The Rwanda Economic Update: Financing Development

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The Role of Deeper and More Diversified Financial Sector
In the new Rwanda Economic Update (REU) launched today, the World Bank projects an economic growth rate of 7.4% in 2015 and 7.6% in 2016. With the projected growth rates, the World Bank projects Rwandas poverty rate to decline from 63% in 2011 to 54% in 2016, thus moving approximately one million people above the poverty rate.
Rwandas growth rate recovered from 4.7% in 2013, the lowest growth since 2003, to 7.0% in 2014, the report says. Private and government consumptions led the recovery, which is reflected in the accelerated growth of the services sector. However, fiscal policy has become less expansionary in recent quarters. On the other hand, developments of the monetary sector have been supportive to the economy. Bank lending has recovered to the pre-aid shortfall level. "Low inflation rate and appreciation of real effective exchange rate (i.e., exchange rate adjusted by inflation and relative importance of trading partners by trade values) is favorable for the accommodative monetary policy to support the economy through financing" says Yoichiro Ishihara, Senior Economist and Task Team Leader of the report.
Analyzing the possible impacts of the oil price decline on Rwandas economy, the report observed positive impacts in both inflation and imports. Transportation prices (including gasoline) declined by about 4%, which brought down the overall Consumer Price Index (CPI). On energy imports, prices started to significantly decline in November 2014, resulting in energy import values drop of 20-40% until April 2015.
According to the report, for Rwanda to achieve high and sustainable growth, the medium term investment is critical. Although Rwandas GDP investment of 24% is slightly higher than the average of low/medium income countries, it is still mostly financed by foreign savings, including aid. Increasing domestic savings in the next several years is difficult. It is therefore imperative to find alternative domestic and external financing sources. "Workers remittance and foreign direct investment are potential sources, as they have steadily increased without significant volatilities in the past several years" says Carolyn Turk, Country Manager for Rwanda.
The development of the financial sector in Rwanda is essential in financing development, for two reasons. First, the financial sector contributes to economic growth and government revenues and supports the mobilization of domestic savings, especially through improving access to finance in the medium to long-term. Second, the financial sector facilitates domestic and foreign debt financing and investments and access to international capital markets.
While commercial banks are still the most important source of financing in Rwanda, their investments are constrained by the maturity of their liabilities, which consist mainly of local short-term deposits. "As the banking sector has limited capacity to provide long-term financing, domestic, regional, and international institutional investors, such as pension and insurance funds, are natural candidates for investing in long-term projects" says Gunhild Berg, Financial Sector Specialist.

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