opinion

Growth, debt and Trump: key economic trends in Africa to watch in 2017

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In 2016, real GDP growth in sub-Saharan Africa is estimated to have been the weakest since the 2008-09 global financial crisis. This was largely because of the weak performance in its two largest economies, South Africa and Nigeria, which together make up about half of sub-Saharan Africa's GDP.

Although oil and mining economies were hurt by the commodity slowdown, much of East Africa as well as oil-importing Francophone economies such as Côte d'Ivoire and Senegal managed robust rates of growth of above 6%. The slowdown in Africa was not uniform.

But what are the prospects for African economies in 2017?

Hopes for faster growth rest on prospects in the region's two largest economies.

In South Africa, recovery after a severe drought in 2016 and improved electricity generation should provide a modest lift. But private sector confidence remains weak, and rising debt levels mean that South Africa remains at risk of losing its investment grade credit rating. With little room to scale up public investment, a tepid recovery is likely, at best. Faster growth will be needed to contain rising public debt. South Africa faces its next round of rating reviews in June, but it will be difficult to achieve anything meaningful by then.

In Nigeria, following a probable contraction of GDP in 2016, it will not take much to drive growth to positive levels in 2017. But higher oil prices alone – we forecast an average of $66/barrel in 2017 – are no panacea. Oil output and Nigeria's ability to curb militancy in the Niger Delta will also matter.

Even more important are prospects in the non-oil economy, which makes up 92% of Nigeria's GDP. Activity in the non-oil sector has been sluggish, hampered by poor policy choices, in particular a poorly-functioning foreign exchange market. Despite several flawed attempts at currency flexibility, Nigeria has never fully embraced a liberalised foreign exchange regime. The authorities are uncomfortable with allowing demand and supply to determine the value of the Nigerian naira. Because Nigeria has low levels of accumulated oil savings and its foreign exchange reserves have come under pressure, it has had to resort to curbing import demand in order to maintain a steady foreign exchange rate. However, squeezing import demand has meant maintaining a severe squeeze on the real economy. Growth prospects will depend on how quickly unsustainable foreign exchange bottlenecks are resolved.

2017 is likely to bring a cyclical recovery to sub-Saharan African economies. But this will not mean a restoration of previously robust growth rates.

Much uncertainty surrounds the likely economic impact of a Donald Trump presidency in the US. In recent weeks, global equity and commodity markets have rallied in anticipation of more expansionary fiscal policy and the possibility of faster US economic growth. The US dollar has strengthened against other currencies, especially those of emerging markets, which are seen as especially vulnerable to a potential trade war.

Many worry about how the US will afford more infrastructure spending; bond markets have sold off (with prices falling and bond yields rising), reflecting the concern that larger fiscal deficits may be needed to enable any spending stimulus. Each of these factors will have implications for sub-Saharan African economies in 2017.Africa is unlikely to be the direct target of any Trump-induced trade protectionism. But if trade tensions escalate, potentially weakening confidence in emerging market prospects, sub-Saharan African economies are likely to be affected. Over the last two decades, Africa's trade with emerging markets has grown rapidly, at the expense of its trade with more developed partners. A slowdown in global trade would be a negative for trade-dependent emerging markets and could hurt their demand for sub-Saharan Africa's export commodities.

To counter this, African economies will have to redouble efforts to boost intraregional trade. While unlikely to compensate for a global trade slowdown, it might mitigate some of its more negative effects. Plans for an African Tripartite Free-Trade Area (TFTA) − encompassing 26 economies from the Common Market for Eastern and Southern Africa (COMESA), East African Community (EAC) and Southern African Development Community (SADC) − should get underway in 2017. The challenge will be how to make the new trade partnership meaningful. Poor infrastructure links and weak trade complementarities hampered earlier trade initiatives. However, faced with the threat of new disruptions to existing trade patterns and supply-chain integration, it is even more important that African economies start trading more among themselves.

In the years following the 2008-09 global financial crisis, , African economies took advantage of cheaper financing to issue record amounts of traded external debt. Many of these countries are now only five or six years away from a large amount of this Eurobond debt maturing. Ordinarily, borrowing countries would be looking to refinance their existing debt, issuing more long-term debt some time before their existing debt is due to mature. But rising US interest rates and higher bond yields may complicate this process as global investors will likely demand even high returns for investing in sub-Saharan African debt, which is perceived to be more risky.

For African governments, borrowing internationally to invest in infrastructure is likely to become more expensive. They will have to do more to reassure lenders that they can repay existing debt. Those countries that are able to boost confidence by signing up for IMF and World Bank reforms will likely be rewarded with access to cheaper financing. Those that fail to adopt reforms could find their access to international capital markets more constrained.

Weak growth in recent years has impacted the health of the banking sector in different sub-Saharan African economies. Weaker commodity prices and sluggish fiscal revenue resulted in many governments falling behind on payments to suppliers and contractors. The prevalence of fiscal arrears (late payment by government) has often been closely linked to the problem of non-performing loans in different banking systems. As banks face mounting losses, they become more reluctant to lend. Economic momentum slows further.

Often the problems are country-specific. Prior to the collapse in the oil price in late-2014, Nigerian banks were used to lending in foreign exchange. But currency depreciation since then has made foreign exchange loan repayment more difficult. It has also called into question capital adequacy, the buffer (measured in local currency) through which banks are able to absorb losses. Until these issues are resolved comprehensively, it is difficult to see the return of new lending appetite on a sustained basis.

Populist policies have also played a role in weakening the performance of the financial sector. In Kenya, the full impact of the adoption of loan rate caps and regulated loan-deposit spreads, introduced in 2016, will only be seen in 2017 or beyond. Banks now face a maximum rate at which they are able to lend to clients. Wherever loan rate caps have been introduced in the past, the effect has been the same. If banks cannot price adequately for risk, they withdraw their lending, choosing to lend only to the safest and most established borrowers. Small and medium enterprises as well as new start-ups with no established credit histories will likely face the brunt of this, meaning several growth and employment opportunities will be forgone somewhat needlessly.

While Africa's economies face more difficult external conditions in 2017, many of the policies that have contributed to weaker economic growth are home-grown. The good news is that average regional growth should recover in 2017. But greater reform and deeper debate on the domestic policy choices that have constrained growth are required for more meaningful transformation.

Ends.

About the author

Razia Khan *is Standard Chartered's Chief Economist for Africa and a well-known commentator on African markets. Razia advises the Bank's clients on Africa strategy and provides regular updates to African central banks, finance ministries and multilateral institutions. She joined the Bank in 1997. Razia holds a BSc (Hons) degree in economics and an MSc (Econ) in development, including monetary economics and international trade law, from the London School of Economics. Razia has been a member of the World Economic Forum's Global Agenda Councils on Population and on Poverty and Development. She serves on the Advisory Board of the Royal Africa Society.*

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