Direction des Études, Banque Centrale du Congo; Conseiller chef du Cabinet adjoint, Premature; Directeur Général Adjoint, Direction Générale des Recettes Administratives judiciaires, Domaniales et Participations (DGRAD); Ministre des Finances Coordinatrice nationale, Observatoire Congolais de la Pauvreté et l’Inégalité (OCPI); Ministre de Plan; Economiste, OMNI Consulting; Professeur Université de Kinshasa, Consultant; Responsable du Bureau Aides Extérieures et Coopération Internationale, Banque Centrale du Congo</td>
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<tr>
<td>Wednesday April 8</td>
<td>11. Kouassi A. Hyacinthe et Coulibaly Medjomo 12. Participating in a World Bank session 13. Mwema Mulungi Mbuyu et Adam N’Tumba Kilala</td>
<td>Principal Macro-Economist, African Development Bank; Resident Representative, African Development Bank; “Comment gérer le portefeuille pour répondre au mieux a la crise financière”; Directeur Général Adjoint, Agence Nationale pour la Promotion des Investissements (ANAPI); Chief Officer, Agence Nationale pour la Promotion des Investissements (ANAPI)</td>
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<tr>
<td>Thursday April 9</td>
<td>14. Ben Mellor 15. Michel B. Losembe 16. Yvon Bouthilette et Vincent Makaya 17. Jeroen Willems 18. Dinner with Dominique Struye de Swielande; Alain Lubambo Wa Lubambo; Raphaël Mondonga-O-Batobandelye ; Samir Jahjah; Daniel Mukoko; Alessandro</td>
<td>Chef de Mission, Coopération Britannique; Président de l’association congolaise des banques; Regional Trade Commissioner, Embassy of Canada; Coordonnateur des services professionnels et Conseiller en économie; Section Economie, Gouvernance et Droits Humains; Delegation of the European Commission in the RDC; Ambassadeur de Belgique; Vice Ministre du Budget; Secrétaire Général au Ministère de la Coopération Internationale et Régionale; Representant of the IMF in the DRC; Directeur de Cabinet adjoint à la Primature; Chef de la Coopération, Delegation of the European Commission in the RDC; Conseiller du Chef de l’Etat, Collège Economique, Financier et Monétaire; Ministre conseiller de coopération, Ambassade de Belgique</td>
</tr>
<tr>
<td>Name</td>
<td>Position and Responsibilities</td>
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<tr>
<td>Palmero; Jean Amisi Mutumbi K.; Paul Cartier</td>
<td>Poverty Reduction adviser, Banque Mondial Ministre conseiller de cooperation, Ambassade de Belgique; Directeur de Cabinet adjoint à la Primature; Premier Conseiller d'Ambassade, Ministère de la Coopération Internationale et Régionale; Economist, Banque Centrale du Congo; Attaché de la coopération au Développement, Ambassade de Belgique; Attaché de la coopération au Développement, Ambassade de Belgique; Conseiller chef du Cabinet adjoint, Premature</td>
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<tr>
<td>Abdou Salam Drabo</td>
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<tr>
<td>Debriefing with Paul Cartier; Daniel Mukoko; Luc Madinda Tshongu; Marceline Nkondi Nsala; Guy Boreux; Jean-Pierre Noterman; Alexandre Nshue</td>
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<td>Friday April 10</td>
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<tr>
<td>Samir Jahjah</td>
<td>Resident Representative IMF</td>
<td></td>
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<tr>
<td>François Kabuya-Kalala et Tshiunza Mbiye</td>
<td>Professors at the Faculté Catholique de Kinshasa</td>
<td></td>
</tr>
<tr>
<td>Odon Nsampanga Assas,</td>
<td>Chef de Division, Direction de la Préparation et du Suivi du Budget, Ministère du Budget</td>
<td></td>
</tr>
<tr>
<td>Saturday April 11</td>
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</table>

Besides, we would also like to thank the people we could speak informally in Kinshasa.
## ANNEX 2: HIPC COMPLETION POINT TRIGGERS

<table>
<thead>
<tr>
<th>Triggers</th>
<th>Progress status August 2008</th>
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<tbody>
<tr>
<td><strong>1. PRSP</strong></td>
<td>Ongoing. The full PRSP was completed through a participatory process, and adopted by the Government in July 2006. The newly elected Government endorsed it in March 2007. The PRSP and the JSAN were presented to the Bank Board in May 2007. The Government made the PRSP its document of reference and used it extensively to elaborate its Program 2007-2011. The PRSP progress report at end-June 2008 is being finalized.</td>
</tr>
<tr>
<td>Completion of a full PRSP through a participatory process and its implementation for one year, duly documented in the DRC’s annual progress report, and confirmed as satisfactory by a joint staff advisory note (JSAN).</td>
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<tr>
<td><strong>2. Macroeconomic stability</strong></td>
<td>Mixed. Inflation increased considerably at end-August 2008 compared to 2007 due mainly to higher food and oil prices. Annualized inflation reached 32.10 percent against 9.96 percent in 2007 and an end of year objective of 23.50 percent. On a monthly basis, inflation slowed down in July (3.47 percent) and in August (1.06 percent), compared to June (4.62 percent). On the foreign exchange market, the Congolese franc stabilized vis-à-vis the dollar to around CDF 555/1USD since February 2008. Compared to December 2007 it depreciated by 10.1 percent after reaching CDF 559.65 at end August 2008.</td>
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<tr>
<td>Continued maintenance of macroeconomic stability after reaching the decision point, as evidenced by satisfactory performance under a program supported by an arrangement under the IMF’s PRGF.</td>
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<tr>
<td><strong>3. Use of budgetary savings resulting from enhanced HIPC Initiative-related debt service relief during the interim period for poverty-related expenditures in accordance with the I-PRSP, with supporting documentation satisfactory to the staffs of IDA and the IMF.</strong></td>
<td>Ongoing. An external audit of the HIPC account to assess the use of budgetary savings from the enhanced HIPC Initiative account has been completed in June 2007. Findings were mixed; however recommendations for improvement have been made.</td>
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<tr>
<td><strong>4. Public expenditure management</strong></td>
<td>Ongoing. (a) The budget-execution system is improving but very slowly. A reporting mechanism is in place within the public finance management system, the <em>Chaine de la dépense</em>. General budget execution reports (<em>États de suivi budgétaire - ESB</em>) are produced, but not on a regular basis and their quality is yet to improve. However, delays in producing ESB harmonized with the State financial operations table (<em>Tableau des opérations financières de l’État - TOFE</em>) are considerable. Sectoral budget execution reports are prepared by line ministries and sent to Ministry of Budget but are not exhaustive to be used by the latter. Treasury accounts produced monthly are as well not yet exhaustive and reliable. (b) The double-entry system is being implemented. The staff have been trained, equipment purchased, and software developed. Additional efforts are needed for the staff to master the new system; (c) A new classification has been adopted. The budgetary reports are produced using economic, administrative, and functional classifications, but with a lag of 2-3 months.</td>
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<tr>
<td>(a) Implementation of a modernized budget-execution system, providing information from commitment to payment, and allowing for the monitoring of arrears; (b) adoption and implementation of a double-entry Government accounting system and a new chart of accounts; and (c) production of quarterly budget execution reports using economic, administrative, and functional classifications.</td>
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<tr>
<td><strong>5. Governance and service delivery in priority sectors</strong></td>
<td>Partially done. (a) (i) The treasury monitors poverty-related public expenditures in all sectors, using the new budget classifications. (ii) Evaluation by user groups of health</td>
</tr>
</tbody>
</table>
### development and infrastructure expenditure, consisting of:
- (i) monitoring the execution of poverty-related public expenditure;
- (ii) evaluation by user groups of the quality of related public services, and
- (iii) evaluation by service-providers of constraints to effective provision; and

(b) Adoption and implementation of a new procurement code and key implementing decrees.

### 6. Social and rural sectors

Adoption of sectoral development strategies and related implementation plans for health, education and rural development, which are satisfactory to IDA.

**Partially done.** The country health status report was issued in May 2005. Health sector strategy was completed in March 2006 based on the findings of this report. In the field of education, the Government finalized, in September 2004, the Status Report on the National Education System, which assesses the sector’s constraints, and adopted a draft action plan for the Education for All (EFA) Initiative. The education sector strategy was drafted in the second quarter of 2006. An agriculture sector review was completed in May 2006, while the rural development strategy is under preparation.

### 7. Debt Management

Installation and full activation of a computerized debt recording system, covering public and publicly-guaranteed debt that can:
- (a) produce monthly debt-service projections, and incorporate actual disbursement and debt-service payment execution data;
- (b) produce advance monthly debt service projections that will be published quarterly; and
- (c) support the centralization of debt information into a single center.

**Partially done.** A public debt management software system (DMFAS / SYGADE) was installed, and the public external debt outstanding was recorded. The implementation program, including the training of the relevant staff on debt management is now complete although OGEDEP is still not producing or publishing the debt service required statistics, in particular projections. A Prime Minister decree strengthening the role of OGEDEP as the single debt information center has been signed on February 2008 and a related action plan validated by the Minister of Finance on May 2008.

Source: World Bank, 2008a
Annex 3: Terms of Reference

“Development Cooperation addresses the Impact of the Financial and Economic Crisis on Low-Income African Countries”

CASE STUDIES IN SENEGAL, DRC, TANZANIA

Terms of Reference

Background

The Belgium’s ‘Development Cooperation Assises’ is a forum of Belgian Development Cooperation policy makers and development actors, civil society/NGOs, parliamentarians and academics, allowing exchange and consultation on different subjects related to Belgian support of the development process in developing countries. The purpose of the Assises is to raise awareness about development cooperation in Belgium, to reflect on international trends and to debate on the broad orientations of Belgian Development Cooperation in view of better responding to the challenges defined by the development process.

In 2008, the harmonization and alignment of the Belgian Development Cooperation within the framework of the Paris Declaration was the key subject of the Assises. The main theme of its second Assises to be organized on May 5-6 2009 in Brussels, Belgium, will be: “Development Cooperation addresses the Impact of the Financial and Economic Crisis on Low-Income African Countries”.

Context

There is a reasonable chance that Africa may come out of the current global financial crisis less bruised and battered than some other parts of the world. At this moment, there is less systemic risk in any African country in terms of banking than elsewhere in the world.

However, the impact of the global financial crisis will be mostly indirect and spilling over to the real economy in Africa’s low-income countries causing inter alia slowing trade flows, reduced remittances, declining aid and a drop in foreign investments followed by exchange rate depreciation and higher interest rates on capital markets.

The impact of the crisis will vary from country to country and effects will be spread over time. The objective of this year’s Assises is to explore the expected impacts in Africa’s low income countries, the population groups going to be most affected and the main channels or mechanisms through which this is going to happen.

The key issue for partner countries, donors and development actors is how to ensure a rapid return to a sustained, inclusive, pro-poor growth pattern and reduced poverty for the most vulnerable. Lessons can be learnt from past successful experiences in Africa and beyond in sustaining economic progress and weathering economic crises. The aim is to identify priority or key policy responses or measures that can have a rapid impact on the well being of the most affected.

Case Studies

In view of preparing the debate to be held during the Assises, three case study papers will be developed on three partner countries of the Belgian Development Cooperation: Senegal, DRC and Tanzania. The goal of these case studies is to improve insights into the impact, policy responses and aid consequences of the financial crisis. Papers will be prepared by research fellows or academics from Belgian or foreign universities in collaboration with the Offices of the Belgian Development Cooperation Attaché in the Embassies of Belgium in the partner countries.
Papers will provide concrete answers to the questions formulated below and will make operational recommendations for the donor, and in particular Belgian, response.

**Guiding questions and topics to be considered**

The list of topics and guiding questions to be considered is provided below:

**A. Impact**

1. *What does the current economic and financial crisis mean for the partner country in the wake of the recent fuel and food price shocks?* What are the main channels of contagion of the global financial crisis to the partner country?

2. *What impacts and consequences of the economic and financial crisis could be expected to occur in the short term (2009-2010) or in the medium term (2011-2012)*? More precisely what are the direct and indirect impacts of the crisis on the partner country at hand? What are the consequences of the crisis on domestic resources and on access to ODA as well as private flows for social services and infrastructure financing?

3. *What will be the impact on economic growth, development and poverty reduction on the country at hand?*

4. *Which sectors, population groups or areas are being / going to be most affected?* What are the main channels or mechanisms through which they are going to be affected?

**B. Policy responses**

1. *Which measures has the country taken so far to offset the direct and indirect impacts of the economic and financial crisis listed above?* What are the priorities/objectives of the policy response in the short term and in the medium term? Is the impact of the crisis monitored in the partner country? (Yes/No) Does the country have the capacity to formulate an appropriate response policy? (Yes/No)

2. *What key policy measures and reforms are the focus of the government of the partner country to accelerate growth and/or to continue progress on poverty reduction in spite of the unfavourable global environment (either in the form of growth stimulus or the implementation of appropriate forms of social protection of those most affected).*

3. *What priority policy measures can be taken that can have a rapid impact on the wellbeing of the most affected groups in the short and in the medium term (e.g., tax cuts, subsidies, social safety nets, labour intensive public works programs, conditional cash transfers or food distributions)*? How can the targeting of potential policy responses be improved?

4. *What will be the budgetary impacts of the policy response?* How to balance fiscal sustainability with growing demands for public investment in infrastructure and achieving the millennium development goals? What are innovative ways of mobilising resources and of effectively using them in light of a possible reduction in aid and foreign investment flows? Is there a role for public-private partnerships as an alternative for infrastructure or social service financing?

5. *How can donors best support reform efforts to help the partner countries seize opportunities and reduce vulnerabilities?*
6. What role could be played by the private sector?

C. Donor response

1. Is there any donor reaction so far? If yes, please specify. Does Belgium engage in the collective effort of donors to react to and support the partner country to mitigate the impact of the crisis? If yes, please specify. Is the Belgian engagement appropriate or can it be improved and how?

2. Has the response of the international community so far been coordinated and/or have multi-donor aid mechanisms been put in place?

3. How should donors further react to mitigate the negative impacts of the crisis on the partner country? Are any modifications in the nature of donor interventions necessary? Is the current array of interventions of the Belgian Development Cooperation in the partner country appropriate to deal with some of the negative consequences of the financial and economic crisis? If not, what essential type of interventions are lacking? Is there any need to scale up existing interventions, to reorient them to other themes or sectors or to front load the available programmed resources in view of responding to urgent short term needs? How to ensure that aid provides counter-cyclical relief to the partner country rather than pro-cyclical distress?

4. What would be the impacts of the decrease in quantities of ODA?

5. Should the partnership with the partner country evolve or be extended in the spirit of the Monterrey Consensus – taking into account trade, debt, research and technology transfer, private sector promotion, domestic resources, policy coherence as well as ODA - to better address current and future challenges?

6. What is / can be the role of private investors and non-governmental actors in the process?

7. What role can Governments, international organisations, civil society and the private sector play to ensure that financial and economic crises do not have a disproportionate negative impact on women and children?

Organisation, outputs and timeline

Interest of universities or research institutions in contributing to one of the case studies (Senegal, DRC, Tanzania) will be sounded by the Directorate-General for Development Cooperation (DGDC) of the Belgian Federal Public Service Foreign Affairs. Three universities - each of them will be attributed one partner country - will be selected in February 2009.

Researchers will be expected to work in collaboration with the DGD Headquarters and with the Offices of the Belgian Development Cooperation Attaché in the Embassies of Belgium in the partner countries, who will provide the necessary guidance and suggest potential useful contacts in the case study countries.

The research should be done based on both the wealth of material that exists on the topic as well as on primary sources (e.g., interviews of/contacts with relevant partner country development actors, local academics/researchers, field visits …).

The expected outputs are:
1. **Each research team will prepare a ‘country case study’ paper** of ten to twenty pages, to be made available to the DGD by mid-April. These papers will be distributed during the Assises. When drafting the papers the researchers should keep in mind that the audience of the Assises is partially the broad public with the interest/experience in development cooperation and not necessarily having an economic background. The selected research institutions will work in close collaboration with the Development Cooperation Attaché in the different Belgian Embassies, who will help provide the necessary guidance and contacts for the study.

2. A **summary paper reflecting the major findings and conclusions of the three country cases will be prepared jointly by the three universities** before the Convention and will be made available to the DGD. This summary paper will serve as a basis for reporting in Assises plenary on the ‘lessons learnt and recommendations’ from the case studies.

3. **During the Assises short presentations (15 minutes per country) will be made by the research teams** during each of the three parallel sessions. The audience will consist of the broad public working with or simply interested in development cooperation, and not necessarily having a background in economics. The presentations of the case studies should be geared to the audience.

4. The **researchers will facilitate the discussion of each of the country cases with the audience of the Assises** in three parallel working groups. The working groups will in particular discuss suggestions and recommendations for donor/Belgian Development Cooperation/development partner responses and approaches to the financial and economic crises impacts in the three partner countries.

5. When the Assises plenary re-convenes after the parallel sessions, the **facilitators will report on the discussion that took place in each of the working groups focusing on the ‘lessons learnt and recommendations’ from the country cases.**