



CHAD

SELECTED ISSUES

August 2016

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Approved By
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MACROFINANCIAL LINKAGES IN CHAD¹

Chad is at a critical juncture, as the sharp and persistent decline in international oil prices and regional security threats continue to severely affect the economy. The authorities' response included a large fiscal adjustment together with the mobilization of additional financing. Still, the government accrued a sizable amount of domestic payment arrears. In this context, and after overviewing the financial sector's structure in Chad, this chapter describes the key macro-financial linkages with a focus on (i) banks vulnerabilities associated to the decline in oil revenue and the sharp fiscal adjustment, and (ii) the consequences of the government's quest for additional financing. Finally, in light of the potential crowding-out of credit to the private sector, we analyze the recent trends on financial inclusion with a focus on microfinance.

A. Financial Sector Overview

1. Chad's financial sector is underdeveloped and dominated by a few commercial banks.

There are eight commercial banks,² with CFAF 1,034 billion in assets as of December 2015 (US\$1.8 billion, 16 percent of GDP), equivalent to 7 percent of CEMAC banks' assets, while Chad accounts for almost 15 percent of CEMAC's total GDP. The banking sector is concentrated, with three banks holding close of two thirds of total assets. The two largest banks are subsidiaries of foreign banks, while four other banks include state participation ranging from 20 to 62 percent of total equity. Banking intermediation is weak, with credit to the private sector limited to 8.4 percent of GDP in 2015, minimal interbank transactions, and no established secondary market for government debt.

2. Microfinance institutions (MFIs) are numerous but their activities are limited. Despite the presence of more than 100 MFIs operating in network, mostly in the form of cooperatives, access to financial services is limited and virtually non-existent in some rural areas. As of end-2015, the microfinance industry is estimated to have more than 200,000 beneficiaries, with a stock of credit of about CFAF 18 billion and CFAF 12 billion in savings (2.8 and 1.9 percent of GDP, respectively).

3. The rest of the financial system is composed by two small pension funds and three insurance companies. Pension funds exist only for the private sector (the pensions of civil servants are directly paid by the State budget) and their activities are extremely limited. It is estimated that less than 5 percent of all employees pay contributions to the National Social Insurance Fund (*Caisse Nationale de Prévoyance Sociale* - CNPS). In the same vein, the activity of insurance companies is small.

¹ Prepared by Gabriel Léost, Jephthe Nsumbu Kibidikila, and Alex Ho.

² Orabank Tchad, Société Générale du Tchad, Ecobank Tchad, Commercial Bank Tchad, Banque Agricole et Commerciale, Banque Commerciale du Chari, BSIC-Tchad, and United Bank for Africa Tchad (<https://www.beac.int/index.php/supervision-bancaire/lexique-des-banques-de-la-cemac>).

4. The financial sector remains relatively stable, but latest available financial soundness indicators suggest some deterioration within an increasingly challenging macroeconomic environment in Chad (see Table 1). The ratio of non-performing (NPL) to gross bank loans rose to 16.5 percent as of end-2015, a 5 percentage point increase from 2014. Returns on assets and on equity have also declined for two consecutive years. The capital adequacy ratio remained moderate at 14.6 percent as of end-2015 (compared to a regulatory target of 8 percent), but well below the peak of 22 percent in 2013. Liquidity ratios remained favorable, with liquid assets representing 142 percent of short-term liabilities (compared to a regulatory target of 75 percent). Going forward, with a dimmer domestic economic outlook, there are important risks to financial stability (see part B).

Table 1. Chad: Financial Soundness Indicators

	2010	2011	2012	2013	2014	2015
Capital Adequacy						
Regulatory capital / Risk-weighted assets	12.5	20.0	18.1	22.0	13.4	14.6
Asset Quality						
Gross nonperforming loans/Gross banking loans	9.9	7.6	7.4	9.8	11.7	16.5
Provisions / Nonperforming loans	81.1	89.0	64.5	65.3	68.3	56.1
Net nonperforming loans/Gross banking loans	1.9	0.8	2.6	3.4	3.7	7.3
Profitability						
Return on assets	3.2	2.1	2.0	2.3	1.8	1.6
Return on equity	32.0	19.2	15.5	21.1	19.4	13.1
Liquidity						
Liquid assets / Total assets	29.4	24.3	28.1	24.0	25.7	26.0
Liquid assets / Short term liabilities	148.3	149.3	146.6	139.3	152.9	142.1

Source: COBAC.

B. Key Macro-Financial Linkages in Chad

Macroeconomic Background

5. Since mid-2014, Chad is facing two massive external shocks. The persistent decline in oil prices has implied a massive reduction in fiscal oil revenues, expected to fall by almost 70 percent in nominal terms between 2014 and 2017. In addition, the security shock linked to regional conflicts (in particular Boko Haram activities) entails important economic and fiscal costs: security concerns directly affect some activities, a disrupt transportation systems and cross-border trade flows with Cameroon and Nigeria, and affects private investment. Direct fiscal costs are difficult to assess, but only the operations against Boko Haram have a cost estimated to be at least CFAF 10 billion (US\$ 16.5 million) per month, i.e., more than 2 percent of non-oil GDP in 2015.

6. In response to those shocks, the authorities have implemented a sizable fiscal adjustment and mobilized domestic and external (concessional) financing. Still, despite sizable support from BEAC (in the form of statutory and exceptional advances) and the international community, the continued fall in oil prices and lower than projected domestic bank financing led to

the accumulation of domestic payment arrears that could not be settled by the end of 2015. Those arrears complicated even further the prospects for 2016 and may strain the financial system.

7. Macroeconomic outcomes are being affected by the external shocks and the fiscal adjustment. The real non-oil GDP is estimated to have contracted by 2.9 percent in 2015 (compared to 7.1 percent growth in 2014), with economic sectors dependent on public expenditure particularly affected (e.g., construction contracted by an estimated 12.5 percent), and the economy remained sluggish in the first months of 2016.

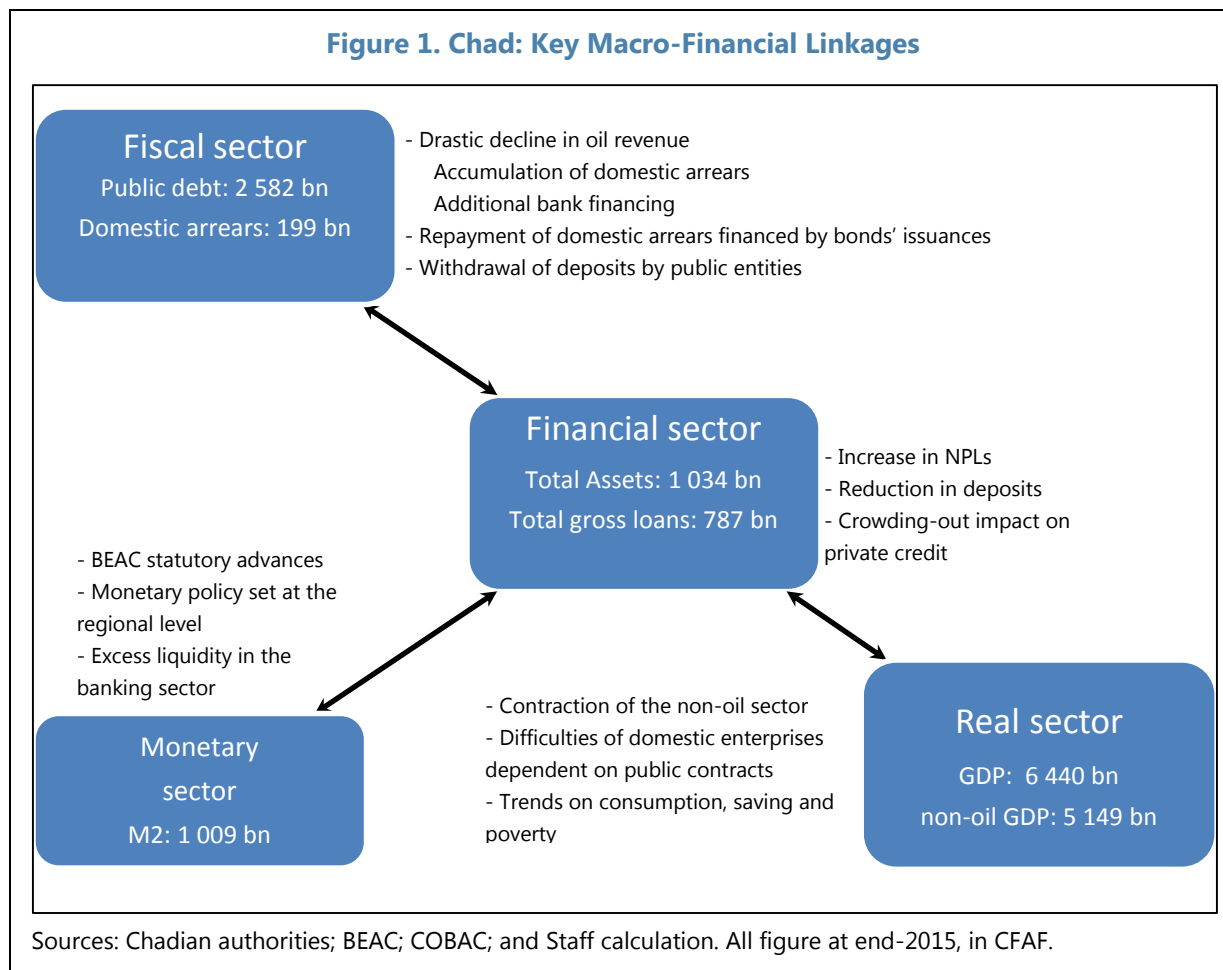
Macro-Financial Linkages in Chad

8. Macro-financial linkages in Chad are driven by a government sector that dominates economic activities in the more modern sectors of the economy thanks to oil-related revenues. Government spending has been a key source of economic growth in recent years, particularly in the urban centers that constitute the backbone of the Chadian financial system's development. Key economic actors (i.e., employees, companies, and even commercial banks) depend directly from government spending, be it in the form of wages, transfers and equity injections to (state-owned) companies, and contracts with private firms for the provision of goods and services and the construction of physical infrastructure. Under that setting, the fiscal, financial, and real sectors are closely inter-related and developments in any of them can be traced back (or forward) to developments in the other sectors. This framework is complicated further by the fact that Chad is a member of the Central Africa's currency union, with monetary policy and the regulation and supervision of the financial system set at the regional level.

9. In that context, the sharp fall in oil prices and its impact on public finances is an event with significant macro-financial implications for Chad. The fall in oil prices should negatively affect the oil companies' profitability, which in turn, could stress the firms and individuals providing services to them. In addition, it also forces the government to reduce spending and increase its financing needs, domestically and externally because oil related income is the government's main revenue source. Overall, economic activity is then being hit both by developments in the oil sector and also by the impact of the government's policy responses. The analysis that follows tries to put together the various transmission channels of the oil price shock (exacerbated by the deterioration in the regional security situation) to the financial system and the spillback to other sectors. In particular, it examines how recent fiscal developments can affect the stability of the financial sector, the margins of maneuver of banks to respond to the government's demand for additional domestic financing (including through a potential securitization of domestic arrears), and the crowding-out impact on private sector of this additional government financing.

10. The main macro-financial linkages are indirect through the associated sharp fiscal adjustment and the government's quest for additional financing (Figure 1). While the direct impact on banks of the oil price shock, through their exposure to oil companies and their suppliers, appears to be limited, the indirect impact of persistent low oil prices, through a contracting economic activity, appears to be sizable (paras. 11 and 12). The latter link mainly works through the banking sector's exposure to the public sector. First, the banks have significant credit and liquidity

exposure to the public sector (para. 13). In addition, the whole economy is highly dependent on public spending, with large cuts in public investment and consumption and the accumulation of domestic arrears leading to a deterioration of banks' loan portfolio (paras. 14 and 15). Finally, the government's need for additional domestic financing can place a burden on banks (para. 17) and lead to a crowding-out of credit to the private sector.

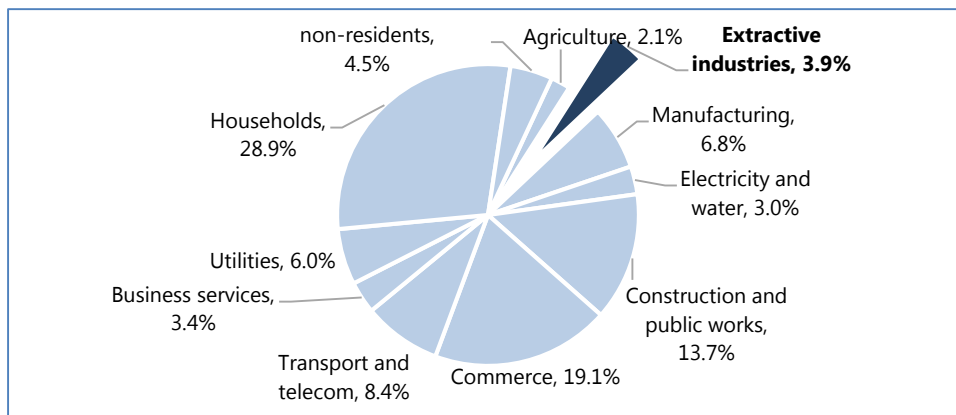


11. Direct credit risks linked to the oil sector appear limited. Oil companies operating in Chad are foreign-owned and rarely borrow from banks operating in Chad. At the end of 2015, the extractive industries' sector accounted for less than 4 percent of the Chadian banks' stock of loans to the private sector, and only one oil sector company was among the largest exposures of one of the Chadian commercial banks.

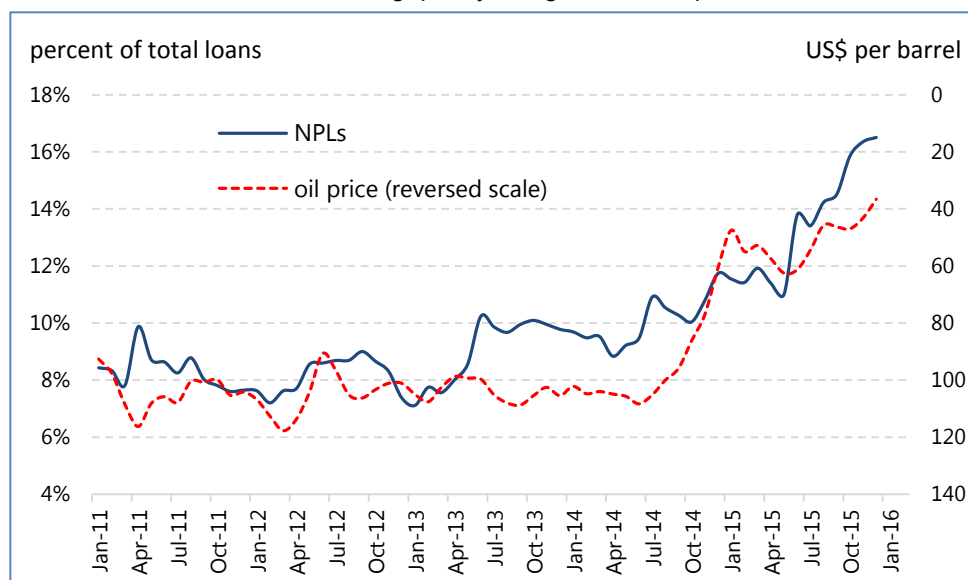
12. However, there seems to be a link between declining oil prices and deteriorating banking soundness indicators. With a prolonged period of low oil prices, financial stability risks are expected to increase as banks face a period of slow asset growth, weakening asset quality, declining profitability and capital erosion. In fact, there has been a rapid increase in banks' non-performing loans (NPLs) in Chad since mid-2014, from 9.5 percent of total banks' loans in June 2014 to 16.5 percent in December 2015.

Figure 2. Chad: Oil Prices and Health of the Banking Sector’s Loan Portfolio

While the banks’ direct exposure to the oil sector is low



...NPL's are increasing quickly along with the oil price fall.

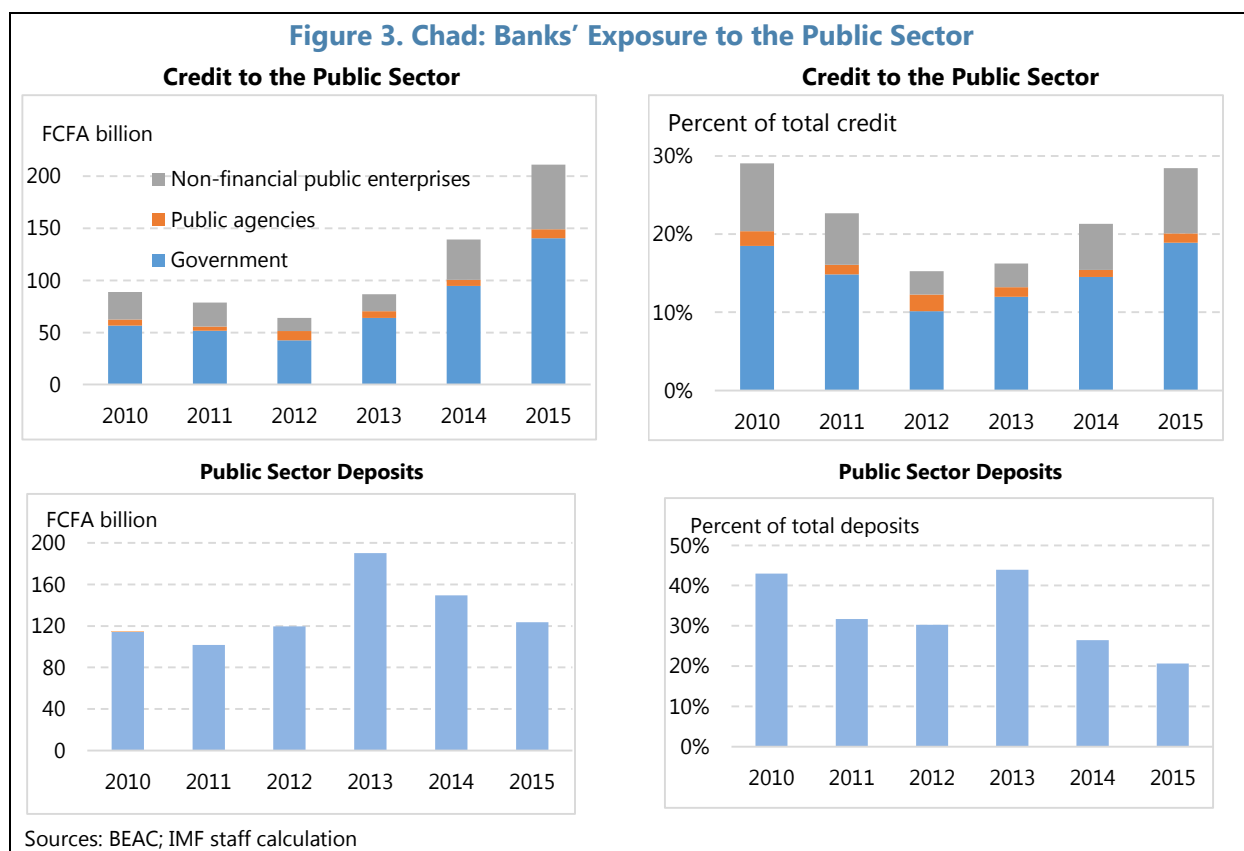


Sources: COBAC; WEO; and staff calculation.

13. Commercial banks have a significant credit and liquidity exposure to the public sector

(Figure 3). The central government, public agencies, and nonfinancial public enterprises accounted for about 28 percent of banks’ total credit as of December 2015 (CFAF 211.2 billion, i.e. US\$353 million or 4 percent of non-oil GDP). This increase in commercial banks’ credit exposure to the public sector could have been even stronger given government efforts to mobilize domestic financing in 2015. However, while the authorities issued a significant amount of securities in the regional bond market, a large part of its proceeds ended up in swaps against existing banks loans (para. 16). This would suggest that there was limited appetite or space for banks to expand its lending exposure to the government under the conditions prevailing in 2015. In terms of deposits at commercial banks, the public sector represented on average more than 30 percent of total deposits between 2008 and 2015, with a maximum of 44 percent in 2013. Since then, public sector deposits

have significantly decreased. At the end of 2015, at CFAF 124 billion (versus CFAF 149 billion at the end of 2014), they represented 20.6 percent of total deposits in commercial banks.

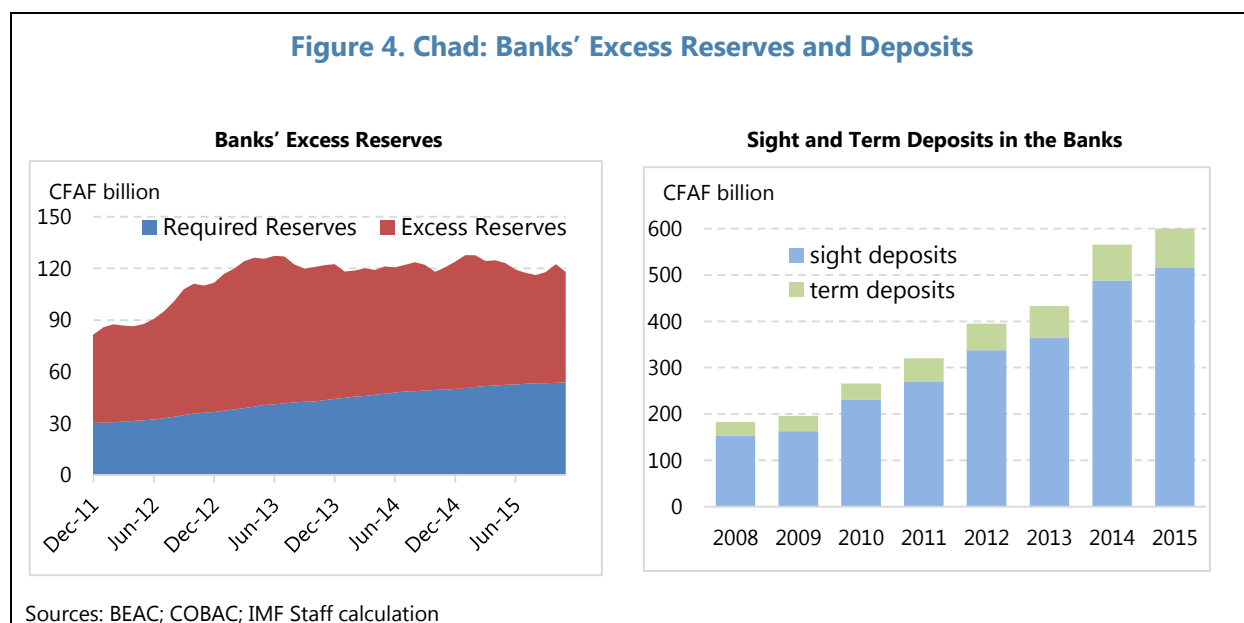


14. The current economic conditions negatively affect private companies dependent on public contracts (and, to a lesser degree, on the oil sector activity), potentially hitting the health of banks' loan portfolio. A significant share of private companies with access to the banking sector depend on public contracts. Their operations should be clearly affected by the 50 percent decline in public investment and outlays on goods and services in 2015 and 2016 relative to 2014 levels. In addition, oil companies have delayed some investments and significantly reduced their operational costs, which translates into fewer contracts awarded to local companies. The impact, however, is certainly more modest than that related to the decline of public contracts because oil companies mainly award contracts to foreign companies. In addition, the projected reduction in government transfers and subsidies over 2016-17 could negatively affect banks' credit portfolio to public corporations or decentralized entities.

15. The recent accumulation of domestic payment arrears brings about several risks to banks. In 2015, the government accrued a sizable amount of domestic payment arrears (around CFAF 148 billion or 3 percent of non-oil GDP, bringing their stock to CFAF 200 billion or 4 percent of non-oil GDP). Initially, companies awaiting the settlement of their bills by the government would have resorted to short-term bank financing, which would explain the fact that credit to the private sector was still growing significantly in the first half of 2015. By contrast, the accumulation of

domestic arrears would have been a factor behind the increase in banks' NPLs to 16.5 percent of total banks' loans as of end-2015. Aware of those problems, the government is implementing a plan to gradually clear its arrears as a way to give a breath of fresh air to the private sector and, consequently, limit the damage to banks' credit portfolio. However, the accumulation of domestic arrears also impacted many decentralized public entities (e.g., universities, hospitals), that have been forced to withdraw deposits (and have in some cases resorted to bank overdrafts) to maintain their operations in the face of a reduction and delays in government transfers, exacerbating thereby banks' resource constraints.

16. The short term-structure of their liabilities have forced banks to maintain high liquidity levels to mitigate risks (Figure 4). The proportion of sight deposits is particularly high in Chad (85 percent of total deposits, the highest ratio among CEMAC members), making banks particularly vulnerable to a withdrawal of deposits. In that context, the banking sector has remained relatively liquid with liquid assets representing 26 percent of total assets. Banks in Chad, as generally in the CEMAC region, have long been characterized by excess liquidity. At end-2015, banks' excess reserves exceeded CFAF 64 billion or 6.2 percent of their total assets.³ On the other hand, the reduction of liquidity risks translates into reduced "transformation of maturities" (a key contribution of banks to economic development) and the provision of credit only at short-term. Short-term loans represented 75 percent of total commercial banks' loans at the end of 2015.

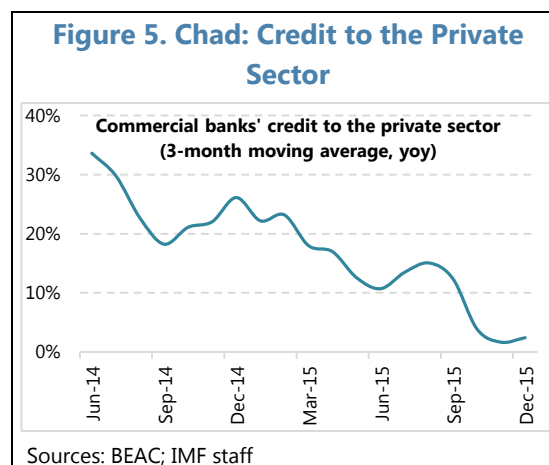


17. The government's needs for additional domestic financing, including to repay part of the stock of domestic arrears, can place a burden on banks, despite recent measures of the BEAC to strengthen their liquidity position.

³ Before the decision from the BEAC's monetary policy committee, on April 6 2016, to lower by 50 percent the reserves requirement for CEMAC's commercial banks.

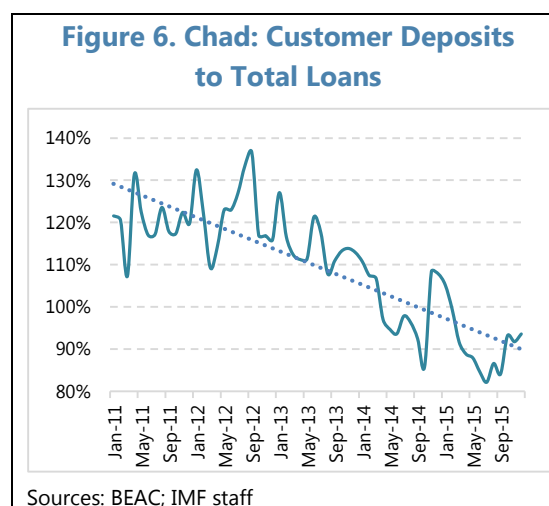
- **Direct monetary financing from the BEAC, widely used in 2015, should no longer be an option in 2016.** In 2015, Chad benefitted from statutory and exceptional advances (on the basis of the security challenges faced by the country) for a total of CFAF 232 billion. Additional direct monetary financing is unlikely in 2016, as it would require changing again the ceiling on such advances, already reached by Chad. In addition, it is not advisable, as further direct monetary financing could compromise the stability of the common currency.
- **The authorities intend to continue to resort to public securities' issuances in the regional market.** Chad successfully increased its public security issuances in the CEMAC regional market in 2015, with net issuances of Treasury bills and bonds of CFAF 190 billion. However, several of those issuances were used to swap against existing banks' direct loans, leading to a principal repayment of the domestic debt of CFAF 234 billion in 2015 (compared to only CFAF 80 billion in 2014). The main benefit of the increased use of Treasury bills and bonds for commercial banks is in terms of increased liquidity of their claims given that they can be rediscounted at the Central Bank. For 2016, the authorities intend to issue Treasury bills and bonds for a net amount of at least CFAF 150 billion (2.5 percent of non-oil GDP). This appears ambitious given developments in 2015.
- **This program of issuance includes an operation of repayment of domestic arrears that can restraint the banks' margins of maneuver for other financing.** As part of their strategy to clear domestic arrears, the authorities issued two Treasury bonds at the end of March 2016, for a total amount of CFAF 65 billion, which proceeds will be used to repay part of the accumulated domestic arrears. This operation benefits the agent banks in two ways: directly as the operation includes a discount of 7 percent on the arrears' claims to be kept by the bank involved in the operation, and indirectly as the clearance of domestic arrears would improve financial conditions of enterprises repaid, therefore improving the banks' credit portfolio. That said, funding for this operation competes with the ordinary financing of the 2016 budget, a reason why additional similar operations should be considered with extreme caution.
- **Recent decisions at the regional level could help the authorities to meet their financing objectives.** The monetary policy committee of the BEAC took two decisions late March and early April 2016. The first one was to raise the ceiling for Chadian commercial banks' refinancing at the BEAC from CFAF 200 billion to CFAF 300 billion, which should amplify their rediscount operations and provide them with more liquidity buffers. The second one was halving of required reserves at the central banks, which immediately translated into around CFAF 25 billion in additional liquidity for Chadian commercial banks.
- **In addition, the ability of banks to respond positively to the offer of Chad's public securities shall be estimated at the regional level.** Only half of the stock of Chadian public securities issued in the regional market is held by domestic banks, the other half being held by banks in other CEMAC countries (mainly in Cameroon). Therefore, the BEAC decisions in terms of monetary easing also impact Cameroonian or Gabonese banks that tend to purchase Chadian government securities. That said, non-Chadian banks holding securities are branches of regional banks, and decisions taken at the banks' headquarters can put added pressure on local banks to satisfy the Chadian government's financing needs.

18. Additional public sector financing could also lead to a crowding-out of bank credit to the private sector. The authorities' quest for additional financing can create competition with the private sector, reinforcing the difficulty of private companies to access to commercial banks' loans, with knock-on impacts on non-oil growth and even on banks' NPL ratios. While short-term credit lines have for now prevented credit to the private sector's growth to fall into negative territory, there is clear evidence of a credit slowdown since mid-2014 (Fig. 5).



Summary of the Risks for the Banking Sector

19. The composition of commercial banks' assets and liabilities is experiencing significant changes that can make them vulnerable. Recent developments related to the macro-financial linkages described above might jeopardize, if they get worse, the traditional key strengths of Chadian commercial banks, which are a deposit-based funding model and high liquidity buffers. For instance, the deposit intermediation level remains prudent with a deposits-to-loans ratio of 94 percent in December 2015, but is declining (Fig. 6). There might be an increasing risk of maturity mismatches between short-term deposits and banks' assets, reinforced by the growing role played by Treasury bonds, as these securities have an average maturity close to 3 years.



20. Recent stress tests show that further increases in NPLs or declines in deposits could have a significant impact on the ability of some banks to comply with the regulatory solvency and liquidity ratios (Box. 1). In the context of regional discussions with the CEMAC, stress tests were carried out in early 2016 on the basis of information provided by the COBAC. Their results show that if NPLs were to reach 20 percent of total loans, some commercial banks would not meet anymore the minimum risk-weighted capital adequacy ratio, especially banks with capital originating in CEMAC countries. In the same vein, a further 25 percent decline in total deposits at commercial banks (for instance with a 50 percent decline in government deposits combined with a 20 percent decline in deposits from non-financial enterprises) would bring most of the Chadian banks below the regulatory liquidity ratio.

21. In this context, a close monitoring of the banking system is warranted. The authorities need, in coordination with the regional regulator, to closely monitor the health of the banking

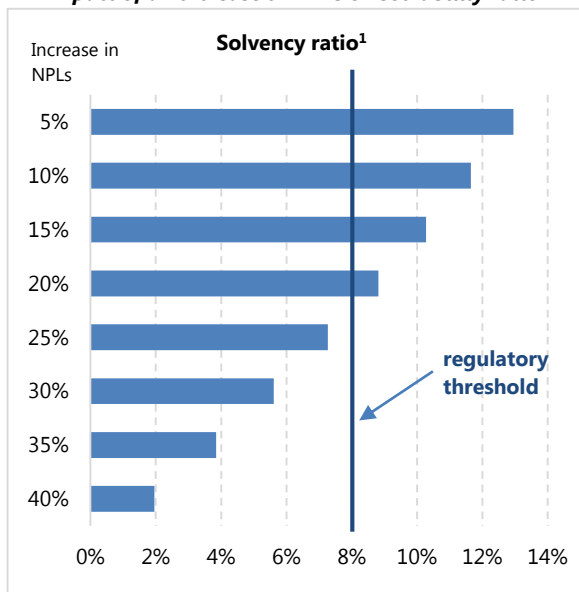
system to minimize potential fiscal costs, including through potential recapitalizations of government-owned banks.

Box 1. Chad: Stress Tests on Commercial Banks

Stress tests were run by IMF staff in the context of the regional consultations with the CEMAC. For the Chadian banking sector as a whole, main vulnerabilities stem from the indirect impact of oil price shock to the real economy, through the risk that government payment delays and arrears pose to economic sectors (like construction) largely dependent from public contracts:

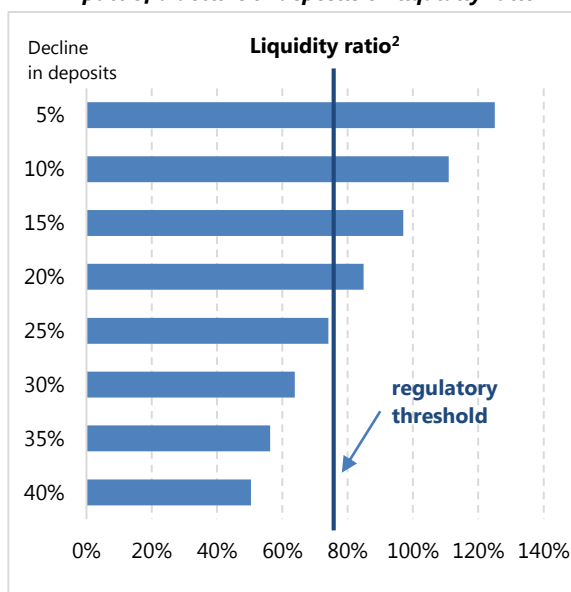
- A further increase in NPLs would deteriorate the solvency ratio, which stood at 14.6 percent at the end of 2015. If NPLs increase by 25 percent, leading them to more than 20 percent of total loans, the solvability ratio would be under its regulatory threshold of 8 percent.
- A decline in deposits at commercial banks would deteriorate the liquidity ratio, which remained at a comfortable level at the end of 2015 (142 percent compared to a regulatory threshold of 75 percent). An important decline in deposits (by 25 percent) would be necessary to see the liquidity ratio under its regulatory threshold. It would suppose, for instance, a decline by 50 percent on public deposits, combined with a decline by 20 percent from non-financial companies.

Impact of an increase in NPLs on solvency ratio



¹Ratio of regulatory capital to risk-weighted assets

Impact of a decline in deposits on liquidity ratio



²Ratio of liquid assets to short term liabilities

Sources: COBAC; IMF staff

C. Financial Inclusion and Microfinance

22. A deeper and more inclusive financial sector could help reduce poverty and improve growth in Chad. Financial inclusion, which means an expansion of access to financial services by households and firms, can lower poverty by reducing credit constraints on the poor and help small firms and entrepreneurs to do business. As shown by Sahay et al (2015), household’s access to

finance has a strong positive relationship with economic growth in general. In particular, they found that higher density of ATM and bank branches has a monotonic positive relationship with economic growth.

23. This section gives an overview of financial inclusion in Chad and discusses policies to promote financial inclusion. Similar to other studies along these lines, the analysis uses mainly 2014 data from IMF's financial access survey (FAS) and the World Bank's Global Findex⁴ (Findex) on financial inclusion.

24. Similar to other SSA countries, underdevelopment of financial services and lagging financial inclusion are chronic problems in Chad. As showed in Alter and Yontcheva (2015), the "financial development gap," which is the ratio between the benchmark and actual private credit to GDP level, was nearly 3 percent in Chad in 2012, compared to 1.7 percent in SSA which is already considered as a large deficiency gap. Even by other metrics to be discussed below, Chad is still lagging behind its peer countries.

Overview of Financial Inclusion in Chad with a Cross-Country Perspective

25. The use of financial services by households has expanded somewhat over the years along with the expansion of commercial banks' physical presence. The geographic expansion of the banking sector in recent years has been significant. The number of branches of the eight commercial banks in Chad doubled between 2004 and 2014 to reach 58. In the same vein, the number of Automated Teller Machines (ATMs) significantly increased in recent years. Together with improvements in the physical presence of banking facilities, the use of financial services also increased remarkably—the number of households' deposit and loan accounts increased in the last decade to 23.82 and 10.93 per 1,000 adults in 2014, respectively. Consequently, households' access to basic financial services has been improving, with the size of households' deposits increasing to 4.1 percent of GDP, and outstanding loans from commercial banks to households reaching 2.3 percent of GDP.

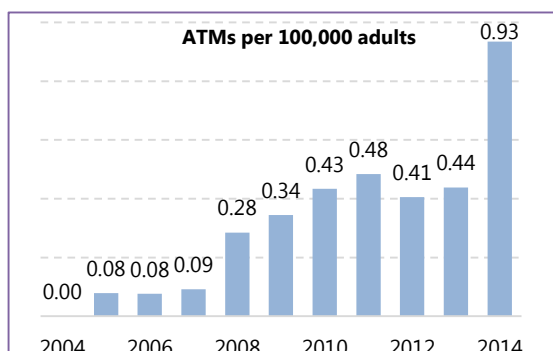
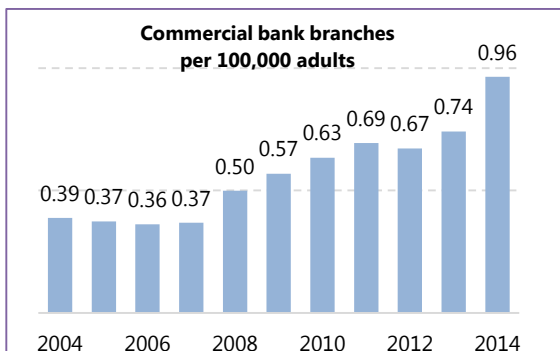
26. Despite this progress, financial inclusion in Chad remains limited and lagging behind its peers. According to Findex, Chadian households' access to basic services in the formal financial sector lags even relative to its CEMAC peers.⁵ In 2014, only 12 percent of adults reported to have an account in Chad and only 7 percent to have an account with a financial institution. In comparison, almost 35 percent of the adult population in Sub-Saharan Africa (SSA) reported to have an account in 2014, with nearly 30 percent having an account with a financial institution.

⁴ Global Findex database is a comprehensive database on financial inclusion, based on interviews with about 150,000 adults in over 140 countries.

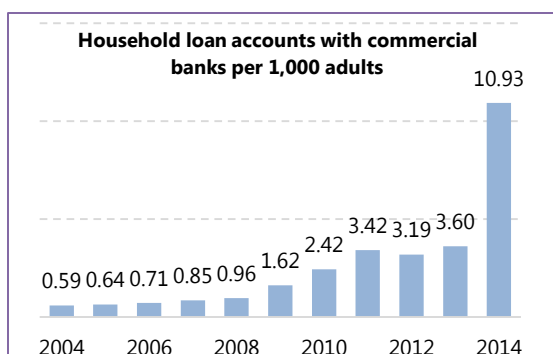
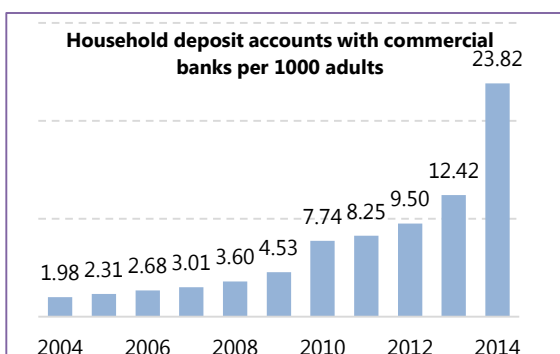
⁵ CEMAC countries include Cameroon (CMR), Central African Republic (CAF), Chad (TCD), Gabon (GAB), Republic of the Congo (COG) and Equatorial Guinea. However, data are not available for Equatorial Guinea in Findex.

Figure 7: Chad - Households' Financial Access

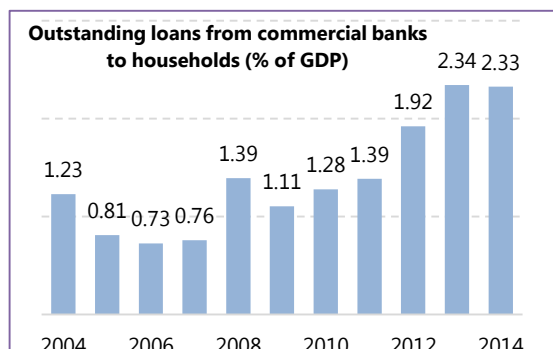
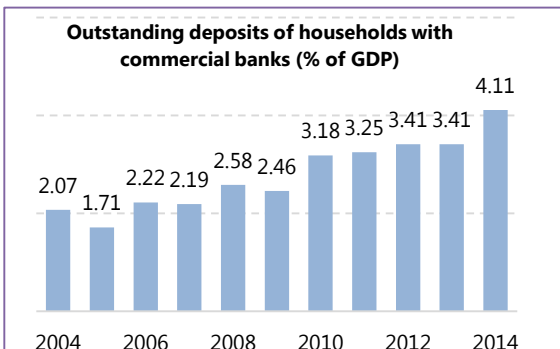
Banks are becoming more accessible over the years.



Improvement in the access to banks' branches translates into a significant increase in the use of banking services.



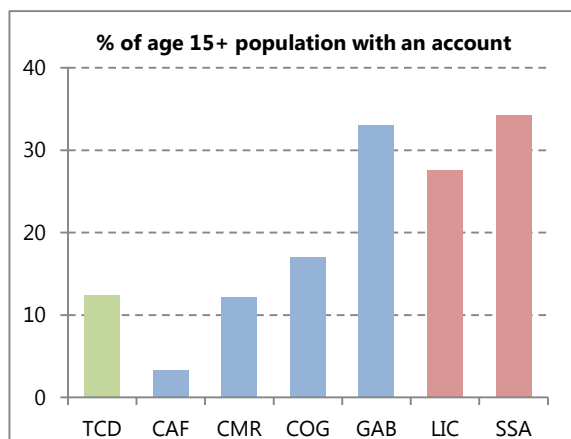
This improvement is shown by the increase in households' deposits and loans.



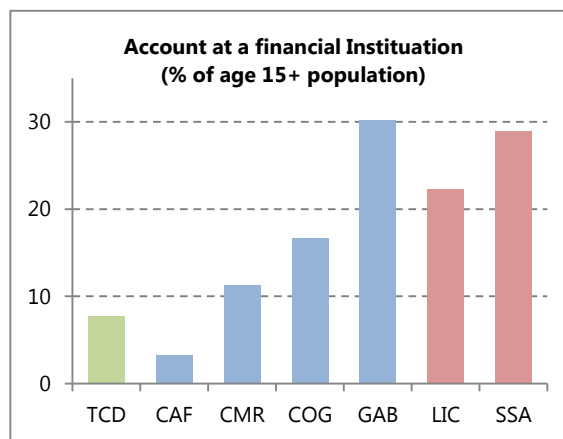
Source: Financial Survey Access, IMF

Figure 8.Chad: A Cross-Country View of Financial Inclusion

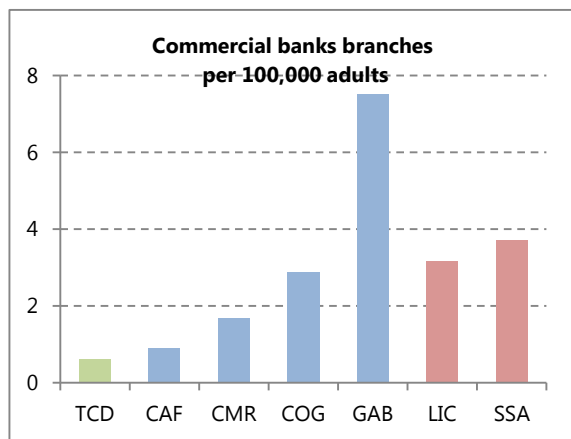
Financial inclusion in Chad is still lagging behind peers...



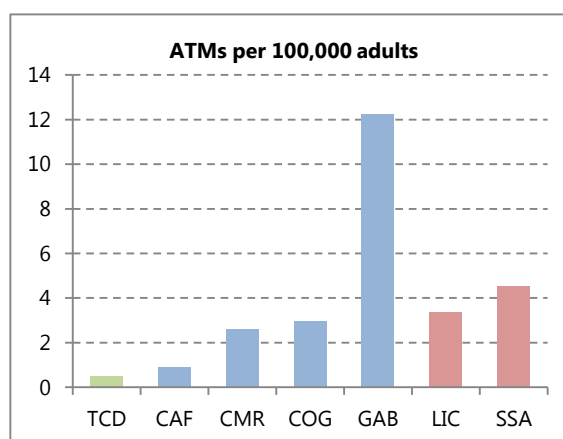
...especially in terms of using the formal financial sector.



Despite the expansion of banking facilities...



...financial access in Chad remains behind its peers.

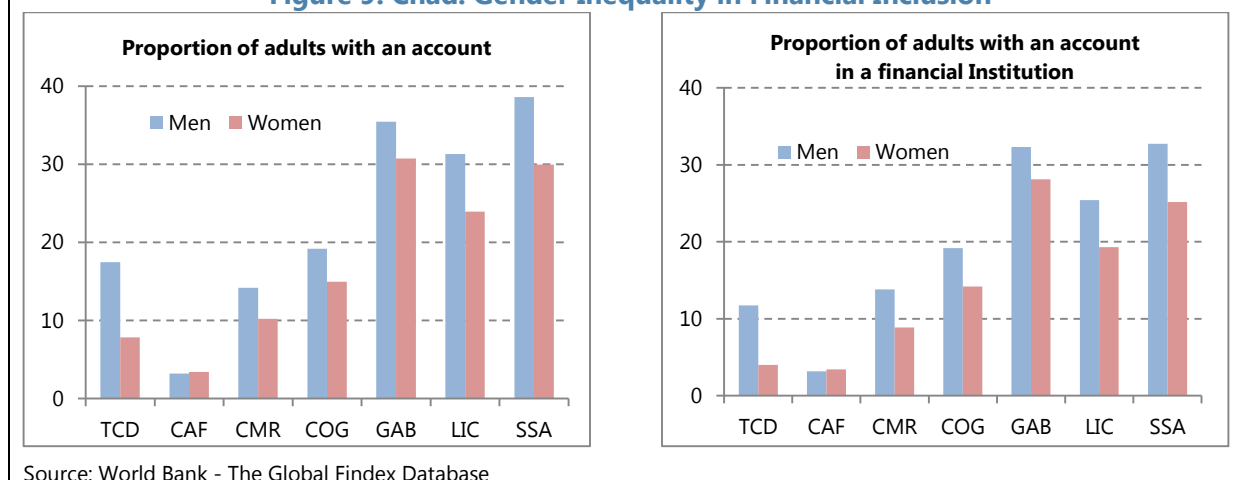


Source: World Bank - The Global Findex Database

27. Gender inequality in access to financial services in Chad is severe and worse than in most of its peers. Women in Chad have considerably less access to basic financial services. Only 8 percent of adult women have an account (only 4 percent in a financial institution) compared to 18 percent of adult men (and about 12 percent in a financial institution). The degree of gender inequality in financial inclusion in Chad is similar to most of its CEMAC peers, but worse than the average for LICs and SSA countries. As argued in Sahay et al. (2015), closing gender gaps in account usage and promoting diversity in the depositor base would help to improve growth without impairing financial stability.

28. The low utilization of financial services in Chad prevails across all demographic groups. Findex shows that adults belonging to the poorest 40 percent, young adults (between 15 and 24 years old), and adults living in rural areas have lower financial access than the adult population in general (in terms of having an account). Once again, all these demographic groups have lower financial access in Chad than in other CEMAC countries, or more generally in other SSA countries.

Figure 9. Chad: Gender Inequality in Financial Inclusion



The Use of Financial Services

29. Low levels of financial access and the lack of development of the financial system are reflected in the main payment methods used in Chad. Most payments are done in cash. The use of more advanced payments methods (checks, electronic payments, debit/credit cards) remains unusual. For instance, in 2014, only 2.8 percent of the population aged 15 years and over had a debit card (compared to 17.9 percent on average in SSA countries) and only 0.5 percent of the population used it to make payments (8.7 percent on average in SSA countries).

30. Underdeveloped financial markets limit the access to the formal sector despite appetite for financial services. Nearly 41 percent of adults in Chad reported to have borrowed any money in 2013 according to Findex, but less than 3 percent borrowed from a financial institution. As expected, the poor face the greatest difficulties in accessing credit. Nearly 27 percent of the poorest said it is not at all possible to come up with emergency funds. On the other hand, almost half of the adults in Chad have saved money in the past year, which is relatively close to the average for SSA countries (59.6 percent). However, only 4.6 percent declared having saved at a financial institution, in contrast with 15.9 percent on average in SSA countries.

Mobile Banking in Chad

31. Increasing mobile phone penetration in Africa in recent years led to rapid development of mobile banking in the continent. Mobile banking complements the traditional form of financial services and allows households and businesses to perform certain transactions, such as making transfers or paying bills, without access to physical banking facilities, which is generally scarce in CEMAC countries. Due to the higher coverage of mobile phone services in the population, mobile banking is now considered as a way to improve financial inclusion.

32. As of 2014, Chad has higher percentage of adults reporting to have a mobile account than its CEMAC peers. According to Findex, about 5.7 percent of adults in Chad reported to have a mobile account in 2014, which is the second-highest among CEMAC countries (just behind Gabon

with 6.6 percent of adults having a mobile account). Nevertheless, this ratio remains significantly lower than the 10 percent and 11.5 percent, respectively, observed on average in LICs and SSA countries.

Microfinancial Institutions in Chad

33. Microfinance institutions started to develop in Chad in the 1980s and 1990s, a period of growing interest in microfinance as a tool for mobilizing local savings, and financing business activities especially in rural areas. According to the Central African Banking Commission (COBAC), Chad had more than 200 MFIs by end-2004. While MFIs were first operated informally, a CEMAC regulatory framework on microfinance was adopted in 2012. Under this regulatory framework, the MFIs need to hold a valid license to operate; they must join the country's professional MFI association; and the COBAC is responsible for regulating and sanctioning MFIs. Implementation of those regulations led to a decline in the number of MFIs, accentuated in 2014 when the unit in charge of microfinance at the COBAC was reinforced and took more decisive administrative actions.

34. The development of the microfinance sector has had a positive, albeit limited, impact on financial inclusion. Despite the recent decline in the number of MFIs in Chad, the number of beneficiaries continued to increase and is now above 200,000 people. Along with the expansion of the client base, the amount of outstanding savings, loans and transfers handled by MFIs also increased significantly. That said, the share of MFIs in the financial market is still limited. At the end of 2015, deposit at MFIs represented only 1.6 percent of total deposits in the financial system while the loans made by MFIs accounted for only 2.3 percent of the total loans by the financial system.

35. MFIs have been innovative in establishing credit tailored to borrowers' specific circumstances. The loans offered by MFIs in Chad comprise commercial loans, targeted to people establishing new activities, construction/housing loans, agricultural loans, and educational and social loans. The MFIs accept different kinds of collaterals, including cattle, land, or equipment. Lending rates are generally at a minimum of 2 percent per month, significantly above the 8-15 percent per year offered by commercial banks.

36. The contribution of MFIs to greater financial access and inclusion may be limited by their geographic concentration. Ideally, MFIs should be located in areas where the presence of banks is limited, where they can substitute their activities and thereby improve the access to financial services. Despite the efforts of international development partners, the microfinance sector expansion has been unevenly distributed throughout the country, with the majority of the MFIs remaining located in the central and southern regions, where the banks' presence is the heaviest.

Table 2. Chad's MFI Sector

Period	MFI (number)	Clients (number)	Employees (number)	Outstanding savings (CFAF billion)	Outstanding loans (CFAF billion)
2000	76	31,300		0.61	1.38
2004	214	97,318		4.42	3.67
2013	170	190,109	880	8.51	10.64
2014	113	197,262	900	10.29	16.04
2015e	--	>200,000--	--	12.00	18.00

Sources: COBAC; professional microfinance association; and Ministry of Finance and Budget

37. Poor performance of MFIs also limits their ability to expand their services and coverage in Chad. MFIs management and financial performance remains weak. Most MFIs have poor management procedures, high administrative costs, and poor internal controls mechanisms. The existence of some MFIs relies on subsidies from foreign partners, and they often have a weak business model to sustain their operations. The lack of risk management procedures can also send some MFIs into distress.

Policy Steps to Improve Financial Inclusion

38. The Chadian authorities recognize the importance of MFIs but the government has mobilized only limited resources in support of the sector. Successive National Development Plans made the microfinance sector a priority, as a tool for economic development and poverty reduction. A specific Ministry in charge of microfinance was created in 2006, but was replaced in 2014 by a technical unit part of the Ministry of Finance and Budget. The resources allocated to this unit are low, and most of the support to the sector is through agreements with development partners, as for instance the Support Program for Inclusive Finance of Chad financed by the Chadian government and the UNDP, or the Microfinance Project in Chad co-funded by the government of Chad and the Islamic Development Bank.

39. Drawing experience from countries in the region, the first key step to increase financial inclusion is to develop appropriate legal, regulatory, and institutional frameworks and a supporting information environment. Even if its direct support to the microfinance sector is limited, the government has a central role to play in dismantling obstacles to financial inclusion by introducing laws that protect property or creditor rights, and by ensuring that these laws are enforced. It can also set standards for disclosure and transparency and promote credit information-sharing systems and collateral registries. More fundamentally, it has a role in educating and protecting consumers. The government could also consider policies such as granting exemptions from onerous documentation requirements, allowing correspondent banking, and shifting to the use of electronic payments into bank accounts for government payments. By moving forward with these policy measures, the authorities can generate significant progress in increasing financial inclusion, reducing inequality, and boosting growth.

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