Background Note for *Mobilizing with Africa II* High-Level Virtual Event

2020 Annual Meetings
October 9, 2020

The coronavirus (COVID-19) outbreak continues to exact a heavy human and economic toll on Africa. An historic recession has set in. African countries mounted a rapid response and the international community provided unprecedented financial assistance. But countries are facing extraordinary financing needs and, in some cases, debt distress. With a highly uncertain outlook for the pandemic, renewed reform efforts, increased official financing, and resumed private inflows are vital for a resilient recovery in Africa.

AFRICAN COUNTRIES RESPONDED QUICKLY TO THE PANDEMIC BUT IT CONTINUES TO EXACT A HEAVY TOLL

With the COVID-19 pandemic causing a deep, synchronized and unparalleled downturn in the global economy, Africa has been hit hard by the health and economic crisis. The reverberations of a global recession, including weak commodity prices, and restrictions imposed on activity that were a necessary response to the pandemic came at a steep economic cost. In just a few months, decades of hard-won development gains have been put at risk with millions of lives and livelihoods upended. Real GDP is projected to contract by at least 2½ percent in 2020, representing one of the worst outcomes on record for the continent. Recovery is expected to start next year but real GDP will only reach the pre-crisis level in 2022, a difficult outlook that faces significant downside risks: particularly regarding the path of the pandemic, the strength of the region's hard-pressed healthcare systems, external financing flows, and future growth in investment and productivity.

The health and human costs are on the rise. More than one million cases have been reported across Africa, with 23,000 confirmed deaths representing 3 percent of confirmed deaths in the world (WHO 2020). At over 650,000 cases, South Africa has the fifth highest number of COVID-19 infections globally. Deteriorating economic conditions and loss of employment could cause a drop in household income up to 12 percent this year compared to a world without COVID-19. As a result, up to 43 million additional people could be pushed into extreme poverty in Africa, wiping out five years of progress in poverty reduction. The crisis also puts at risk the past decade's progress in building human capital, including improvements in health, school enrollment, and reduced stunting.

So far, policymakers across the continent have acted swiftly to protect the population from the worst of the crisis, making some difficult choices in the process. African countries individually and collectively have taken important policy steps and made significant investments to curb the spread of COVID-19 and protect lives and livelihoods. By March 2020, the AU-Africa CDC established the AU COVID-19 Response Fund, which galvanized African leaders' ownership and commitment to respond to the pandemic. This timely and catalytic intervention led to the mobilization of additional resources from other development partners in support of the continental response. However, falling revenues and tight resource envelopes have meant postponement of capital spending to accommodate health and social costs. Some countries are confronting high debt burdens having to choose between debt service and social spending. Beyond much-needed relief measures, African governments will require international financial and technical support to implement policies that build greater resilience, boost productivity and generate more and better jobs — enabling African economies to recover faster and thrive in the post-COVID-19 world.

THE INTERNATIONAL COMMUNITY HAS STEPPED UP TO PROVIDE FINANCIAL SUPPORT

In response to the crisis, the international community has so far provided significant financial assistance this year, mostly in fast-track concessional support:

- The Fund has significantly scaled up financial assistance to Africa with year-to-date disbursements of around $26 billion to over 40 countries in 2020, nearly ten times higher than the annual average of the last decade in percent of GDP.[1] Country authorities are committed to ensure transparent planning, use, monitoring, and reporting of COVID-19-related spending. Several countries have already enacted legislation and established oversight bodies to implement the enhanced governance measures (e.g., Burkina Faso, Central African Republic, and Gambia). The Fund has also provided grants for debt service relief to 22 countries in Africa for $0.2 billion as part of the Catastrophe Containment and Relief Trust (CCRT).

- The World Bank (IDA and IBRD) has provided about $21.9 billion in in lending, 90 percent of which is on concessional transfers from IDA. This includes $881m in emergency health operations to 30 countries financed through the COVID-19 Fast Track Facility. Emergency operations are strengthening health systems, supporting containment measures, increasing surveillance, providing essential medical supplies and broadening social protection programs, while longer-term development projects have pivoted to lay the groundwork for a robust and sustained recovery in Africa. The World Bank is now working on a financing package to support equitable access to vaccines and their distribution in African Countries.

- The International Finance Corporation has disbursed over $1 billion in financial support to entrepreneurs, SMEs, and financial intermediaries. It is also creating “upstream” investment opportunities in countries, by creating markets and projects with investment potential to underpin the recovery phase. MIGA has issued over $640 million in guarantees through its COVID-19 Facility to support African economies in the procurement of medical supplies, provision of short-term funding and working capital, and trade finance to kickstart value chains.

- In response to the COVID-19 crisis, the G20 responded with the Debt Service Suspension Initiative (DSSI), enabling eligible countries to postpone debt service payments due in 2020 to official creditors. To date, 26 African countries have requested to participate, resulting in additional fiscal space of $1.8 billion, with Angola, the Republic of Congo, and Mauritania being among the largest beneficiaries. The G-20 and international financial institutions have also called on private creditors to participate in the DSSI.

- Other international and regional institutions, notably the African Development Bank and Islamic Development Bank have also provided targeted financial support of over $4 billion. Much of the financing aimed at improving health systems, expanding social protection, and supporting businesses.

[1] The amount indicates financial assistance disbursed so far in 2020 under emergency lending instruments, existing programs, augmentations, and CCRT.

MEDIUM-TERM EXTERNAL FINANCING NEEDS ARE LARGE

Despite significant immediate financial support and the projected sizable medium-term domestic adjustment, the 54 countries in Africa are facing large external financing needs. Some of these financing needs would be met by debt stock reduction where appropriate. Even more important, financing from the international community and the private sector should be channeled to help African countries pave the way for productive and transparent investments, key to a sustained and inclusive recovery. For 2020–23, Africa is facing cumulative gross external financing needs of about $1.2 trillion. They include the following:

- projected current account deficits ($510 billion), including interest payments ($120 billion), and external debt amortization ($590 billion) for 2020–23;
- resumption of non-health and non-social spending that were put aside ($90 billion, or 1 percent of GDP annually) due to a reprioritization to accommodate COVID-19 related fiscal support, which are important to ensure economic recovery; and
- additional spending that would allow countries to mount a crisis response in the health and social sectors ($40 billion or 0.4 percent of GDP annually) more at par with other emerging market economies.[2] [3]

Under current trends, such financing needs are likely to see significant shortfalls. The current commitments from the international community are expected to fill less than a quarter of the projected financing needs during 2020–23. Despite a resumption of capital flows to some EMs since June, external borrowing costs are still prohibitively high for the frontier emerging markets, and the timing of their return to international capital markets remains uncertain. Assuming private capital inflows remain in their downbeat phase, reaching only up to 75 percent of the level in pre-crisis years (2015–19), **the financing gap is projected to be around $345 billion for 2020–23,** which will make it difficult to implement critical reforms and programs for a strong and sustained recovery. Africa's lowest income countries, which are eligible for access to the IMF's concessional Poverty Reduction and Growth Trust (PRGT) fund, account for more than 40 percent of this gap .

CONCERTED SUPPORT FOR AFRICA

Without significant additional assistance, including debt relief, many countries in Africa will struggle to simply maintain macroeconomic stability, while also meeting the basic needs of their population. Stepped-up and concerted financial support from the international community is imperative to help policymakers make the right choices:

- ***Providing debt relief.*** The Bank and Fund recommend extending the DSSI initiative for up to one year (with a mid-term review), along with flexibility in the repayment schedule, to provide much-needed additional fiscal space that can be used to support the recovery and avoid bunching of DSSI repayments. For countries with high risk of debt distress, or that have been assessed to have unsustainable debt, it is recommended to condition DSSI access in 2021 on requesting and working toward a Fund-supported reform program aimed at reducing debt vulnerabilities and addressing debt levels where needed.

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[2] Countries in Africa increased their COVID-19-related spending by about 2½ percent of GDP compared to 5 percent of GDP average spending by emerging market economies outside Africa.

[3] Additional expenditure needs under bullets 2-3 are larger amongst countries in sub-Saharan Africa owing to stricter financing constraints.

- ***Continued financial and policy support from the World Bank Group.*** Over the IDA19 replenishment period (FY21–23), about $50 billion in concessional resources will be available to eligible countries in Africa to support their recovery and their development needs. Creditworthy countries on the continent will also have access to resources from the IBRD. The World Bank will use its Development Policy Operation Instrument to support reforms that catalyse productivity-driven growth; and Investment Project Financing and Programs-for-Results Instruments to re-commit to long-term goals in a transformed setting, including improved pandemic-readiness of health and other critical systems. The IFC and MIGA are collaborating closely with the World Bank to pool available resources, bring public and private sectors together, and enable large-scale solutions to mobilize market finance by packaging and tranching risks, in order to attract private sector investments.
- ***Ensuring adequate resources for PRGT-eligible countries.*** In response to an unprecedented demand for concessional financing, there has been a strong positive response from member countries so far in raising over SDR 15 billion ($21.2 billion) in new PRGT loan resources. In light of the increasing demand for PRGT resources, the Fund will review its concessional facilities and financing by the end of the year, including access limits, to ensure appropriate levels of concessional support to PRGT-eligible countries while maintaining the self-sustaining PRGT framework. Also, significant additional grant pledges will be required to increase the PRGT subsidy account and to unlock a possible third tranche of the CCRT to provide 23 of the poorest PRGT-eligible African countries.

- ***Continuing IMF lending from the General Resource Account (GRA).*** IMF will continue to support EMs and better off frontier emerging markets in the region through its GRA lending instruments by relying on its war chest of $1 trillion.

However, these stepped-up IMF/World Bank financing and G20 debt relief initiatives will not be sufficient to meet the medium-term financing gap faced by the continent. Fresh resources will need to come from both other official and private sources. Regional development banks will need to maximize their lending capacity and mobilize more resources. Private capital inflows will need to rebound stronger than envisaged. This will depend critically on the reforms and policies countries undertake to navigate this crisis (see below).

ENSURING A STRONG EXIT FROM THE CRISIS

Prior to the pandemic, many African countries needed a fresh wave of reforms to lift medium-term growth, create jobs for a growing population, and make progress toward meeting the SDGs. The need for reforms remains urgent and is complicated by the possibility that the post-COVID world may be significantly different from the one envisaged just a year ago.

Reforms could significantly strengthen policy space and growth prospects. If African countries were to raise revenues worth 1 percent of the continent's GDP, additional resources equivalent to $26 billion could be mobilized annually. Governance and PFM measures to increase transparency, efficiency and accountability of the public sector can unlock significant private sector investment, both foreign and domestic. These should be complemented by reforms to enhance the business climate and broaden financial inclusion. Supporting policy actions and investment that address the challenge of creating more, better and inclusive jobs will be key to a resilient recovery. These include investing in energy, human capital, women empowerment, and boosting agricultural productivity.

Governments must also look to invest in digital infrastructure. This will support the accelerated shift to e-commerce and increased digitalization of the economy, including to expand to coverage and improve the targeting of social safety nets. The risk of not doing so is to allow an already growing digital divide between and within countries to become entrenched—with implications for longer-term productivity and growth. Investment in digital infrastructure and e-government would also help boost government transparency and accountability and fight corruption.

Trade integration will be important. The COVID-19 crisis may prompt a significant reorganization of global and regional value chains, underscoring the potential of the African Continental Free Trade Area (AfCFTA) as an engine for the development of regional trade. An effective framework that would include reducing cross-border frictions to promote trade facilitation among neighboring countries will be essential. These reforms would not only reduce Africa's vulnerability to global disruptions, but would also boost regional competition and productivity, and promote food security. As the region moves into the recovery phase, policy makers should resume their efforts to ensure implementation as soon as possible.

For many countries in Africa, climate change poses strong challenge—where the region is especially vulnerable, and where the ex-ante costs of mitigation are far less than the ex-post costs of cleanup and recovery. This will entail investing in technologies that support public goods like clean air, flood defenses, resilient infrastructure, and renewable energy.

CONCLUSION

Both additional external financing and reforms will be imperative to ensure a resilient recovery. After all, the continent's potential and resourcefulness remain undented by this crisis.

Key deliverables by partners include:

- Increasing PRGT loan and subsidy resources to make it possible to raise PRGT access limits and ensure the PRGT self-sustainability.
- Mobilizing CCRT grant resources to ensure debt-service relief for the full 24 months.
- Increasing concessional lending and grants by the World Bank, MDBs, and bilateral donors.
- Extending the DSSI for up to one year to provide liquidity support, and strengthening the international architecture for debt restructuring to assist countries with unsustainable debt.