

# Op-Ed on Regional Economic Outlook for Sub-Saharan Africa

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### **Sub-Saharan Africa growth remains strong, but challenges lie ahead**

The global economy faces significant uncertainty and growth prospects remain weak. Yet, Sub-Saharan Africa continues to perform strongly, with economic growth expected to exceed 5 percent this year and next. This resilience was already in evidence 2008–09, when the global economy experienced its deepest recession since the 1930s, while notably low-income countries fared much better than they had during past global downturns. Ample policy space, resulting from prudent policies over the preceding decade as well as comprehensive debt relief, helped many countries to respond counter-cyclically by allowing fiscal deficits to widen. This helped protect critical spending: most countries were able to increase spending on infrastructure, health, and education. Strong growth in emerging markets, growing trading partners for many countries in Sub-Saharan Africa, also helped cushion the impact of the recession in traditional partner countries.

Will Africa prove to be as resilient now? Considerable challenges face the global economy. The euro zone is exposed to fiscal and financial stress, the United States contemplates the risk of a sharp fiscal tightening, and now even emerging countries like China face a growth slowdown. IMF estimates suggest that a sustained global slowdown of 2 percentage points of GDP would reduce growth in Sub-Saharan Africa by 1 percentage point per year. Moreover, many Sub-Saharan African countries continue to face local challenges. Droughts remain a risk for many countries, with potentially dire consequences for food prices. The recent surge in security tensions in West Africa also contributes to economic risks. Security risks are critical as they not only disrupt economic activity where they occur, but also spill over to neighboring countries.

### **The region will be able to manage these challenges with prudent policies**

The successful management of the 2008–09 crisis came at a cost. Debt levels were low, but have increased since, albeit moderately. Deficits are also wider. Many countries retain some space to respond flexibly to shocks, and where such room remains, it should be used. But clearly the space has shrunk. And financing sources may also be less ample. Development assistance is at risk from tighter budgets in advanced economies. Market financing, which is increasingly available to African economies, may also dry up suddenly should the world face a sharp economic downturn.

Therefore, prudence suggests that where growth continues to hold up, fiscal space should be rebuilt, ahead of those new risks. Several options exist. For example, many countries maintain costly energy

subsidies (averaging 4 percent of GDP in Sub-Saharan Africa). Such subsidies are not only costly, crowding out other public spending on infrastructure or health and education, they are also inefficient, stifling growth by providing a disincentive to maintenance and investment in energy generation, which is vital for Africa's future growth performance. Many countries also have scope for raising additional revenue, notably from natural resources.

In the case of Ethiopia, where robust growth has been maintained, a prudent policy framework needs to address current macroeconomic imbalances, reflected by continued high inflation, while building up foreign exchange reserves that currently are only at about 2 months of imports. This will require a tight monetary policy stance and a pacing of the planned scaling up of public investments in line with the availability of noninflationary financing. Fiscal space (or savings) should be expanded, including by strengthening tax collections. In this respect, the ongoing efforts to improve tax administration should assertively continue and considerations should be made to modify existing costly tax incentive for investment schemes.

### **Africa's long term prospects remain strong**

The world economy may face a prolonged period of uncertainty and weakness. But Africa's long term prospects remain strong. Many countries, including Ethiopia, are enjoying a prolonged period of robust growth. Investment is increasing, raising future economic potential. And new discoveries of natural resources combined with still-high commodity prices bring new growth opportunities. The key will be to seize these opportunities. Recent IMF studies show that economic transformation, whereby rising agricultural productivity releases labor for a developing manufacturing sector, is much slower in Africa than it was in Asia. And the importance of extractive industries in many African countries, which often generate less employment than basic manufacturing, has meant that growth has been less inclusive than desirable. These are important challenges that needed to be addressed. Infrastructure development will have important positive spill-overs, also for the agricultural sector; investments in education and health will build human capital to take advantage of Africa's young labor force; accelerated regional integration will create larger markets and offer economies of scale for investors; and improving the business environment will attract foreign investment and capital, progressively reducing aid dependency. None of these will happen automatically. But strong policy making, as we have increasingly seen across the African continent, will continue to be a powerful force for change.