

1. Two-Track Recovery Amid Elevated Uncertainty

Economic recovery in sub-Saharan Africa is set to continue with growth projected to pick up from 3 percent in 2018 to 3.5 percent in 2019.

But economic performance remains bifurcated (Figure 1.1).

- Some 21 countries, mainly the region's more diversified economies, are expected to sustain growth at 5 percent or more and remain on the impressive per capita convergence path they have been on since the early 2000s.
- But in the 24 other more resource-dependent economies, including the largest (Nigeria and South Africa), the growth looks set to remain anemic in the near term. With some two-thirds of the region's population residing in these countries, this implies much slower improvement in standards of living for the lion's share of sub-Saharan Africans.

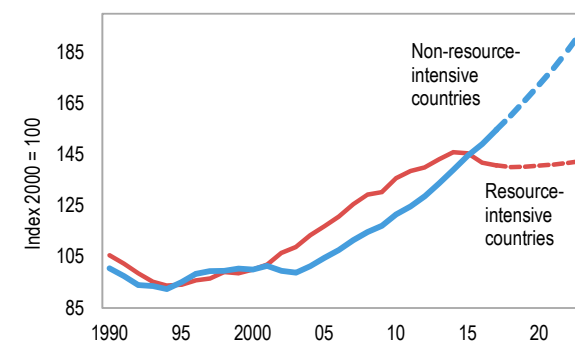
Against the backdrop of a complex and less-supportive external economic and geopolitical environment, the implications for policies (in the broadest of terms) are twofold:

- For the fast-growing economies, there is need to hand over the reins of growth from the public to the private sector. High growth in many of these countries has in part been spurred by higher levels of public investment, leading to a steady increase in public debt levels, notwithstanding rapid growth. This is a sign that fiscal policy has been procyclical, and the focus should switch toward limiting the increase in public debt and looking for alternative approaches to create fiscal space for further development spending, including through higher revenue mobilization, strengthening public financial management, and enhancing the efficiency of public investment.
- In the more resource-intensive countries and slower growing economies, there is a pressing need to complete the required fiscal

and external account adjustments to lower commodity prices, for reforms to facilitate economic diversification, and to promptly address the policy uncertainties that are holding back growth (particularly in Nigeria and South Africa). Weaknesses in public and private balance sheets are weighing on credit to the private sector and growth.

On current plans, macroeconomic policies are reasonably well calibrated in most countries in the region. Most sub-Saharan African countries have either a neutral or a tight monetary policy stance and have announced fiscal consolidation plans, which if implemented would contain their debt trajectories. These macroeconomic policies may need to be recalibrated to support growth in the event downside external risks materialize. However, countries would need to ensure that any shift in their policy stance is consistent with credible medium-term macroeconomic objectives, available financing, and debt sustainability. Fast-growing countries that face elevated debt vulnerabilities would need to prioritize rebuilding their buffers. In contrast, in the face of shocks that are deemed temporary, slow-growing countries could seek additional financing to accommodate a more gradual macroeconomic adjustment. And where this additional financing is not available, they should design the composition of macroeconomic adjustments with the least damage to near- and medium-term growth prospects.

Figure 1.1. Sub-Saharan Africa: Real GDP per Capita, 1990–23



Source: IMF, World Economic Outlook database.

Note: See Statistical Appendix for country groupings table.

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Such policies, together with measures to raise productivity growth and ensure more equitable sharing of the benefits of increased prosperity, would help sub-Saharan African countries strengthen resilience and create the conditions for sustained high and inclusive growth.

The rest of this chapter looks more closely at (1) the challenges the global environment poses for the region, (2) the causes behind and impact of rising public debt levels, and (3) some of the reforms needed to facilitate higher productivity growth.

Chapter 2 is devoted to a comprehensive analysis of the challenges faced by conflict that is exacting a toll on human lives and economies in a number of countries in the region, in particular, the analysis considers (1) the evolution in prevalence and intensity of conflicts over time in sub-Saharan Africa, (2) the impact (both directly and indirectly, through spillover effects) of conflicts on economic growth, (3) the key channels through which conflict affects output, and (4) the fiscal implications.

Chapter 3 assesses the opportunities for the region from the African Continental Free Trade Area (AfCFTA), which is in the process of ratification by countries. The agreement should create an important avenue to expand trade and foster closer economic integration between countries in the region. The analysis focuses on three key questions (1) How has Africa's intraregional and international trade evolved over time and what lessons can be drawn from the continent's subregional economic communities on the potential for further integration? (2) What is the potential impact of the AfCFTA on intraregional trade, and what policies are needed to foster further regional trade integration? and (3) How will the AfCFTA affect the welfare, income distribution, and fiscal revenue of African countries?

MACROECONOMIC DEVELOPMENTS AND PROSPECTS

A Complex External Environment

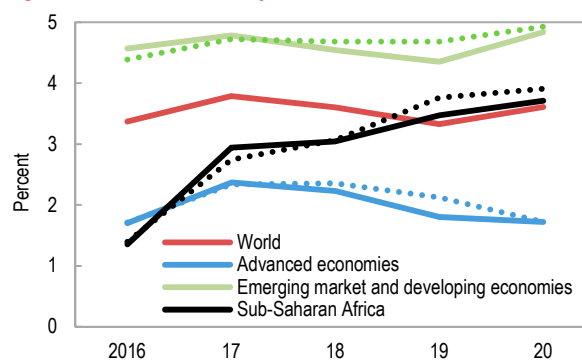
The global expansion has weakened amid rising trade tensions, volatile global financial conditions, and lower commodity prices (Figure 1.2). Global growth is estimated at 3.6 percent in 2018,

0.1 percentage point less than projected in the October 2018 *World Economic Outlook* (WEO), and is expected to slow to 3.3 percent in 2019 before recovering to 3.6 percent in 2020. The outlook for the global economy reflects a persistent weakening in activity in advanced economies, especially the euro area, and a slowdown, albeit temporary, in emerging markets. Over the medium term, global growth is expected to remain below the average prior to the global financial crisis amid weak productivity growth and a declining labor force growth in advanced economies.

Meanwhile, countries continue to deal with sharp swings in commodity prices (Figure 1.3). Volatility in commodity prices has increased, with a sharp fall in oil prices during the last quarter of 2018. Other non-oil commodity prices have also weakened, partly due to subdued demand from China. This marks a break from the sustained commodity price recovery since 2016, and markets are expecting most commodity prices to weaken further in 2019–20. Thus, the terms of trade for the region's oil exporters are expected to deteriorate, while those for the oil importers are poised to improve somewhat (Figure 1.4).

Volatility has also increased in global asset markets, and at the same time global financial conditions tightened in the latter half of 2018 (Figure 1.5). Nevertheless, foreign investors' appetite for the region's securities remained elevated, with issuances of international sovereign bonds by sub-Saharan African frontier markets reaching US\$17.2 billion in 2018, higher than the annual total in any previous year. Nigeria and Angola

Figure 1.2. Global Growth Projections: Current versus October 2018

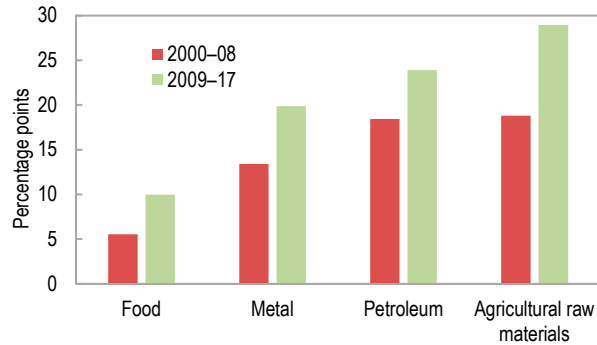


Source: IMF, World Economic Outlook database.

Note: Solid lines show current projections; dotted lines show projections of October 2018, IMF, World Economic Outlook database.

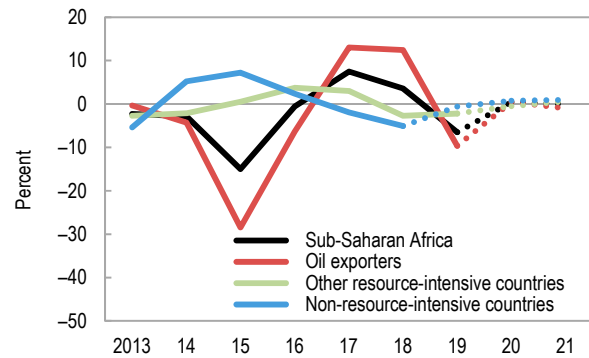
accounted for over half of the issuances, with about US\$5.4 billion and US\$3.5 billion worth of Eurobonds, respectively, with the remainder broadly evenly distributed across four other countries (Côte d’Ivoire, Ghana, Kenya, Senegal). But while

Figure 1.3. Real Commodity Price Indices: Volatility of Changes in Price Indices, 2000–08 and 2009–17



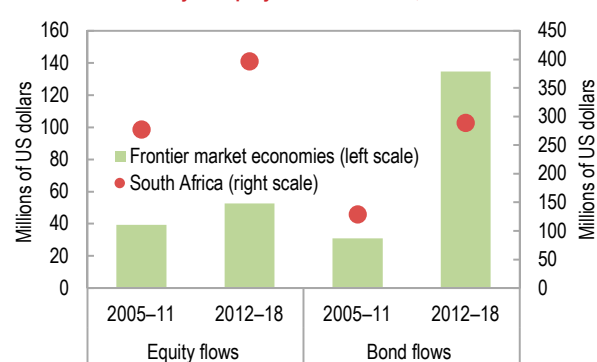
Source: IMF, Commodity Price System.
 Note: Standard deviation of biannual change in indices. All indices are deflated with US consumer price index.

Figure 1.4. Sub-Saharan Africa: Goods Terms of Trade Growth, 2013–21



Source: IMF, World Economic Outlook database.
 Note: See Statistical Appendix for country groupings table.

Figure 1.5. Sub-Saharan African Frontier and Emerging Market Economies: Volatility of Equity and Bond Flows, 2005–11 and 2012–18



Source: Haver Analytics.
 Note: Standard deviation of monthly flows.

the issuances were oversubscribed, the borrowing cost at issuance for the 30-year maturity has increased (for example, by about 162.5 basis points for Nigeria over the past year). The tightening in financing costs reflects monetary policy normalization in advanced economies and increased risk aversion, with some differentiation based on countries’ underlying fundamentals.

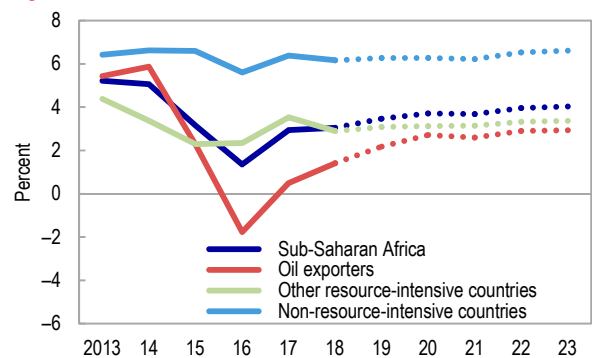
The Recovery Is Expected to Continue at a Slower Pace than Envisaged in October 2018

Against the backdrop of a less supportive external environment, sub-Saharan Africa’s average growth (weighted by GDP in purchasing power parity terms) is expected to increase from 3.0 percent in 2018 to 3.5 percent in 2019 and 3.7 percent in 2020 (Figure 1.6), about ¼ percentage point less than envisaged in the October 2018 *World Economic Outlook*. But these aggregate figures mask considerable heterogeneity across countries, with substantial differences between resource-intensive and non-resource-intensive countries.

Starting with resource-intensive countries, the overall performance remains weak in the largest economies, especially Nigeria and South Africa.

- Growth in Nigeria was 1.9 percent in 2018 and is expected to reach 2.1 percent in 2019, driven by recovering oil production and a pickup in the non-oil economy in the aftermath of the election. However, the near-term outlook remains subdued as a result of lower oil prices, which have large spillover effects, including to the non-oil economy. Over the medium

Figure 1.6. Sub-Saharan Africa: Real GDP Growth, 2013–23



Source: IMF, World Economic Outlook database.
 Note: See Statistical Appendix for country groupings table.

term, and under current policies, growth is projected to plateau at about 2¾ percent, implying that per capita income will remain broadly unchanged. These subdued growth prospects are likely to weigh on the region's growth performance both directly and indirectly through spillovers to Nigeria's trading partners, remittances to recipient countries, and financial linkages (see IMF 2018a).

- South Africa is expected to grow at 0.8 percent in 2018 and 1.2 percent in 2019. The recovery is predicated on a gradual improvement in business and consumer confidence as policy uncertainty diminishes. Under current policies, growth is expected to stabilize at about 1.8 percent over the medium term, barely above population growth. As a result, positive spillovers to other countries through import demand and the financial sector are likely to be limited (see IMF 2018a).

Non-resource-intensive countries are expected to continue growing rapidly at about 6.3 percent on average in 2019–20. Ethiopia, the region's third largest economy, is expected to see growth accelerate to 7.7 percent as the uncertainty engendered by political headwinds and external shocks abates. The government has also announced its intention to pursue reforms to hand the reins of growth to the private sector, which, if implemented properly, could raise growth in the medium term. Growth will remain driven mainly by rapid public investment (Senegal) and private consumption (Côte d'Ivoire, Kenya), particularly in the western and eastern parts of the region. Growth in other resource-intensive countries is expected to pick up, albeit at a more moderate pace of about 3.1 percent on average.

For the region as a whole and based on current policies, medium-term growth is expected to plateau at about 3¾ percent, or 1¼ percent in per capita terms. This is well below what is needed to lift the living standards of the region's population to the average of the rest of the world and help create the 20 million jobs a year needed to absorb new entrants to labor markets.

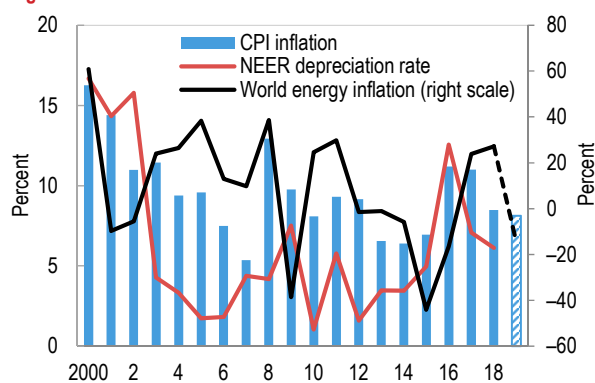
Inflation Pressures Are Easing, Driven by Low Oil Prices

Average inflation in sub-Saharan Africa is projected to decline to 8.1 percent in 2019 from 8.5 percent in 2018, reflecting the large decline in global energy prices. The pass-through of lower energy prices is expected to more than offset the lingering effects from past exchange rate depreciation (Figure 1.7). Demand pressures have played a limited role in inflation dynamics, and there is little persistence in inflation pressure, with only a quarter of each year's inflation manifesting itself into the next year, on average, across countries.

External Buffers Remain Low

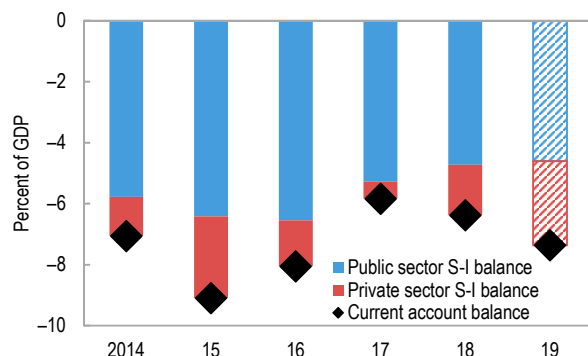
The (simple) average current account deficit is projected to widen to 7.3 percent of GDP in 2019 from 6.6 percent of GDP in 2018, mainly reflecting a larger deficit in non-resource-intensive countries and oil-exporting countries. The deficit in oil-exporting countries is expected to widen, owing to projected lower oil prices. The size of the current account deficit primarily reflects imbalances in public accounts (Figure 1.8), with public savings-investment deficits about three times as large as for the private sector in non-resource-intensive countries. The region is highly vulnerable to terms-of-trade shocks, and these have a large impact on current account positions, mainly through the trade balance. In particular, a 1 percent change in the commodity terms of trade translates into a 0.3–0.6 percent of GDP change in the trade balance, with the effects varying across countries and between positive and negative shocks.

Figure 1.7. Sub-Saharan Africa: CPI Inflation



Source: IMF, World Economic Outlook database.

Note: CPI = consumer price index; NEER = nominal effective exchange rate.

Figure 1.8. Sub-Saharan Africa: Savings-Investment Balance, 2014–19

Source: IMF, World Economic Outlook database.

Note: S-I = savings-investment.

Current account positions in the region remain below levels consistent with medium-term fundamentals and desired policies.¹ However, the range of current account imbalances varies widely across countries, ranging from no gaps in oil-exporting countries to large ones in non-resource-intensive and other resource-intensive countries.

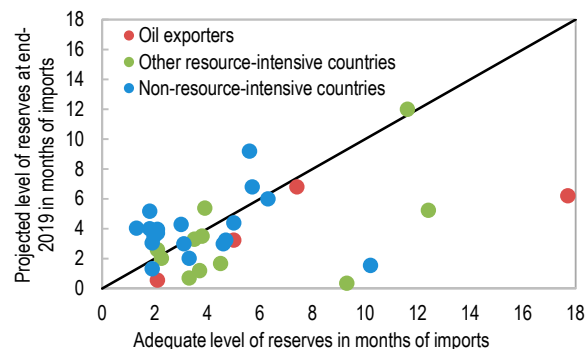
Widening current account balances are expected to further weaken foreign exchange reserve buffers, which are projected to fall to 3.7 months of imports in 2019, weakening particularly in oil exporters, and remaining below levels deemed adequate based on metrics derived from the crisis experiences of emerging market and developing economies (Figure 1.9).² The level of reserves in the region had been bolstered somewhat in 2018 by large capital inflows, especially following Eurobond issuances by frontier economies.

Fiscal Consolidation Is Expected to Proceed More Slowly as Terms-of-Trade Gains Erode

Following a significant contraction in 2018 by about ½ percent of GDP, the (simple) average fiscal deficit in the region is expected to narrow to about 3.2 percent in 2019–20 and continue on a consolidation path beyond 2020. The consolidation path primarily reflects the evolution of fiscal positions in oil-exporting countries, which are now expecting much lower oil revenue (Figure 1.10). This highlights the procyclicality of revenue and

¹ Based on the findings from staff analysis in “The Revised EBA-Lite Methodology” (forthcoming).

² The assessment of reserve adequacy is made using IMF tools specifically designed for emerging market economies and credit-constrained economies. See <http://www.imf.org/external/np/spr/ara/> for details.

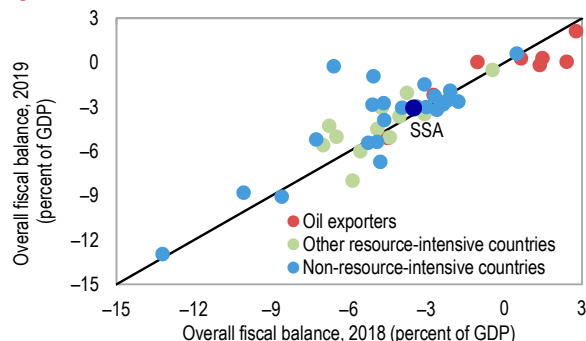
Figure 1.9. Sub-Saharan Africa: Reserve Buffers

Sources: IMF, World Economic Outlook database; and IMF staff calculations.

Note: Oil exporters, excluding Angola, Nigeria, and South Sudan, are grouped into one data point corresponding to Central African Economic and Monetary Community (CEMAC). West African Economic and Monetary Union (WAEMU) countries are grouped into one single data point and classified as non-resource-intensive. See Statistical Appendix for country groupings table.

capital spending to oil prices. In the face of adverse terms-of-trade shocks, fiscal adjustment tends to be uneven and skewed toward revenues and capital expenditure, particularly for oil exporters (Figure 1.11).

But this procyclicality is asymmetric. In general, an increase in the terms of trade above trend during “good times” raises revenues in oil exporters, while during a decline below trend in the terms of trade in “bad times,” revenues generally fall by an even larger margin. This reflects in part the sensitivity of corporate profits to commodity price cycles, compounded by tax design challenges (related, for example, to forward-carry losses). Similarly, oil exporters tend to expand capital expenditure

Figure 1.10. Sub-Saharan Africa: Overall Fiscal Balance, 2018–19

Source: IMF, World Economic Outlook database.

Note: See Statistical Appendix for country groupings table.

when the terms of trade are increasing and contract such expenditure during bad times by an even larger margin. Recurrent expenditures are much less sensitive to terms-of-trade cycles, reflecting some rigidities in spending items. Fiscal positions are expected to remain broadly unchanged in other resource-intensive countries and improve somewhat in non-resource-intensive countries. The improvement in non-resource-intensive countries mostly reflects some increased grants.

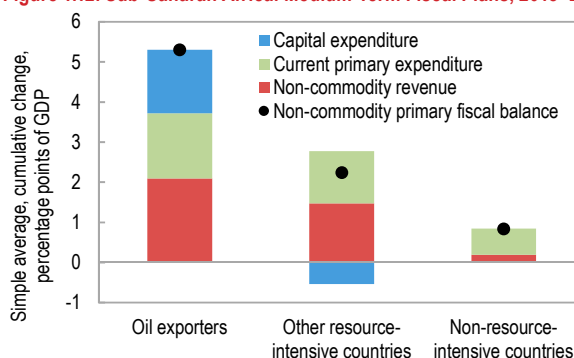
While some countries have made some progress on domestic revenue mobilization, most have not. Noncommodity revenue (excluding grants) increased as a ratio of GDP in 2018 in 25 countries, with the largest increases in the Democratic Republic of the Congo, Equatorial Guinea, Niger, Sierra Leone, and Togo. Most of the revenue increase stemmed from tax revenue.³ Progress on domestic revenue mobilization reflected (1) tax policy reforms, including through lower exemptions, and (2) improvements in revenue administration, including by assigning tax identification numbers to commercial importers, improving the land registry, and strengthening tax audits. In other countries, non-commodity-related revenue remained broadly unchanged or even declined as a share of GDP in a few cases (Botswana, Republic of Congo, Nigeria). The fall in noncommodity revenue partly reflects one-off factors and the introduction of exemptions (Botswana). Weak revenue administration and narrow tax bases continue to hold back domestic revenue mobilization. Overall, for sub-Saharan African countries, the revenue gap, estimated at

3–5 percent of GDP on average across countries, is not expected to be closed through the medium term (Figure 1.12).

Public Debt Vulnerabilities Remain Elevated

Sixteen sub-Saharan African countries are classified as having either a high risk of debt distress (Burundi, Cameroon, Cabo Verde, Central African Republic, Chad, Ethiopia, Ghana, Sierra Leone, Zambia) or being in debt distress (Republic of Congo, Eritrea, The Gambia, Mozambique, São Tomé and Príncipe, South Sudan, Zimbabwe) (Figure 1.13). The remaining 19 low-income and developing countries have low to moderate debt vulnerabilities. For middle- and upper-income countries, public debt remains sustainable under the baseline in most cases. However, debt ratios are close to or exceed risk thresholds in a few countries (Namibia, Seychelles).

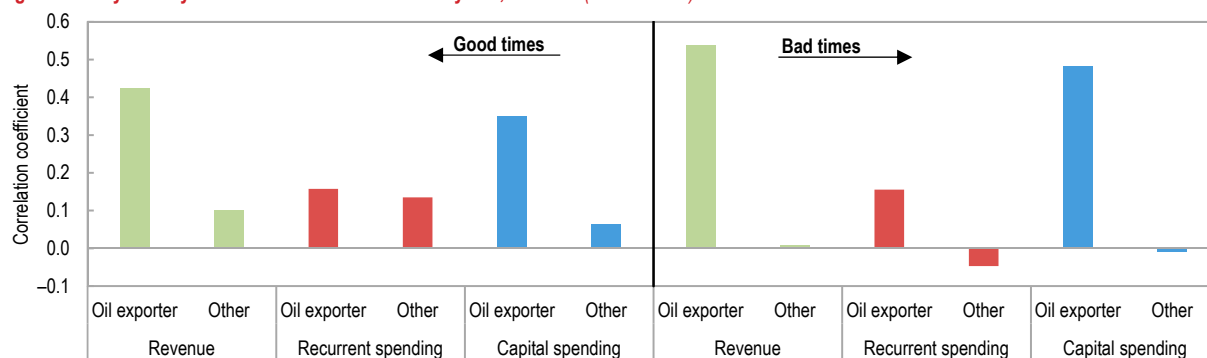
Figure 1.12. Sub-Saharan Africa: Medium-Term Fiscal Plans, 2018–23



Sources: IMF, World Economic Outlook database; and IMF staff calculations.

Note: Excludes Burundi, Eritrea, and South Sudan due to data availability. See Statistical Appendix for country groupings table.

Figure 1.11. Cyclicity of Fiscal and Terms of Trade Cycles, 2000–17 (In real terms)



Source: IMF staff calculations.

³ For successful episodes of revenue mobilization, identified in IMF (2018b), the annual increase in the revenue-to-GDP ratio was 1.2 percentage points, two-thirds of which was contributed by taxes.

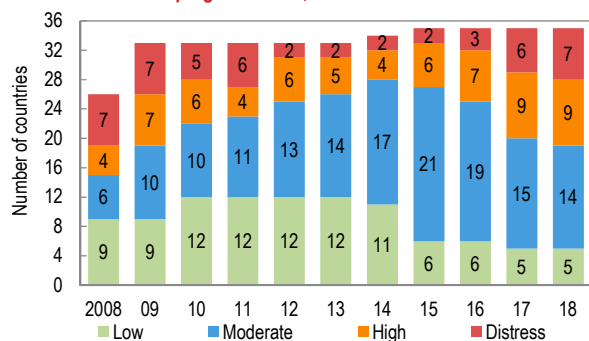
Average public debt in sub-Saharan Africa was estimated at close to 56 percent of GDP at the end of 2018, with wide heterogeneity in debt dynamics across countries. Oil exporters have seen some debt reductions, while other resource-intensive and non-resource-intensive countries continue to see increases in debt. Debt reductions mostly reflect fiscal consolidation in non-resource-intensive countries and a growth rebound in oil exporters.

Recent GDP rebasing contributed to a sizable drop in the debt ratio (The Gambia) and to a lesser extent elsewhere, as this was partially offset by commercial bank resolution (Ghana) and expansion in the debt perimeter to cover the broader public sector (Senegal). Also, in some highly indebted countries, continued improvement in revenue performance (Republic of Congo) and higher GDP

growth (The Gambia) are expected to strengthen debt-servicing capacity. Progress with debt resolution has helped reduce outstanding external arrears (Chad), and a number of other highly indebted countries are making good faith efforts to reach agreement with creditors (Republic of Congo, The Gambia).

Looking ahead, under current consolidation plans, public debt ratios are expected to stabilize or even decline across country groupings on average (Figure 1.14). But the baseline public debt trajectories are subject to significant uncertainties, including foreign exchange and rollover risk. Furthermore, fiscal uncertainties related to state-owned enterprises (SOEs) and the accumulation of public domestic arrears also weigh on public balance sheets (Cameroon, Ethiopia, The Gambia, Mozambique). In some cases, SOEs pose significant fiscal and financial risks, in part due to their relative economic size (Angola, Cabo Verde, South Africa), and have contributed to crowding out higher-priority public spending (Botswana, Cabo Verde, Madagascar).

Figure 1.13. Sub-Saharan Africa: Debt Risk Status for PRGT Eligible Low-Income Developing Countries, 2008–18



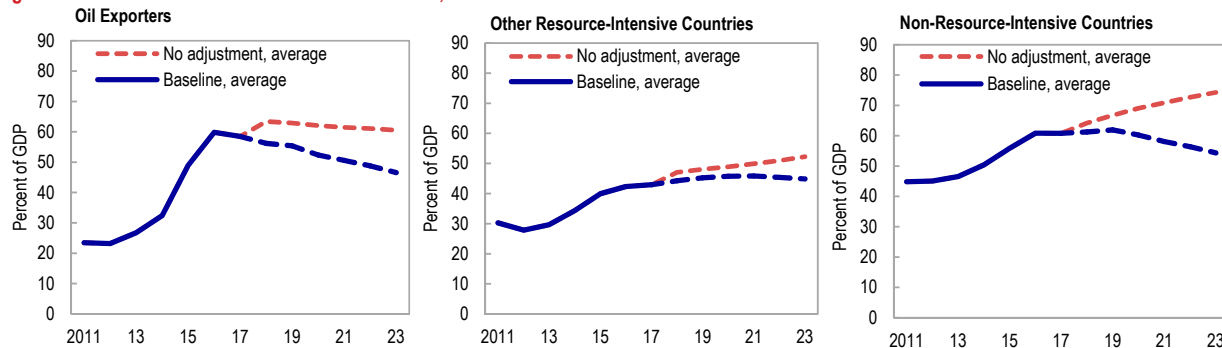
Source: IMF, Debt Sustainability Analysis Low-Income Developing Countries database.

Note: Debt risk ratings for Burundi, Chad, The Gambia, Lesotho, Rwanda, São Tomé and Príncipe, and Zimbabwe begin in 2009, Cabo Verde in 2014, and for South Sudan in 2015. PRGT = Poverty Reduction and Growth Trust.

Weaknesses in Bank Balance Sheets Are Weighing on Credit Growth

Nonperforming loans (NPLs) remain high in many sub-Saharan African countries and have continued to rise, particularly in some countries where the ratios are already elevated (Central African Economic and Monetary Community [CEMAC]) (Figure 1.15). The high NPL levels reflect the legacy of the 2014 commodity shock,

Figure 1.14. Sub-Saharan Africa: Public Debt to GDP, 2011–23



Sources: IMF, World Economic Outlook database; and IMF staff calculations.

Note: Baseline projections reflect the program or baseline scenarios reported in the latest IMF staff reports. No adjustment projections assume that the primary deficit, the real interest expenditure, and the other components of debt accumulation will remain at their 2017 levels, while the exchange rate and real GDP growth components are as in baseline projections. Excludes Burundi, Eritrea, and South Sudan due to data availability. See Statistical Appendix for country groupings table.

weak risk management practices, and government arrears (Central African Republic, Chad, Equatorial Guinea). In Ghana, write-offs are helping reduce the NPL overhang, as the systemwide NPL ratio reached 18.2 percent at end-2018. More generally, high NPL levels are weighing on credit growth (Figure 1.16) and encouraging banks to hold more government bonds (Bouis, forthcoming).

Despite some improvements in capital adequacy ratios, pockets of vulnerability remain. Banks' capital has increased as a ratio to risk-weighted assets in several countries (Chad, Republic of Congo, Equatorial Guinea, Gabon, Ghana, Malawi, Namibia), though zero risk weighting of government bonds could mask underlying capital coverage in the event that sovereign risk materializes (Figure 1.17). In many countries, capital increases reflect recent measures to raise minimum capital requirements, to resolve insolvent banks, or to

support illiquid ones (Ghana, Kenya). However, in a number of countries, a few small banks remain undercapitalized (Kenya, Nigeria, Togo), and in a few cases, systemic banks remain undercapitalized as well. Other sources of concern for the health of banks' balance sheets include foreign currency liquidity mismatches (Angola), high loan concentration (Benin, Equatorial Guinea, Eswatini, Malawi, Namibia), insufficient provisioning (Angola), and increased household and corporate debts (Tanzania).

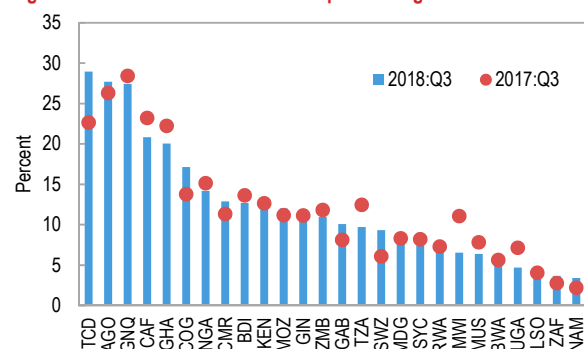
RISKS TO THE OUTLOOK

Risks are mainly tilted to the downside in the near term and balanced over the medium term. In the near term, deteriorating external conditions could slow growth in sub-Saharan Africa amid an escalation and broadening in trade tensions, stronger-than-anticipated tightening of global financial conditions, and greater policy uncertainty. In addition, the region's dependence on agriculture makes it vulnerable to extreme weather conditions. Over the medium term, while low potential growth and slow employment creation raise risks of dislocation and threaten social cohesion, further trade and financial integration promise to improve living conditions and facilitate structural transformation.

Trade Tensions

Trade tensions between the United States and China and several advanced economies have contributed to slowing global demand, especially in China, which in turn has led to lower commodity prices and

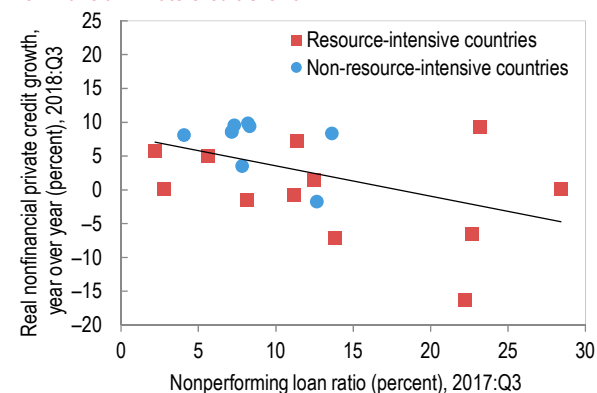
Figure 1.15. Sub-Saharan Africa: Nonperforming Loan Ratio



Sources: Country authorities; and IMF, Financial Soundness Indicators database.

Note: See page vi for country abbreviations table.

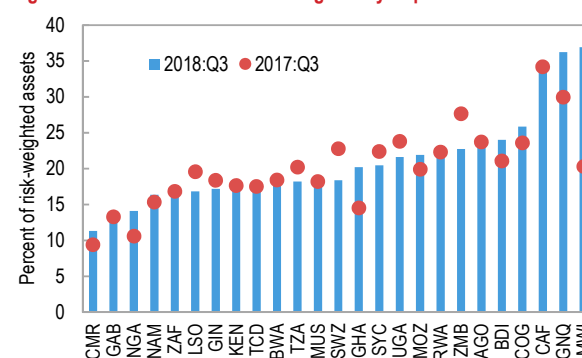
Figure 1.16. Sub-Saharan Africa: Nonperforming Loan Ratio and Real Nonfinancial Private Credit Growth



Source: IMF, Financial Soundness Indicators database.

Note: See Statistical Appendix for country groupings table.

Figure 1.17. Sub-Saharan Africa: Regulatory Capital Ratio



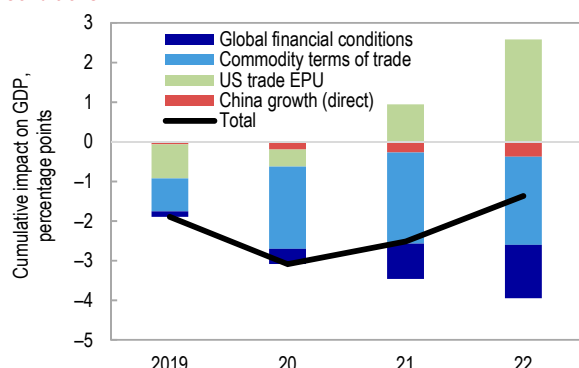
Sources: Country authorities; and IMF, Financial Soundness Indicators database.

Note: See page vi for country abbreviations table.

weaker demand for sub-Saharan Africa’s commodity exports. Intensification of these tensions beyond what is already incorporated in the forecast could slow growth in the region significantly. Indeed, growth-at-risk analysis indicates that heightened trade tensions along with increased trade policy uncertainty in the United States, slower growth in China, lower commodity prices, and tighter global financial conditions could lower growth in sub-Saharan Africa by 2 percentage points in 2019 and 1½ percentage points in 2020 (Figure 1.18). Sub-Saharan African countries most affected by trade tensions would be commodity exporters, along with those countries (commodity exporters and importers alike) that have stronger linkages with China and global markets, and those with large refinancing needs.

However, if there is a resolution of trade differences without increasing distortionary barriers, improved sentiment and continued easing financing

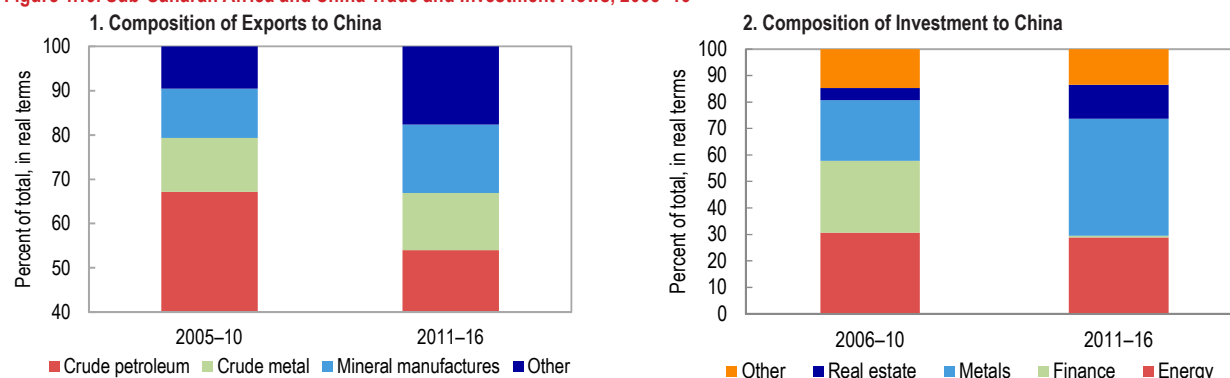
Figure 1.18. Trade Tensions, China Slowdown, and Global Financial Conditions



Source: IMF staff calculations.

Note: EPU = economic policy uncertainty.

Figure 1.19. Sub-Saharan Africa and China Trade and Investment Flows, 2005–16



Sources: United Nations, Commodity Trade Statistics database; Chinese Global Investment Tracker; and IMF staff calculations.

conditions could lift global growth, with positive effects on sub-Saharan Africa.

Sharper-than-Anticipated Growth Slowdown in China

China’s economic ties with the region have deepened markedly over the past 20 years both through trade and financial linkages. China is the region’s largest trading partner, accounting for about 20 percent of total trade. About 70 percent of the region’s exports to China are related to commodities, particularly oil, minerals, and metals. About 20 percent of the region’s imports are from China, and they are dominated by consumer goods imports (45 percent) and to a smaller extent physical capital goods and intermediates. Imports from China amounted to US\$67.5 billion in 2017, compared with US\$13.7 billion imports from the United States and US\$79.7 billion imports from Europe. At the same time, China has become a major creditor for the region, providing significant lending to several countries as well as foreign direct investment (about 5 percent of total foreign direct investment). China’s direct investment into the region is typically in metals and energy and flows primarily to resource-intensive countries. These investments are then channeled back into China through exports of metals and minerals (Figure 1.19).

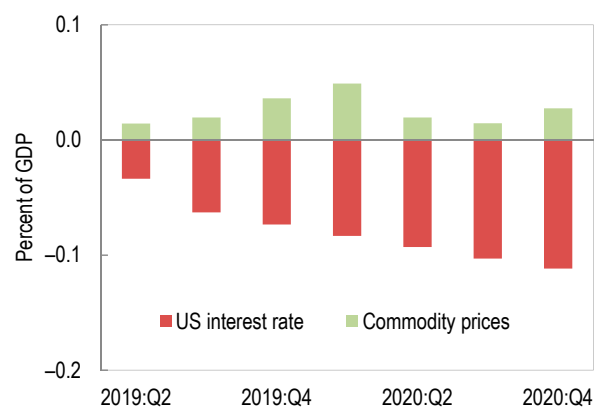
Thus, a sharper-than-anticipated slowdown in China has the potential to affect growth in the region significantly, mainly through trade linkages, particularly the demand for commodities with its attendant effects on commodity prices.

Overall, empirical estimates indicate that, over a one-year horizon, a 1 percent fall in industrial production in China leads to a 5–7 percent fall in metals and fuel prices (see IMF 2016b). These effects could be compounded by several factors, including a reduction in China’s investment in resource-intensive countries and increased volatility in global financial markets as uncertainty rises about economic prospects in China. Increased volatility in global markets could lead to a tightening in financing conditions for the region’s frontier economies.

Tighter Global Financial Conditions

Stronger-than-anticipated tightening of global financial conditions could arise from a range of triggers besides escalating trade tensions, including higher-than-expected inflation in the United States, a “no-deal Brexit” withdrawal of the United Kingdom from the European Union, or a deeper-than-envisaged slowdown in China. Tighter global financial conditions could constrain financing and growth for many sub-Saharan African countries, especially the region’s frontier economies, which have relied heavily on global markets to finance development needs. Furthermore, as tighter financial conditions are likely to manifest themselves in higher US interest rates, a stronger US dollar, and lower commodity prices, capital outflows and refinancing risks—particularly given the lumpy maturity of bonds (Figures 1.20 and 1.21)—could rise, increasing the likelihood

Figure 1.20. Net Financial Flows: Estimated Cumulative Impact of External Factors



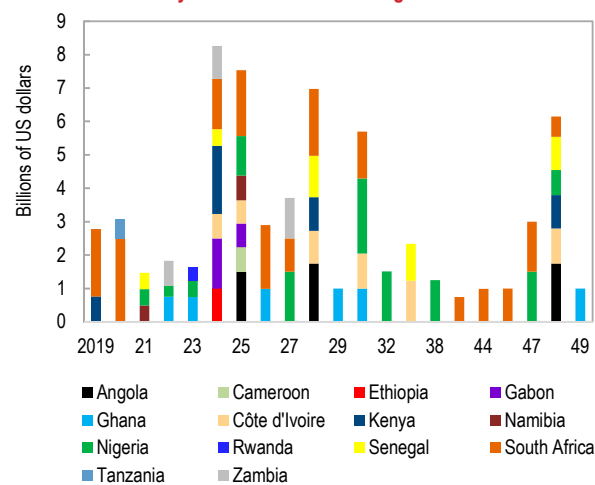
Source: IMF International Financial Statistics database. IMF staff estimation based on Chapter 2 in *Regional Economic Outlook: Sub-Saharan Africa*, October 2018.

of a balance of payments crisis in sub-Saharan Africa. Second-round effects could be substantial, compounded by growing sovereign-bank linkages that make banking sectors increasingly vulnerable to tightening global financial conditions and fiscal challenges.

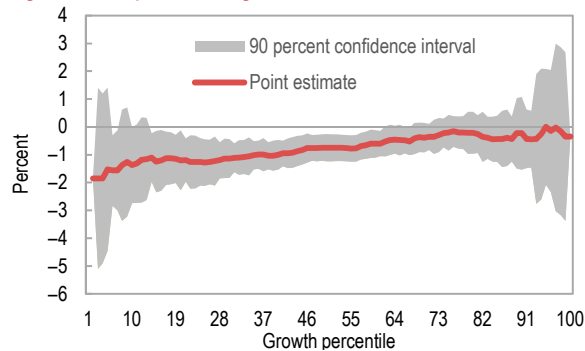
Climate Shocks

Climate shocks such as excessive rains or a delayed rainfall season can lower agricultural output, increase food imports, reduce export and tax revenue capacity, and increase public spending needs. Below-average precipitation can reduce growth by up to 1½ percentage points within the same year in extreme cases (Figure 1.22). Cyclone Idai made landfall in March 2019 in southeast Africa with more than 2.6 million people affected and a decimation of physical infrastructure and farmland. In addition, El Niño could cause droughts in southern Africa (Botswana, Lesotho, Malawi, Mozambique, South Africa, Zambia, Zimbabwe) as well as above-average rainfall in east Africa (Ethiopia, Kenya, Tanzania, White Nile Basin). Thus, southern African countries are likely to suffer from lower crop production, while east Africa could benefit from abundant production in certain areas while suffering from flooding in others (particularly along the river systems of Kenya). These weather vagaries could also imply significant welfare implications with potential effects on conflicts.

Figure 1.21. Sub-Saharan African Frontier and Emerging Market Economies: Maturity of International Sovereign Bonds



Source: Bloomberg Finance L.P.

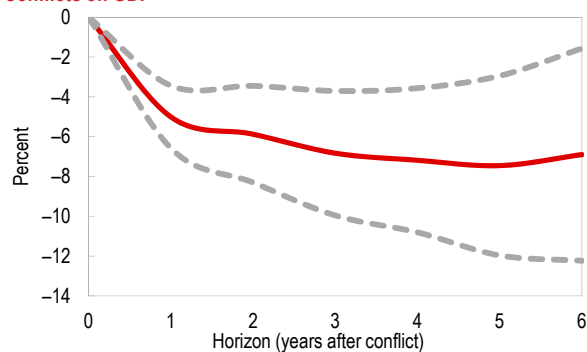
Figure 1.22. Impact of Droughts on GDP¹

Source: IMF staff calculations.

¹ Drought is defined as a dummy for average annual rainfall being at least one standard deviation below the mean.

Security

Heightened security risks have taken a toll on several countries, displacing millions of people and causing significant economic and social costs. The number of internally displaced persons is estimated to have reached 18 million in 2018 alone. As shown in Chapter 2, the loss of human life; destruction of infrastructure, human capital, and institutional quality; political instability; and elevated uncertainty associated with conflicts hamper investment and economic growth—not only in the year of the conflict but also afterward, making it difficult to escape the “conflict trap.” Intense conflicts could lower output by a cumulative 7½ percentage points through the medium term (Figure 1.23). They could also place significant strains on countries’ public finances, raising expenditure (including military spending) and lowering revenue, hampering governments’ ability to effectively respond to public finance challenges and thereby exacerbating the economic and social

Figure 1.23. Sub-Saharan Africa: Cumulative Impact of Intense Conflicts on GDP¹

Source: IMF staff calculations.

¹ Intense conflict is defined as moving from 0 to the top quartile of countries in terms of conflict-deaths-to-population ratio.

costs of the conflicts. Furthermore, these effects are also transmitted to neighboring regions and countries. In particular, the empirical evidence in Chapter 2 shows that large conflicts (involving 100 fatalities or more) in neighboring states within 500 kilometers are associated with a reduction in growth of about 2 percentage points. Thus, persistent security challenges could have global economic and humanitarian consequences.

POLICIES

For close to 20 years starting in the mid-1990s, the lion’s share of sub-Saharan countries recorded strong economic growth and improved development outcomes. During this period, growth was spurred by reforms and improved economic policies, a boom in commodity prices that benefited commodity exporters, fiscal space created by debt relief, and increased trade and investment flows.

But since 2015 this period of rising incomes has stalled, mainly for resource-intensive countries, and baseline projections indicate limited improvement over the medium term. The deterioration in economic outcomes and prospects is mainly due to the historically large adverse terms-of-trade shock in 2014. Oil exporters faced the largest real oil price decline since 1970—a decline that was unanticipated both in timing and magnitude, with real GDP for oil-exporting and other resource-intensive countries turning out to be significantly below earlier projections. At the same time, economic outcomes for non-resource-intensive countries have been broadly in line with projections, if not slightly better than expected, and baseline projections suggest continued strong growth over the medium term. Nevertheless, by 2023 more than half of sub-Saharan African countries won’t see a narrowing in their per capita income gap with the rest of the world. And as these countries are home to more than two-thirds of the region’s total population, it is imperative that the challenges they face be resolved if the region is to achieve its Sustainable Development Goals. Meeting these goals would require substantial investment in infrastructure, education, and health care, the financing of which hinges on the ability to spur joint efforts from national authorities, the donors’ community, and the private sector (Gaspar and others 2019).

The rest of this section considers the reforms required to strike a balance between continuing to invest in much-needed human and physical capital, keep public debt levels at manageable levels, and create conditions to generate jobs for some 20 million new entrants into the labor market each year.

Ensuring Macroeconomic and Financial Stability

Striking the right balance between addressing development needs and containing public debt levels.

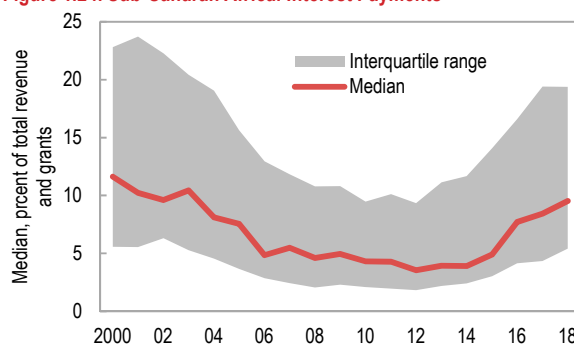
The reasons for the pronounced increase in public debt in many sub-Saharan African countries are generally country-specific. Some of the debt increase reflects efforts by countries to address much-needed human capital and infrastructure development needs at a time of easier global financial conditions. In other cases, the debt increase was unanticipated and instead reflected the adverse impact of the commodity price shock—in many cases, the impact of the 2014–16 commodity price slump on output (and public debt) was commensurate with that observed in the wake of the global financial crisis on many advanced and emerging market economies. And in other cases, the contributory factors to the public debt buildup have included the migration of contingent liabilities to the public sector balance sheet, sometimes reflecting losses by SOEs and valuation effects associated with exchange rate depreciations.

The concerns with the rising level of debt are threefold:

First, seven countries, mainly in fragile situations and/or hard-hit by the commodity price slump have found themselves unable to service their debt and thus needing to restructure it. This includes Chad, Mozambique, and the Republic of Congo.

Second, even where public debt remains at manageable levels, higher public debt is translating into higher debt service payments that are consuming a growing share of tax revenues. Debt servicing costs have increased sharply in sub-Saharan Africa, with the median interest payment burden doubling to about 10 percent of revenue since 2011 (Figure 1.24). This increase

Figure 1.24. Sub-Saharan Africa: Interest Payments



Source: IMF, World Economic Outlook database.

in debt service is due both to higher debt levels and a shift in the composition of debt. As official development assistance has declined in relation to recipient countries' GDP, and against a backdrop of increased fiscal space from debt relief, many countries in the region have turned to commercial and other nonconcessional sources to borrow to meet their development needs.

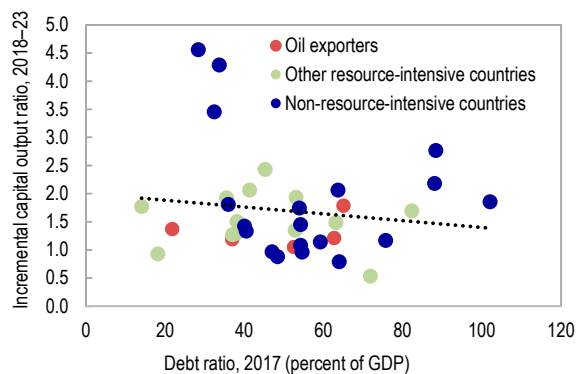
Third, the composition of public debt has become more complex in many cases. Of the US\$366 billion increase in debt between 2010 and 2017, about two-thirds was due to market borrowing (either from domestic financial systems and/or international capital markets) and thus subject to repricing risk; about 43 percent was in foreign currency and thus sensitive to exchange rate movements; and 13 percent was from bilateral creditors. Of course, the increased availability of alternative funding sources has also been helpful in some instances—for example, Côte d'Ivoire, Ghana, Kenya, Nigeria, and Senegal, have used favorable global financing conditions to improve the maturity structure of debt, replacing short-term debt with longer-term debt, thus reducing rollover risk.

These challenges highlight the need for fiscal policy to pay strong attention to avoiding an unsustainable debt buildup as well as strengthening debt management practices.

While debt ratios have gone up, the investment needs remain large, including in infrastructure, education, and health. To navigate these challenges and strike the right balance between meeting development needs and reducing debt vulnerabilities, the focus should be on:

- Ensuring efficient public investment. This requires improved project planning, allocation and implementation phases (IMF 2015a). In particular, it entails assessing the macroeconomic consequences and potential risks associated with alternative financing strategies, different public investment trajectories, and changes in investment efficiency. The appropriate trade-off between these two competing priorities clearly depends on country-specific circumstances and conditions, including financing modalities. The baseline projections assume higher efficiency in public investment for countries with high debt (Figure 1.25), but the case for ramping up infrastructure spending varies across countries based on needs, capacity, and fiscal space. Where debt dynamics are a serious cause for concern, the case for using fiscal savings to contain debt accumulation and rebuild fiscal buffers is stronger. Even so, rebalancing public spending away from nonessential recurrent spending and subsidies toward social and development spending could help provide space to advance development needs. Where infrastructure gaps are impeding growth and public investment management capacity is high, the case for using fiscal space for development purposes would be strong.
- Implementing growth-friendly fiscal policies. Multipliers of both public investment and consumption expenditure are significantly larger in countries where public investment is most efficient, and lower in countries where

Figure 1.25. Sub-Saharan Africa: Public Investment Incremental Capital Output Ratio and Public Debt



Sources: IMF, World Economic Outlook database; and IMF staff calculations.

Note: Sample excludes outliers and negative incremental capital output ratio. See Statistical Appendix for country groupings table.

it is less efficient (IMF 2017). In many cases, improving the composition and quality of spending requires decisive action to substantially cut low-priority capital expenditure and recurrent spending while protecting social outlays to mitigate the impact on the most vulnerable population. Efficiency improvements in goods and services (including reducing subsidies), payroll cleanup, and limits on nonwage compensation (as successfully done in Benin) could help contain recurrent spending while placing priority on social spending on health, education, and social safety nets. The region's growth potential could also benefit from growth-friendly fiscal policies. For example, simulations indicate that reducing income and gender inequality in the West African Economic and Monetary Union (WAEMU) could boost real GDP per capita by 0.5 percentage point on average and reduce the volatility of GDP growth.

- Stepping up revenue mobilization. With an average revenue gap estimated at 3–5 percent of GDP, all countries have significant room to raise revenue. And yet progress on domestic revenue mobilization has been elusive. Revenue advanced in 2018 by about 0.3 percent of GDP on average across countries, mainly on the back of higher-than-anticipated oil prices. This compares with an average increase in revenue (excluding grants) of 1¼ percent of GDP in past successful cases of revenue mobilization, which was mostly contributed by noncommodity revenue (Liberia, 2006–10; Mozambique, 2007–12; Rwanda, 2012–14; Senegal, 2001–03; Tanzania, 2005–07; Uganda, 2014–16). These successful episodes were based on improvements in revenue administration and tax policy reform (IMF 2018c). To increase the efficiency of the tax system and enhance tax administration, a number of countries are considering measures to broaden their tax base, such as introducing or reforming the value-added tax system (Angola, Senegal), bringing the informal sector into the tax net (Senegal), and reducing tax expenditures (Benin, Kenya)—including by streamlining tax exemptions and ensuring that those exemptions in place are granted through a rules-based transparent process.

- Improving economic efficiency and containing fiscal risks from SOEs. In the context of continued restructuring efforts, several countries have increased transparency by publishing findings of official reports on SOE performance (Cabo Verde, Cameroon, Ghana), strengthening and improving the governance of an SOE oversight agency (Angola, Ghana), auditing SOE governance and operations (The Gambia, Niger, Seychelles), updating the legal framework for SOEs (Cameroon, Guinea, Mozambique), and outsourcing SOE management (Guinea-Bissau). In some cases, an SOE restructuring program includes resolving insolvent SOEs (Angola) or possible privatization of nonstrategic SOEs (Angola, Cabo Verde, Chad, Ethiopia, South Africa).
- Reducing procyclicality of spending. Some countries plan to develop a fiscal rule to support transparent and prudent management of future oil revenue and move to a fiscal stabilization fund to help reduce the procyclicality of spending (Angola, Senegal, Uganda).
- Strengthening public financial management. The failure of existing systems and tight financing conditions is manifesting itself in large domestic arrears (Cabo Verde, Cameroon, Ghana, São Tomé and Príncipe, South Africa, Zambia), with attendant negative effects on growth and domestic financial systems. Enhancing the medium-term expenditure framework (Angola, Botswana), switching to the Treasury Single Account (Republic of Congo, Côte d'Ivoire), moving to performance-based budgeting (Botswana), and enforcing internal controls (Angola, Uganda) could help avoid misallocation of expenditure and smooth arrears management. Furthermore, improving capital project selection (Benin, Senegal, Seychelles, Tanzania) would enhance the efficiency of investment and reduce potential risks arising from SOEs and public-private partnerships (Seychelles).
- Improving debt management frameworks to better manage currency and rollover risks. A number of countries have used debt buybacks to ease near-term refinancing risks and reprofile external debt (for example,

Ghana's buyback of the 2022 Eurobond with proceeds from the 2018 Eurobond, which was also its first ever bond with a 30-year maturity) and to better align the repayment currency with foreign exchange earnings (Seychelles). To reduce bunching of external loan repayments, most countries have turned to multitranche Eurobond issuances. Nevertheless, caution is warranted as delayed buybacks with the Eurobond proceeds could result in unnecessary carry costs.

Strengthening the effectiveness of monetary policy

The monetary transmission mechanism in the region has strengthened, but there are large differences across countries. Empirical evidence suggests that the transmission mechanism is much stronger in countries where monetary authorities clearly communicate their policy objective, instrument, and strategy. Strengthened communication and transparency have helped reduce the frequency of surprise monetary policy decisions (Mozambique, South Africa). However, in recent years, a few countries (Kenya, Malawi, Nigeria) have witnessed a reversal of some of these gains. In those cases, central bank financing, redirecting bank lending toward government securities (Malawi), crowding-out effects (Nigeria), and lending rate caps that reduce the central bank policy rate's signaling effect (Kenya) have affected the transmission mechanism. In addition, concerns about access to credit and borrowing costs have led to populist pressures to introduce interest controls (Kenya, Malawi), with attendant adverse consequences on the availability of credit.

Enhancing the monetary transmission mechanism would require raising caps on interest rates; moving toward a more market-oriented monetary policy operating system and reducing fiscal dominance; improving secondary bond and interbank markets; reducing excess liquidity in banking systems through active use of open market operations; enhancing transactions in interbank markets, including by addressing concerns about counterparty risks, such as a new collateral mechanism for bank refinancing operations (CEMAC, WAEMU); and expanding the collateral framework to include all government securities (CEMAC, Botswana). Additional policy recommendations include

bringing short-term interest rates into positive territory in real terms and keeping them there (especially in Angola); narrowing the overnight interest rate corridor and establishing a symmetrical interest rate corridor with rates linked to the key policy rate; developing robust forward-looking frameworks for forecasting liquidity and managing inflation; and strengthening the independence of central banks.

Enhancing real exchange rate flexibility

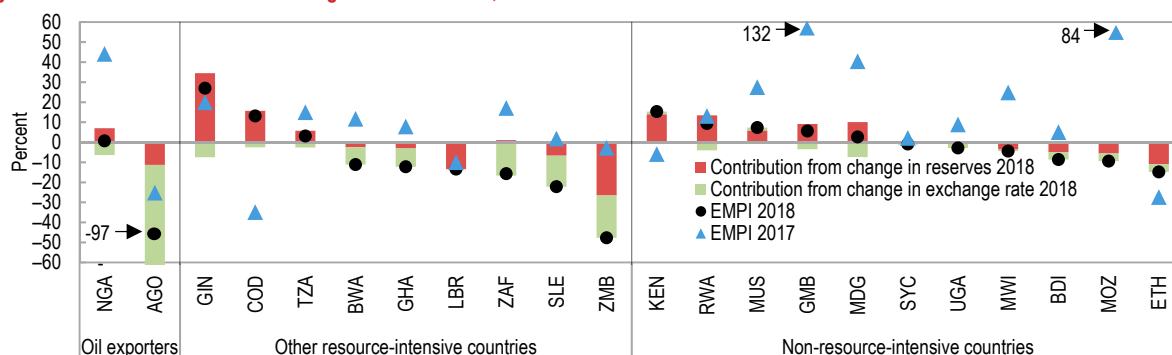
Lower external buffers have meant increased exchange rate pressures in some countries and have exacerbated foreign exchange shortages. This has translated into large premiums between official and parallel market exchange rates, particularly for oil exporters (Angola, South Sudan) (Figure 1.26) and a few other resource-intensive countries, such as Ghana. Countries have generally responded to market pressure by relying more on reserves than exchange rate flexibility. In part this reflects concerns about large foreign-currency-denominated liabilities, significant pass-through of exchange rate changes to inflation (estimated at about 40 percent), and limited responsiveness of output and exports to real exchange rate changes (owing to the small size of the manufacturing sector). Nevertheless,

further exchange rate flexibility, barring balance sheet vulnerabilities, as part of a broader product and labor market reform effort would enhance resilience and facilitate structural transformation. In countries with de jure fixed exchange rate regimes, such flexibility would mainly stem from relative price adjustments, and thus would require further structural reforms to enhance wage and price flexibility.

Securing financial stability

Several sub-Saharan African countries have tightened macroprudential policies to safeguard financial stability, including through restrictions on banks' foreign exchange positions, higher reserve requirements, and capital requirements (Angola, Ghana, Mozambique, Nigeria). Some countries are taking steps to reduce NPLs, including by strengthening creditor rights and reducing lengthy judicial processes in recovering collateral, halting net accumulation of public domestic arrears to the private sector (Equatorial Guinea), improving the credit information system, modernizing the insolvency regime, implementing financial education programs for medium-size corporates, and providing adequate safeguards to borrowers, including through customer protection measures.⁴

Figure 1.26. Sub-Saharan Africa: Exchange Market Pressure, 2017–18



Sources: IMF, International Financial Statistics database; and IMF staff calculations.

Note: The indicator of exchange market pressure index is the sum of the negative percent change in US dollar/local currency exchange rate plus the percent change in reserves. The changes are December to December of previous year. Negative values indicate pressure. EMPI = exchange market pressure index. See page vi for country abbreviations table and Statistical Appendix for country groupings table.

⁴ Many countries in the region have recently engaged in several initiatives to promote bank lending. Cabo Verde is considering providing partial guarantees on loans to small and medium-size enterprises; CEMAC plans to update the credit registry (though the initiative has been postponed until the end of 2020) and to have an operating credit bureau by early 2020; Guinea has operationalized a new credit information system to provide better information on customers' creditworthiness; Kenya is improving information from credit reference bureaus and has adopted a law on a movable collateral registry to expand the collateral available against bank lending; and Niger has strengthened the credit bureau through March 2018 legislation that obliges utilities to provide information about the payment discipline of their clients, and is preparing a law on "warrantage" (defined as granting credit with grain as collateral in secure warehouses).

Nevertheless, addressing persistent NPLs requires comprehensive NPL reduction strategies, including regulatory efforts to accelerate loss recognition, a stronger supervisory focus on recovery actions by banks and reforms of insolvency and debt enforcement frameworks to enable swift restructuring of the debt of distressed but viable borrowers, and support for the consistency and efficiency of judicial proceedings. Authorities could also establish permanent macroprudential buffers (on top of a microprudential minimum) that could be relaxed at the discretion of regulators in the event of shocks, thereby allowing NPLs to be absorbed by capital and for continued provision of credit.⁵

Sub-Saharan African countries have made progress in strengthening their banking sectors. CEMAC adopted a number of new regulations, including on the definition of systemically important institutions (in line with the Basel Committee recommendations), the accelerated resolution of small microfinance institutions, and a sound emergency liquidity assistance framework. WAEMU adopted new prudential rules aligned with the Basel II/III principles that should help consolidate banks' balance sheets and address vulnerabilities. Despite this progress, transitioning to the International Financial Reporting Standard 9 (IFRS 9) requires further strengthening banks' balance sheets, since the requirement to increase provisioning has meant raising further capital for many countries. Banks' compliance with IFRS 9 could have substantial macro-financial implications during the transition, including for credit growth and sovereign exposures, though it is too early to tell if the transition to IFRS 9 has had any such effect (Box 1.1).

The loss in correspondent banking relations is compounding financial sector challenges

A number of countries have responded to the loss of correspondent banking relationships (CBRs) by upgrading their anti-money-laundering/combating the financing of terrorism frameworks and other related legal and regulatory amendments in line with Financial Action Task Force standards (Angola, Seychelles). The decline in CBRs has resulted in a higher concentration in those relationships that remain, which carries a risk to financial stability

should any of the few remaining correspondent banks struggle to honor obligations. Looking ahead, ongoing reforms to strengthen the financial stability framework are expected to help reduce the risk of further loss of CBRs, especially through international capital adequacy requirements (Seychelles). In addition, countries are actively engaging with correspondent banks and their supervisors to better understand the specific reasons for the loss (Seychelles). There are various initiatives underway to help countries develop more sustainable frameworks, including at the multilateral level. For example, the IMF has established regional initiatives to facilitate policy dialogue and identify solutions to CBR issues, including a high-level workshop on CBR withdrawal for Southern African Development Community (SADC) countries in 2018 and three more events covering all of Africa planned for 2019. Some countries are also implementing a data monitoring framework (Angola, The Gambia, Seychelles) with some capacity support from the IMF.

Raising Medium-Term Growth

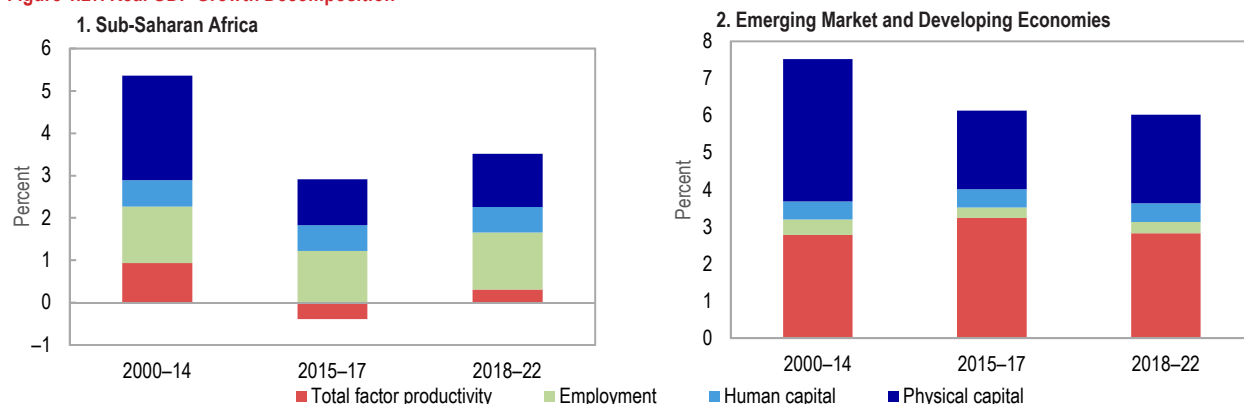
The region's medium-term growth prospects are held back by low productivity growth and limited physical capital accumulation, compared with countries at similar levels of development in Asia, developing Europe, and Latin America (Figure 1.27). Raising these growth prospects will require increasing productivity and promoting private investment and risk taking, including by deepening financial systems, while sustaining the gains will require making growth more inclusive.

Increasing productivity and enhancing the business environment

Increasing productivity will require enhancing the contestability of markets and nurturing a dynamic private sector. This in turn means removing the most salient constraints to business operations, especially access to reliable electricity provision, rent seeking, informal sector practices, security concerns, tax rates, and access to credit (Figure 1.28). Thus, measures aimed at leveling the playing field between public and private firms and between firms in the formal and informal sectors, improving governance, and fostering trade openness and integration could

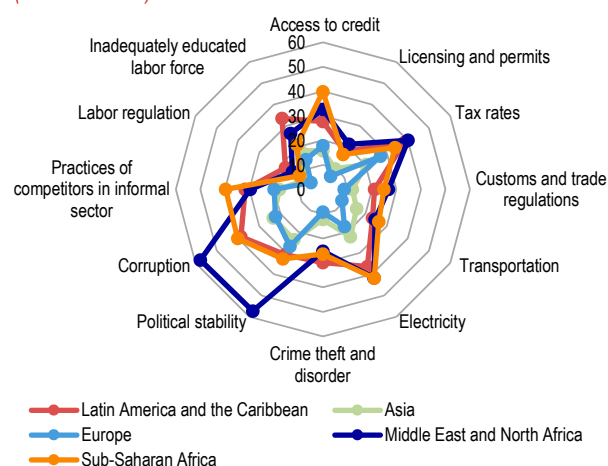
⁵ For more details, see IMF (2014 a, b).

Figure 1.27. Real GDP Growth Decomposition



Sources: IMF, World Economic Outlook database; Penn World Tables; and IMF staff calculations.

Figure 1.28. Selected Emerging Market and Developing Regions: Major Constraints to Business Operations (Percent of firms)



Source: World Bank, Enterprise Survey Data.

spur competition and help lift productivity.⁶ As shown in Chapter 3, further trade integration through the AfCFTA could significantly boost intra-African trade, foster competition, and increase efficiency. The growth impact would be positive, but relatively muted, amounting to an estimated 1 percent increase in GDP levels if tariffs are eliminated and nontariff barriers are halved.

Deepening financial markets

Deepening financial systems with improved provision of and access to financial services as well as increased efficiency requires improving financial regulation and supervision, and more broadly,

improving the relevant institutional environment. Such efforts could help enhance access to finance, particularly for small and medium-size enterprises, as firm-level survey data suggest that access to finance tends to be more constrained in economies with very high NPL ratios or severe corruption. Countries in sub-Saharan Africa have focused on strengthening controls and anti-corruption frameworks (Angola, Benin). Additional measures to deepen financial markets include promoting credit/collateral registries (Angola, Benin, Tanzania), enhancing financial literacy (Seychelles), developing regional capital markets, and leveraging fintech (for example, mobile money, see Box 1.2) for greater financial inclusion.

Equality of opportunities

Empirical evidence suggests that most of the return to capital in sub-Saharan Africa accrues to nonfinancial corporates (55 percent), while households receive the least (20 percent), and their share has been declining over time. Within corporates, those with high levels of state ownership seem to enjoy higher benefits, including greater access to credit. Within households, there has been some progress toward greater equity, with the share of income earned by the highest 20 percent of the income distribution declining⁷ and that of the “middle-income earners” increasing. This is consistent with a scenario in which there is a rising middle class with increasing opportunities to reap benefits from returns to capital. Despite these

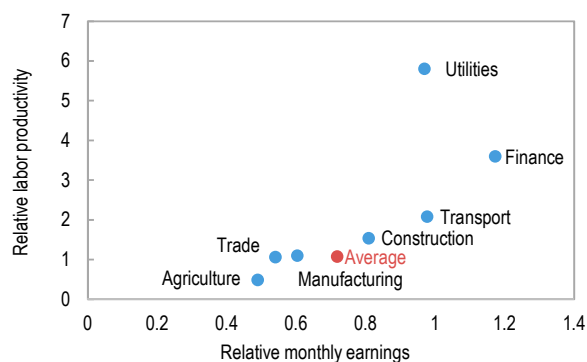
⁶ See IMF 2019a for a discussion on governance issues.

⁷ However, there are well-known underreporting issues for earners at the top of the income distribution.

improvements, however, there is scope to foster greater inclusion. Some 40 percent of people in sub-Saharan Africa still live on less than US\$1.25 a day, and the region has among the highest levels of gender inequality in the world. Addressing these challenges will require, in particular

- Facilitating the movement of labor toward other sectors than the government and agriculture to generate significant gains in efficiency (Figure 1.29).

Figure 1.29. Sub-Saharan Africa: Labor Productivity and Earnings Relative to Government Sector



Sources: Timmer, de Vries, and de Vries (2015); International Labour Organization; and IMF staff calculations.

Note: Weighted average.

- Fiscal reform, including domestic revenue mobilization and subsidy reform, to create space for transfer mechanisms targeted to the poor, and efficient spending on physical and human capital.
- Deepening financial systems with greater financial inclusion to help further reduce inequalities.
- Enhancing women’s participation in the economy, including by abolishing legal restrictions for women to open bank accounts or accept jobs, and addressing inequality in education (Box 1.3) to strengthen inclusivity of growth and growth potential.

These steps should be supported by measures to promote flexible education systems, while ensuring full enrollment with recourse to digital technologies to overcome existing bottlenecks.

Box 1.1. Transitioning to International Financial Reporting Standard 9

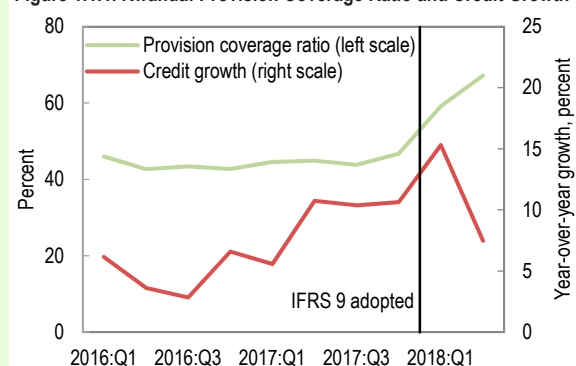
International Financial Reporting Standard (IFRS) 9, which changes the accounting rules for financial instruments, became effective worldwide in 2018. Adopting IFRS 9 is expected to provide more transparent disclosure of financial instruments, but banks would need to possibly increase provisions and possibly raise capital during the transition. Transitional arrangements, as introduced in some countries in the region, can help mitigate the potential impact on credit, while quantitative impact studies can help measure their severity.

Banks may need to increase loan loss provisions and raise capital, which is costly, during the transition to IFRS 9. IFRS 9 is used in about four-fifths of sub-Saharan African countries. While sectoral application of the standards differs across countries, banks are required to use IFRS 9 in many of them. Under the old standard (International Accounting Standard 39), provisions depended on actual incidences of default, implying that if a default had not occurred, banks did not have to take impairments. This implied a delayed recognition of credit losses in some cases, which was identified as a weakness of the old standard after the global financial crisis. Thus, the new standard, IFRS 9, intends to ensure that the credit risk of financial assets is assessed based on a forward-looking “expected credit loss” framework. This means that provisions are based on the likelihood of a default and potential losses. Overall, IFRS 9 is expected to provide more transparent disclosure of financial instruments. However, banks may need to raise regulatory capital due to increased provisions during the transition to IFRS 9, which is costly.

The modalities of the transition to IFRS 9 for banks vary across sub-Saharan African countries. In order to mitigate the potential impacts of IFRS 9 on capital positions, some authorities responded by allowing banks to adjust their capital over an extended period (for example, for three years in South Africa, four years in Rwanda and Nigeria, and five years in Kenya). Some authorities took a further step by setting the provisioning for government securities at zero (Rwanda).¹

There is a concern that adopting IFRS 9 could have adverse macro-financial impacts during the transition period, including downward pressure on credit growth. A quantitative assessment of the impact of the move to IFRS 9 on South African banks found a 39 percent increase in credit impairment but no breaches of capital adequacy ratios (SARB [2018]). In Rwanda, the provision coverage ratio has been on an increasing trend since the adoption of IFRS 9, and credit growth remains lower than the 2017 average (Figure 1.1.1). That said, the causality from IFRS 9 adoption to credit growth has so far been hard to establish (particularly given transitional arrangements). Further work by supervisors in the region will be needed to achieve compliance with the new global standard while avoiding an excessive impact on banks’ ability to lend.

Figure 1.1.1. Rwanda: Provision Coverage Ratio and Credit Growth¹



Source: IMF, Financial Soundness Indicators.

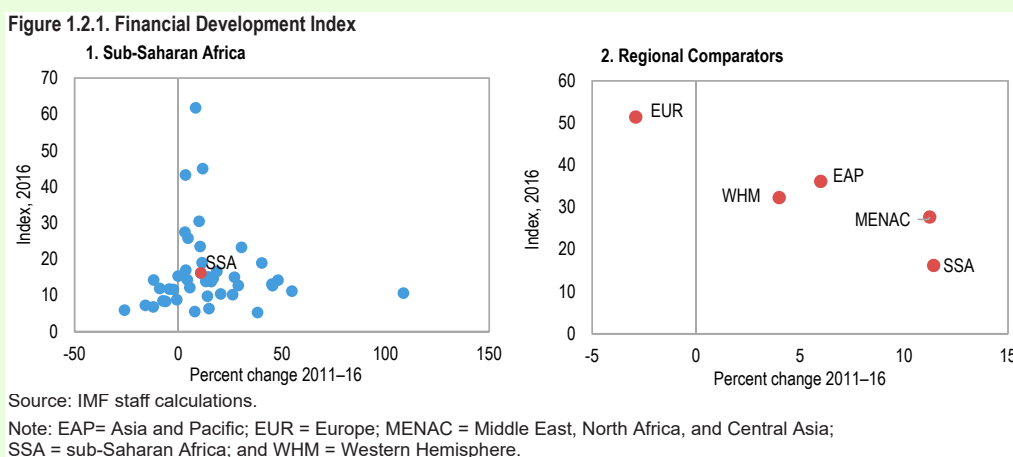
¹ Credit refers to total gross loans.

This box was prepared by Seung Mo Choi and Amadou Sy.

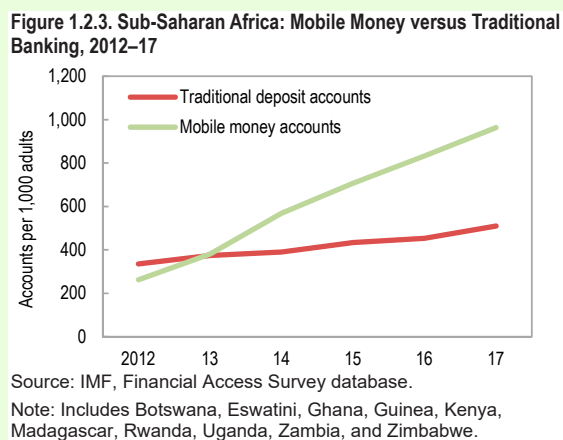
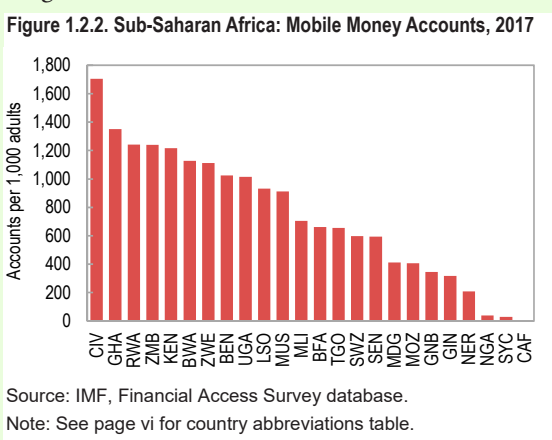
¹ However, setting the provisioning for government securities at zero could distort banks’ decision to allocate assets.

Box 1.2. Financial Development and Mobile Money Growth in Sub-Saharan Africa

*Financial development—excluding mobile money transactions—has grown faster in sub-Saharan Africa than in other regions, but its overall level continues to trail that of other economies.*¹ Progress in financial development differs across countries, with faster growth among countries that started off with lower financial development (Burkina Faso, Chad, Democratic Republic of the Congo, Republic of Congo, Côte d’Ivoire, Gabon, Sierra Leone, Togo). Overall, during 2011–16, the pace of development in financial markets has far exceeded that of financial institutions, albeit starting from a low base. Financial markets benefited primarily from deepening in the stock and bond markets, while financial institution development was propelled by improved access to banking sector infrastructure (branches and ATMs). Sub-Saharan African countries outperformed comparator regions in Asia and the Middle East and central Asia in these categories but trailed in financial deepening of banking and nonbanking sectors (Figure 1.2.1).



Usage of mobile money accounts has continued to surge at a faster pace than in other regions. Indeed, mobile money accounts have surpassed traditional deposit accounts in sub-Saharan African (IMF 2019a) (Figures 1.2.1 and 1.2.2).



This box was prepared by Amadou Sy and Torsten Wezel based on findings from IMF (2019b).

¹ Financial development is measured by the Financial Development Index, which encompasses financial institutions—banking and nonbanking—as well as markets across three dimensions: depth, access, and efficiency (Sahay and others 2015).

East Africa, which has the highest mobile money usage in sub-Saharan Africa, offers useful lessons as it developed an infrastructure that uniquely built on the latent demand for mobile financial services in the region

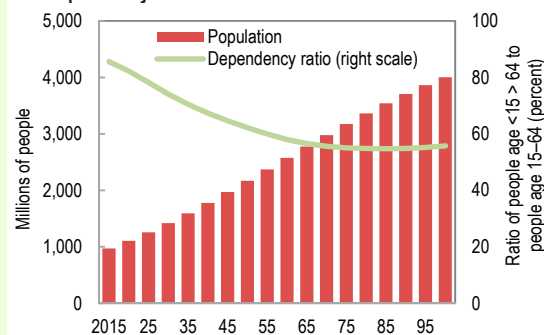
- East African countries favored a telecom-led regulatory model. In this framework, the telecom provider works with the financial regulator to establish the infrastructure for mobile payments. The telecom-led model has proved more successful in attracting users than the bank-led model that other sub-Saharan African countries promoted.
- East African countries tended to have a dominant telecom provider with a large market share, which provided an initial critical mass of users needed to push mobile money past the niche level. In Kenya, Safaricom has a share of nearly 70 percent of the market; in Tanzania, Vodacom has a market share of close to half. Having a large market share allowed most mobile payment users to operate on a single platform without facing compatibility issues, though this raises concentration and potential stability concerns. Mobile money interoperability is increasingly allowing transactions between users of different service providers.
- East African countries, particularly in the East African Community, have national identification systems. These systems facilitate faster mobile payment adoption rates and enable more secure transactions.

Box. 1.3. Sub-Saharan African Demographic Trends and Gender Gaps in Education

Sub-Saharan Africa's population is growing rapidly, presenting an opportunity for a demographic dividend. The region's population could double in the next three decades, and quadruple by the end of the century (Figure 1.3.1). The large entry of young people into the labor force is associated with a decline in the dependency ratio as fertility rates are expected to decline from current levels. This declining dependency ratio presents a large opportunity for the region. Indeed, many developing economies in south and east Asia that saw their dependency ratios decline witnessed a demographic dividend and rapid growth (IMF 2015b; Aiyar and Mody 2011). However, for the region to harness its demographic dividend, declining dependency ratios are not sufficient but need to be complemented by creating jobs to absorb new entrants into the labor market and scaling up human capital through improvements in health and education to ensure that new workers enter the labor market at higher wages and into higher-productivity employment.

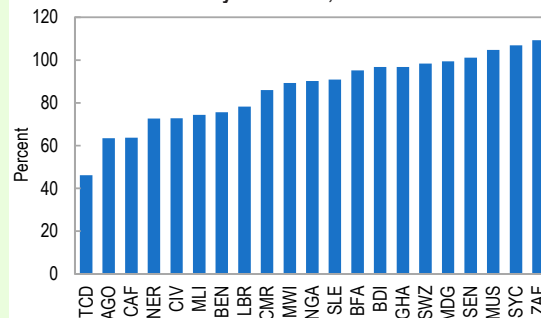
Scaling up human capital to support growth will require closing gender gaps in education which requires work on several margins. While gender gaps in education have narrowed substantially in many countries, some still see fewer than three girls enrolled in secondary education for every four boys in some sub-Saharan African countries (Figure 1.3.2). Higher public spending on education is part of the solution. Better infrastructure, in particular, improvements in sanitation facilities and women's health, and in some cases raising the legal age of marriage for men and women, are other factors that are associated with narrower education gaps across all developing economies (Jain-Chandra and others 2018). These policies should be complemented by measures to level the playing field for economic participation by women, including in the context of rapid technological advances, including automation. Overall, such measures would level the playing field between women and men and could result in higher productivity growth and stability gains (Cuberes and Teignier 2016; Sahay and Cihak 2018).

Figure 1.3.1. Sub-Saharan Africa: Projected Population Size and Dependency Ratio



Source: United Nations Population Division.

Figure 1.3.2. Selected Sub-Saharan African Countries: Ratio of Female-to Male Secondary Enrollment, 2016



Source: World Bank, World Development Indicators.

Note: See page vi for country abbreviations table.

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