Djibouti's financial sector

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The financial sector of the Republic of Djibouti has grown dramatically in recent years, a process that began in the early 2000s, and that was in large part prompted by an explosion the number of exchange agencies and remittances throughout the country.

Growth in the banking sector began in the middle of the decade, paralleled by an expansion of the microfinance sector. Microfinance is a growing field in Djibouti, but access to finance remains limited for micro and small enterprises, reducing the potential for self-employment. Currently, only 4 percent of the population benefits from microcredit. In the coming years, microfinance institutions are expected to develop a range of new services including micro-insurance and micro-transfers. Authorities are also working closely with banks to address these issues and further expand their range of financial products and services (such as automated teller machines, Islamic products, and products for small and medium-size enterprises). The area of micro-finance has, for its part, three savings banks with service points located throughout the country.

Djibouti's banking sector, which features both Islamic and conventional banks, has grown significantly in recent years with the arrival of new banks bringing the number of institutions to eleven, compared with only two in 2006. The sector remains highly profitable with low level of non-performing loans (approximately 6 percent). The banking sector accounts for 97 per cent of financial assets and 10 per cent of GDP, and is a showcase for Djibouti, and enjoys a solid reputation in the region.

In addition to the intrinsic characteristics of expertise, professionalism, and experience inherent in each bank that has contributed to this reputation, the whole profession and hence the financial sector has benefited from the solid foundations provided by the country's monetary system.

The Republic of Djibouti today can thus boast of having a healthy and reliable banking centre fully connected to the international banking sphere, and able to provide all banking services, both locally and internationally via a large network of foreign correspondents.

The Djiboutian financial sector, with total assets of 265 billion FD or 102 per cent of GDP, has not been affected by the international financial crisis. Banking is entirely under the supervision of the Central Bank of Djibouti, while the capital of local banks is majority owned by foreign groups. The insurance sector, regulated by the Ministry of Finance, consists of two large corporations.

A favourable environment overall

Political stability
Since independence, the Republic of Djibouti has been considered an oasis of peace and a model of political stability in a region, the Horn of Africa, which is buffeted by incessant conflicts.

Macroeconomic stability
The growth of the Djiboutian economy has accelerated substantially in recent years, while macroeconomic stability has been maintained despite adverse external shocks. GDP growth has increased from 2.4 per cent in 2001-2005 to nearly 5 per cent over the period 2006-2013. Inflation remains under control at an annualized rate of around 2 to 3 per cent in recent years.

The emergence of Djibouti as a regional logistics hub with strong development of port activities, as well as in the field of construction and tourism has been accompanied by a large influx of foreign direct investment. Between 2006 and 2013, cumulative FDI amounted to $1.274 billion, against only $12 million between 2001 and 2005. The share of FDI in GDP is estimated at 19.6 per cent in 2013.

Other competitive advantages
Among the factors helping to make Djibouti the regional financial centre of choice are:

- The availability of the most efficient communications infrastructure in Africa (latest generation fibre optic submarine cable);
- The absence of all restrictions on capital movements (free repatriation of profits, absence of exchange controls)
- A tax incentive framework (investment code, no tax on bank transactions and / or financial products).

The financial landscape also includes a large network of branches of foreign exchange and money transfer agencies, with 17 agencies approved by the Central Bank of Djibouti.

Djibouti features no active capital markets or fixed income markets. As of March 2013, the country received no sovereign rating from any of the three major credit rating agencies. The national pension system, based on a pay-as-you-go system, is comprised of 3 pension funds: one for civil servants, one for retired military personnel, and one covering employees from the private sector and public enterprises.

A complete overhaul of banking regulations, carried out in 2000, 2005, and most recently in 2011 modernised the financial sector, which now meets national and international standards in relation to capital ratios, risk management, the fight against money laundering and the financing of terrorism, Islamic finance, etc.,), all of which has helped consolidate the credibility of the Central Bank and the return to sustainable development within the banking sector.

Djibouti's banking sector is liquid, profitable, and generally well capitalised. Recent evaluations of the sector conducted by a joint team of the IMF and the World Bank show that the banking sector is generally solid, with a solvency ratio above 10 per cent. The rate of bad loans has continued to decline over the last five years while the provisioning rate was increased up to 67 per cent.

Between 2008 and 2009 commercial bank deposits increased by 19.3 per cent to reach FDJ 183.9 billion, while sight deposits rose by 34.8 per cent and bank balance sheets improved by 20.7 per cent. However, weak enforcement of creditor rights and the absence of comprehensive information on borrowers keep lending risks high. Bank lending has increased in recent years but still remains fairly limited, with the ratio of bank credit to bank deposits rising from 29.5 percent in 2006 to 37 percent in 2008 and 41.6 percent in 2009.

It should also be noted that in recent years banks have played a key role in providing the necessary impetus to economic growth and support the emergence of a truly dynamic private sector and provide jobs in very large numbers.

An IMF analysis of the financial sector estimates that systemic risk is low. However, the authorities have, under the aegis of the IMF, initiated reforms to strengthen banking supervision and regulation. The aim is to prevent the risk of money laundering or terrorist financing. There are also plans to raise the minimum capital required for opening a bank and reduce the granting of licenses in an effort to sustainably regulate the sector's expansion.

Foreign investors benefit from a favourable tax environment created by the tax exemption policy of the investment code and the free trade zones. Tax exemptions are expected to be streamlined in the coming years without, however, withdrawing the exemptions previously granted.

SMEs/SMIs receive only 5 per cent of the funds allocated to enterprises despite the project opportunities available to banks. This is due to the banks' aversion to risks and the difficulty of calling up security in the event of a default.

The adoption of a policy to facilitate access by enterprises to domestic credit would leverage their growth and the employment-generating potential of SMEs/SMIs. F

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The monetary system in Djibouti

Djibouti's exchange rate is pegged to the US dollar under the currency-board regime at DJF 177.721 (Djibouti franc) since 1973, and no change is expected in the short or medium term. The government ensures parity by maintaining 105% coverage in foreign exchange of currency in circulation. This regime does not allow for a monetary or exchange policy, but since 2010, the authorities have been considering introduction of a banking reserve requirement as a way to manage liquidity though the rate has not yet been set. Despite its limits, the currency-board regime has provided monetary stability and also given the country a chance to become a regional financial centre thanks to free movement of capital and free conversion of the Djibouti franc into all currencies.

Inflation remains sensitive to rising prices of food and oil products. Despite the acceleration in 2010, inflation has remained under control at an annual price increase rate of 3.9 per cent, mainly driven by rising food prices. The government intends to maintain its policy of subsidising food and oil prices to mitigate the impacts of an increase in prices.

Foreign-exchange reserves continue to rise, reaching $243 million at the end of 2012 (up from $228 million year-on-year).

The lack of discretionary monetary policy and the inability of the Central Bank to act as lender of last resort towards the banking sector are the disadvantages of the monetary system. Monetary policy boils down to careful management of reserve assets. The banking system also implies effective banking supervision.

The stability of the monetary system over time has allowed for the emergence of a sound and secure financial marketplace. F