Navigating Uncertainty
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Navigating Uncertainty
OCTOBER 2019

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Governor, Reserve Bank of Malawi, Dr Dalitso Kabambe and IMF Res Rep
Dr. Farayi Gwenhamo
Roadmap

- Recent Developments and Outlook
- Macro Policies and Structural Reforms
- Response to Downside Risks
SSA growth remains bifurcated, with non-resource intensive countries outpacing resource-rich ones

Real GDP per Capita, 1990–2024

Source: IMF World Economic Outlook database.
Wide heterogeneity in growth outlook will persist in 2020, including among the largest economies

Real GDP Growth Distribution, 2020

Source: IMF World Economic Outlook database.
Global developments pose significant downside risks to growth

Export Growth, 2014–19

Source: IMF, Direction of Trade Statistics.
In Malawi, however, export growth is volatile

Export growth for Malawi, 2010-2019
Inflation has stabilized, converging to regional averages

![Inflation Graph]

**Headline Inflation**

- Malawi
- Rwanda
- Kenya
- Uganda
- Tanzania
- Zambia
Relative to April, growth was revised down in about 2/3 of SSA countries

Downward Revision of WEO Projections for Current Year (Oct. vs Apr.)

Source: IMF World Economic Outlook database.
In per capita terms, some 25 countries will continue to converge, but another 20 countries lag behind

Sub-Saharan Africa: Real GDP and Real GDP per Capita Growth, Average 2019–24 (size of the bubble reflects population)

Source: IMF, World Economic Outlook.
Roadmap

▪ Recent Developments and Outlook
▪ **Macro Policies and Structural Reforms**
▪ Response to Downside Risks
Implementing fiscal consolidation plans should stabilize or lower debt ratios

Public Debt to GDP, 2012-2024
Efforts to enhance fiscal data provide better assessment of arrears

Stock of Domestic Arrears in SSA Countries, 2005–18
Promoting competition can lift medium-term growth and improve welfare

**Competition and Macroeconomic Performance**

- Growth
- Private investment
- Non-oil exports
- Labor productivity growth

**Impact of Competition on Prices**

- Clothes and footwear
- Health services
- Food and beverage
- Individual consumption

Sources: IMF staff calculations.
Roadmap

▪ Recent Developments and Outlook
▪ Macro Policies and Structural Reforms
▪ Response to Downside Risks
Response to shocks depends on their nature and strength of balance sheets and fundamentals

Baseline

- Implement planned fiscal consolidation
- Room to ease monetary policy where inflation is running low

Shocks

- Fast growing countries with elevated debt vulnerabilities should focus on rebuilding buffers
- Slow growing countries should seek more gradual adjustment, if financing is available, and fine-tune its composition to minimize impact on growth
Thank You
Key messages

Product market competition in sub-Saharan Africa is low
► More than 70 percent of SSA countries are below the world’s median competition indicator
► Firm markups are 11 percent higher than in other emerging markets and developing countries

Enhancing competition can help improve economic performance
► It is associated with an increase in the rate of growth of real GDP per capita by about 1 percentage point, driven by a boost to productivity growth and export competitiveness
► Helps to significantly lower product prices, improving welfare and competitiveness
► At the firm level, it is associated with an increase in investment, exports, productivity growth, and the labor’s share in output

Improving competition requires a holistic approach that encompasses…
► An effective competition policy framework
► Trade and investment liberalization
► Reduction in regulatory and structural barriers, including trade and investment liberalization
► Complementary fiscal and other macroeconomic policies
Roadmap

- **Product market competition in SSA**
- **Gains from increased competition**
  - Growth and welfare
  - Firm performance
- **How to improve competition**
  - Competition framework
  - Complementary policies
Product market competition in sub-Saharan Africa is low

Product Market Competition, 2007-17

Source: World Economic Forum, Global Competitiveness Index.
But there is considerable heterogeneity across countries

Product Market Competition in sub-Saharan Africa, 2007-17

**By resource intensity**

<table>
<thead>
<tr>
<th>By resource intensity</th>
<th>Average 2013–17</th>
<th>Average 2007–12</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oil exporters</td>
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<td>Other resource-intensive</td>
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**By region**

<table>
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<tr>
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<th>Average 2007–12</th>
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<tbody>
<tr>
<td>Central Africa</td>
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<td>West Africa</td>
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<td>Central Africa</td>
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<tr>
<td>West Africa</td>
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</tr>
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</table>

Source: World Economic Forum, Global Competitiveness Index.
High profitability and markups, and rising in some major economies

**Firm-level competition indicators**

- Emerging market economies and developing countries (excl. SSA)
- Sub-Saharan Africa

**Firm Markups**

Sources: World Bank Enterprise Survey and Orbis.

Sources: Orbis database.
Competition is weaker across nearly all sectors, especially in non-tradables.

**Firm markups by sector**

- Sub-Saharan Africa
- Emerging market economies and developing countries (excl. SSA)

**Source:** World Bank Enterprise Survey.

**Economic Competition in SSA**

- Gains from increased competition
- How to improve competition

**Source:** Orbis database.
Roadmap

- Product market competition in SSA

- **Gains from increased competition**
  - Growth and welfare
  - Firm performance

- How to improve competition
  - Competition framework
  - Complementary policies
Sub-Saharan Africa is likely to benefit significantly from enhanced competition

Effects on Macroeconomic Performance

Sources: IMF Staff calculations.
Increasing competition helps to lower prices, improving welfare and competitiveness

**Gains from increased competition**

- How to improve competition

**Sources:** World Bank, International Comparison Program.

**Price differentials with other countries**

- **Effects of increased competition on prices**

**Sources:** IMF Staff calculations.

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**Percent**

- Advanced economies
- Developing countries excl. SSA
- Emerging market economies

**Category**

- Food and beverages
- Clothes and footwear
- Health
- Individual consumption basket

**Percent**

- 0
- 10
- 20
- 30
- 40
- 50
- 60

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**Category**

- Clothes and footwear
- Health services
- Food and beverage
- Individual consumption

**Percent**

- 0
- 10
- 20
- 30
- 40
- 50

---

*Note:*** indicates statistical significance at the 1% level; ** indicates statistical significance at the 5% level; * indicates statistical significance at the 10% level.*
Lower firm markups are associated with higher firm investment, exports, and labor share in output...

**Effects on Firms’ Behavior**  
(World Bank firms data)

![Graph showing the relationship between firm markups and various firm behaviors in Sub-Saharan Africa and emerging market economies and developing countries](image)

- **Investment to value added**
- **Exports to value added**
- **Labor share to value added**

Sources: IMF Staff calculations.
And also with higher growth of labor productivity and total factor productivity

**Effects on Firms’ Behavior**
(Orbis firms data)

![Graph showing effects on firms' behavior with Sub-Saharan Africa and Emerging market economics and developing countries.]

Sources: IMF Staff calculations.
Roadmap

- Product market competition in SSA
- Gains from increased competition
  - Growth and welfare
  - Firm performance
- How to improve competition
  - Competition framework
  - Complementary policies
The momentum of product market reforms appears to have slowed down in the last decade.

Structural Reforms, 1973-2014

Index

Sources: IMF Staff calculations.
Despite competition laws and agencies, improvement in the state of competition has been limited.

Sources: World Economic Forum, Global Competitiveness Index.

Anti-monopoly Enforcement

Sources: World Economic Forum, Global Competitiveness Index.
A holistic approach is needed to improve competition, encompassing:

An effective competition policy framework including:

► An adequate competition law backed by an independent and well-resourced competition authority

Product market reforms to reduce structural and regulatory barriers to business activity

Trade and foreign investment liberalization policies

► To bolster foreign competition

► Improve access to intermediate inputs

Supportive fiscal policy framework

► Fiscal policies, tax administration and procurement systems should not benefit a few market players

Greater cooperation among national competition authorities in the region to tackle cross-border anti-competitive practices
Policies tend to be mutually reinforcing

- Trade and investment liberalization help to stimulate competition…
- But concerns about increased foreign competition hurting the domestic industry and creating dominant firms can be mitigated by implementing an appropriate competition policy framework.
- Development policies to foster sectors deemed essential to boost productivity and growth should not lead to increased market power that would go against the goals of the original policies.
- More generally, countries need to maintain a stable and sound macroeconomic and institutional environment to attract private investment and ensure that policies to stimulate competition have traction.
Malawi Experiences: Institutional Arrangements are in place...

Competition and Fair Trading Commission (CFTC) legislated by the Competition and Fair Trading Act:

Anonymous agency of government with a mandate to regulate, monitor, control, and prevent anti-competitive practices

- Regulation of mergers and acquisitions of companies
- Monitoring monopolies and concentrations of market power and taking corrective action against abuse of dominance
- Prohibiting anti-competitive practices by enterprises against each other
- Protecting consumers from unfair trading practices
Malawi Experiences: Outcomes

➢ Is the institutional framework robust?

➢ Are the levels of competition in Malawi’s key sectors/markets (e.g. energy and agricultural sectors) conducive for:
  ➢ Efficiency
  ➢ Productivity
  ➢ Entrepreneurship
  ➢ Growth
Key messages

Product market competition in sub-Saharan Africa is low
- More than 70 percent of SSA countries are below the world’s median competition indicator
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Enhancing competition can help improve economic performance
- It is associated with an increase in the rate of growth of real GDP per capita by about 1 percentage point, driven by a boost to productivity growth and export competitiveness
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- An effective competition policy framework
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Thank You
Domestic Arrears in SSA: Size, Symptoms, and Cures

OCTOBER 2019

Regional Economic Outlook
Why we should care (1)

Domestic arrears are significant in SSA

- 70 percent of sub-Saharan African countries report domestic arrears

- Sub-Saharan Africa has the lowest PEFA (Public Expenditure and Financial Accountability) score for the domestic arrears

Source: PEFA 2016 methodology; and IMF staff calculations.
Why we should care(2)

Domestic arrears have detrimental macroeconomic effects

- Despite the prevalence of arrears, their causes and effects are not well-understood
- The literature on domestic arrears is very limited
- Their true scale and cost may be hidden
- Little operational guidance exists as to the best practices on arrears clearance

Sources: IMF staff calculations..
Key messages

Domestic arrears are prevalent in sub-Saharan African countries and have increased in recent years

► Most SSA countries officially report expenditure arrears, but also have “unrecognized” arrears
► After declining steadily in the late 2000s, arrears have increased recently

They have widespread macroeconomic, financial and social consequences

► They negatively affect the private sector
► Arrears accumulation can lead to stress in the banking system
► They undermine trust in government and the effectiveness of fiscal policy

Country authorities should make every effort to clear existing arrears and prevent arrears accumulation

► A clearance strategy entails three main steps: verification, payment and prioritization strategy, and repayment
► Preventing the accumulation of arrears requires a combination of PFM reforms, sound fiscal policy, and political commitment
Roadmap

- Stock taking of domestic arrears in SSA
- Causes of domestic arrears accumulation
- Macroeconomic effects of domestic arrears
- Cures: clearance and prevention of domestic arrears
**Dataset**

**Challenges**
- No existing database on domestic arrears
- Absence of standardized definition and coverage of public sector

**Staff approach to collect data**
- Survey among IMF African Department desk economists (30 countries)
- Supplemented with information from IMF Staff Reports
- Cross-checked against data included in public expenditure and financial accountability assessments (PEFA)

**Looking ahead**
- More work needed to build a comprehensive database, based on more regular and methodical reporting and better monitoring systems across the region
Stock taking of domestic arrears in SSA (1)

A majority of SSA countries report domestic arrears

Share of Countries with Recorded Domestic Arrears in Sub-Saharan Africa, 2018

Sub-Saharan Africa: Stock of Domestic Arrears by Country Group, 2018

Percent of GDP

Sources: IMF staff calculations..
Stock taking of domestic arrears in SSA (2)

Domestic arrears have increased since 2013 in SSA, especially in oil-exporting countries

Stock of Domestic Arrears in Sub-Saharan Africa, 2005–17

Sub-Saharan Africa: Frequency of Domestic Arrears-Related Terms in IMF Staff Reports, 2005–17

Sources: IMF staff calculations.
Stock taking of domestic arrears in SSA (3)

Arrears to private suppliers of goods and services are the most common

1. Domestic Arrears by Spending Category

- Compensation of employees
- Acquisition of goods and services
- Transfers
- Acquisition of nonfinancial assets

2. Domestic Arrears by Economic Agent

- Private sector suppliers
- Government employees
- SOEs
- Sub-national governments
- Statutory funds
- Others

Source: Survey of IMF African Department desk economists.
Roadmap

- Stock taking of domestic arrears in SSA
- Causes of domestic arrears accumulation
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- Cures: clearance and prevention of domestic arrears
Causes of arrears accumulation (1)

Countries accumulate expenditure arrears due to both structural and cyclical factors

Structural causes include weak fiscal and PFM institutions, notably:

- The formulation of unrealistic budgets
- A lack of commitment controls
- Poor cash management
- Delays in processing payments

Cyclical factors are primarily those that adversely impact government resources like:

- Economic downturns
- Commodity price shocks
- Internal shocks such as conflict and political instability
Causes of arrears accumulation (2)

The stock of domestic arrears is negatively associated with governance indicators

Sub-Saharan Africa: Selected Governance Indicators and Stock of Domestic Arrears, 2005–18

Sources: IMF staff calculations.

Stock taking of domestic arrears in SSA

Causes of domestic arrears accumulation

Macroeconomic effects of domestic arrears

Cures: clearance and prevention of domestic arrears
Causes of arrears accumulation (3)

Large domestic arrears accumulate following fiscal shocks

Sources: IMF staff calculations.
Causes of domestic arrears accumulation (4)

Large domestic arrears accumulate following fiscal shocks

Causes of Domestic Arrears Accumulation: Regression Output

- Regression analysis indicates that lower growth, a decline in the commodity terms-of-trade, and political instability are associated with a larger stock of domestic arrears.

Sources: IMF staff calculations..
Causes of arrears accumulation (5)

Large domestic arrears accumulate following fiscal shocks

Oil shocks seem to have a larger impact for:
- countries under fixed exchange rate regimes
- countries with weak indicators of governance

Sources: IMF staff calculations..
Roadmap

- Stock taking of domestic arrears in SSA
- Causes of domestic arrears accumulation
- Macroeconomic effects of domestic arrears
- Cures: clearance and prevention of domestic arrears
Macroeconomic impact of domestic arrears (1)

- **Real sector**
  - Lower corporate profit
  - Reduced household income
  - Weaker fiscal multiplier

- **Financial sector**
  - Liquidity shortages
  - Deteriorating asset quality
  - Lower credit to the economy

- **Poorer social outcomes**
  - Erosion of trust in government
  - Weaker tax payment discipline
  - Corruption vulnerabilities

- **Second-round fiscal effects**
  - Higher deficit
  - Constrained fiscal space

**Adverse effects on:**
- Employment, investment and growth
- Financial sector health
- Public service delivery
- Debt sustainability
### Domestic arrears undermine macro outcomes

Macroeconomic Impact of Domestic Payment Arrears: Regression Output

<table>
<thead>
<tr>
<th>Variable</th>
<th>Regression Output</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP per capita growth</td>
<td>-0.331 ***</td>
</tr>
<tr>
<td>NPLs to total gross loans</td>
<td>0.323 *</td>
</tr>
<tr>
<td>Tax revenue (percent of GDP)</td>
<td>-0.213 *</td>
</tr>
<tr>
<td>Access to electricity (percent of population)</td>
<td>-0.589 **</td>
</tr>
<tr>
<td>Firms' sales growth</td>
<td>-4.68 ***</td>
</tr>
<tr>
<td>Firms' employment growth</td>
<td>-2.54 *</td>
</tr>
<tr>
<td>Firms' productivity growth</td>
<td>-5.43 ***</td>
</tr>
</tbody>
</table>

**Sources:** IMF African Department Desk Survey; Financial Soundness Indicators; World Bank Enterprise Surveys; World Development Indicators; World Economic Outlook database; and IMF staff calculations...
Macroeconomic impact of domestic arrears (3)

Higher levels of arrears are associated with lower citizens’ trust

1. Trust in President/Prime Minister: Not at All
2. Governments’ Management of the Economy: Very/Fairly Well
3. Corrupt Tax Officials: All of Them
4. Access to Medical Care: Very Difficult

Sources: Afrobarometer; IMF African Department Desk Survey; and IMF staff calculations.
Macroeconomic impact of domestic arrears (4)

Domestic arrears reduce the fiscal multiplier

Fiscal multiplier in the presence of government domestic arrears

Fiscal multiplier in the presence of government domestic arrears and liquidity constrained private sector

Fiscal multiplier in the presence of large accumulation of domestic arrears and liquidity constrained private sector

Source: IMF staff calculations.

Domestic arrears reduce the fiscal multiplier.
Roadmap

- Stock taking of domestic arrears in SSA
- Causes of domestic arrears accumulation
- Macroeconomic effects of domestic arrears
- **Cures: clearance and prevention of domestic arrears**
Cures: clearance and prevention of arrears (1)

Essential elements of a clearance strategy

**Guiding Principles**

- Full transparency to address governance concerns.
- Prioritization guided by the impact on macro stability and inclusive growth.
- Prevention requires a combination of PFM reform, sound fiscal policy, and political commitment.

**Steps**

- Stocktaking and auditing of arrears
- Development of a repayment strategy
- Repayment

Stocktaking of domestic arrears in SSA

Causes of domestic arrears accumulation

Macroeconomic effects of domestic arrears

Cures: clearance and prevention of domestic arrears
Cures: clearance and prevention of arrears (2)

Repaying Arrears – Stylized Decision Tree

Assessment of available financing and debt sustainability

Financing available and debt sustainable

Financing constraints/concerns about debt sustainability

Fiscal adjustment and/or concessional external financing

Assessment of macroeconomic impact

Internal/external stability concerns

No

Yes

Not feasible

Impact on financial stability and macroeconomy

Repayment of arrears

Repay

Reprofile

Restructure

Stock of arrears

Feasible

Source: IMF staff calculations.
Cures: clearance and prevention of arrears (3)

Preventing Arrears Accumulation

- Strong Political Commitment
  - Public Financial Management Reform
    - Credible budgeting
    - Strong commitment and expenditure controls
    - Adequate Liquidity Management
  - Sound Fiscal Policy
    - Build buffers if susceptible to shocks (commodity exporters)
    - Diversify revenue sources
    - Adopt appropriate fiscal rule
Thank You