From:
African Economic Outlook 2011
Africa and its Emerging Partners

Access the complete publication at:
http://dx.doi.org/10.1787/aeo-2011-en

Executive Summary

Please cite this chapter as:

OECD, *et al.* (2011), "Executive Summary", in *African Economic Outlook 2011: Africa and its Emerging Partners*, OECD Publishing.
http://dx.doi.org/10.1787/aeo-2011-2-en

Executive Summary

Africa´s economies have weathered the global economic and financial crisis relatively well and have rebounded in 2010. The continent is expected to continue on its path of recovery although serious headwinds weigh on the momentum for expansion in 2011, notably the political events in North Africa and the high fuel and food prices. The dismal situation in Libya and Côte d´Ivoire shows once again how citizens suffer and economies are brought to a halt when political transitions are not pursued in a peaceful way.

Part I of this year's *African Economic Outlook* analyses Africa's macroeconomic and structural developments. It examines how the African continent, its regions and countries, have fared during the global crisis and forecasts economic developments in 2011 and 2012. It describes changes in external financial flows and discusses trade policies and measures to foster regional integration. Furthermore, it discusses why poverty reduction has remained relatively slow in Africa and characterises the status and trends of human development.

Part II explores the relationship between Africa and its emerging partners and casts new light on the impacts for Africa´s development.

Africa's Performance and Prospects

Macroeconomic Prospects

Africa´s economies have rebounded from the slump which had been caused by the global recession. In 2010, *Africa´s average rate of growth* amounted to 4.9%, up from 3.1% in 2009. The political events in North Africa are likely to depress the continent's growth to 3.7% in 2011. However, this forecast is surrounded by considerable uncertainty. Risks are related to the global economy, notably the impact of the earthquake and nuclear crisis in Japan, and to Africa, in particular the development in Libya and Côte d´Ivoire and how this affects neighbouring countries. With the assumption that economic normality returns in these countries, Africa´s average growth is expected to accelerate to 5.8% in 2012.

North Africa is expected to be the only region with lower growth in 2011 compared to the previous year (less than 1% after 4.6% in 2010). Under the assumption of a return to normal economic life, growth of the region is expected to rebound again in 2012. *East Africa* is likely to continue on its growth path of above 6% during the projection period, while growth in West Africa is expected to decelerate to below 6% due to the events in Côte d´Ivoire. In Southern Africa and in Central Africa growth is projected to accelerate, but remain lower than in East and West Africa.

Monetary policies are expected to gradually tighten to respond to inflation concerns related to higher food and energy prices. But, as in most countries, underlying inflationary pressures are expected to remain subdued; there is no need for vigorous tightening. Policies should focus more on core inflation and inflation expectations rather than on the temporary increase of headline inflation.

Africa´s average *fiscal deficit* is expected to increase in 2011 to below 4% of GDP but decline again to slightly above 3% in 2012. But the average masks large differences across countries. However, if disbursements of ODA fall short of expectations as donor countries are facing fiscal problems, and if African governments introduce food and fuel subsidies to protect households from high prices, deficits could be significantly larger. Furthermore, the large number of national elections on the continent this year also bears the risk that office holders will raise spending to get political support from voters, and such "election-cycle politics" would also undermine fiscal consolidation.

After the deterioration in 2009, which had been caused by the fall in commodity prices and export volumes, *external positions* improved as commodity prices and export volumes recovered. But current account positions have generally not regained the levels prior to the global crisis and in some oil-importing countries imbalances are widening.

The current economic recovery in Africa is likely to reduce the cyclical component of unemployment, but structural unemployment remains high in many countries. In North Africa, where economic activity has been disrupted by the political upheavals, unemployment is likely to further increase in 2011. *Youth unemployment* has long been a major problem in North Africa (but also in many other African countries) and contributed to the political unrest which led to the overthrow of governments in Tunisia and Egypt. Labour markets have not been flexible enough to absorb the growing supply of young workers. Given Africa´s rapidly growing population, the demographic pressure on labour markets will continue in many African countries. But in North Africa and Southern Africa the demographic pressure on labour markets will ease as the youth population is projected to remain close to current levels.

A comprehensive approach is needed to address the problem of unemployment in general and of youth unemployment in particular. Improvements are needed both on the supply and the demand side of labour markets. More needs to be done to improve the quality of labour supply so that it better matches the skills required by employers. This also refers to university graduates who are vulnerable to unemployment if their skills do not match job requirements. At the same time labour demand needs to be boosted by further improving framework conditions for economic growth in general and for private sector activity in particular, including through the creation of new firms.

African policy makers must be aware of several sources of global and domestic risks. Economic and social stability needs to be sustained – or where it is disrupted – be quickly restored. Policy requirements are to pursue prudent macro policies and at the same time implement appropriate measures to cope with higher commodity prices. In resource-rich countries, part of the windfall profits could, for example, be put into sovereign wealth funds in order to prepare for the time when prices fall again or resources will be depleted. Given the currently high food prices, governments, which have the necessary resources, might consider protecting vulnerable groups from hunger by providing targeted subsidies, while refraining from costly food and fuel subsidies to the general public. Furthermore, framework conditions for farmers should be further improved so that they are able to increase investment and productivity in response to higher agricultural prices.

External Financial Flows

During the last decade, financial flows to Africa have increased rapidly. Between 2000 and 2010 the sum of Foreign Direct Investment (FDI), portfolio investment and Official Development Assistance (ODA) increased almost five-fold from USD 27 billion to USD 122 billion.

FDI is an especially important source of investment in Africa and over the last decade has amounted to one fifth of Africa´s gross fixed capital formation. FDI to African countries peaked in 2008 at USD 72 billion, five times the value of FDI receipts in 2000. During the global crisis in 2009 Africa´s FDI inflows fell by 20%, to USD 59 billion. Estimates for 2010 point to a further decline to around USD 50-52 billion. Looking forward, the global recovery with high growth in emerging countries, high commodity prices and improvements in economic conditions in many African countries should further stimulate FDI in Africa. However, the recent political events in parts of Africa, notably North Africa with the war in Libya, will likely hold off foreign investors in this region. In recent years, North Africa has been the top destination-region for FDI in Africa, receiving a little more than one-third of all FDI flows to Africa.

Africa´s FDI inflows continue to be unevenly distributed, with a large share going to a limited number of countries. About three-quarters of Africa´s FDI is invested in oil exporting countries. Attracting investment into diversified and higher value-added sectors remains a challenge. Some progress has been made recently in the services sector, led by telecommunication, which is attracting increased investor interest.

OECD countries are the most important source of FDI flows to African countries, accounting for more than 70% of Africa´s FDI inflows between 2000 and 2009. South Africa, Egypt and Nigeria were main beneficiaries of OECD investment in Africa and most of OECD FDI in Africa came from the United Kingdom, France and the United States.

Data on FDI to Africa from non-OECD countries is difficult to obtain. According to its statistical bulletin, China invested USD 5.5 billion in sub-Saharan Africa in 2008, representing almost 10% of its outward FDI. This investment from China was up from USD 70 million in 2003 but declined to USD 1.1 billion in 2009. However, this number understates China´s engagement as activities of state-owned enterprises often involve a range of other financing instruments and are not counted as FDI.

FDI of other emerging economies is also largely in extractive industries but sometimes combines investment in mining with the development of industrial complexes for these sectors and the construction of necessary infrastructure. Moreover, emerging economies also invest in manufacturing at an increasing rate.

Intra-African FDI has equally gained in importance with most of it made in neighbouring countries, focussing on manufacturing and services, thus boosting regional integration and also contributing to diversification. South Africa is the most vital source of intra-African FDI. Libya has invested in many African countries, and Egypt, Morocco and Tunisia have also invested large parts of their outward FDI stocks in Africa. Given this importance of North Africa as a source of intra-African FDI, the recent political turmoil in this region will likely have adverse effects on FDI inflows of African countries in the near term.

ODA to Africa has been rising steadily over the last decade, from USD 15 billion in 2000 to USD 48 billion in 2009. Despite this increase, donors risk failing to meet their Gleneagles commitments made in 2005. In 2009, overall ODA to Africa was almost a quarter short of the target. Net bilateral ODA from DAC donors to Africa totalled USD 28 billion in 2009, of which USD 25 billion went to sub-Saharan Africa. This number represents an increase of 3% in real terms over 2008 for all of Africa and an increase of 5.1% for sub-Saharan Africa --an increase which helped African countries to mitigate the adverse effect of the global economic crisis.

Among non-DAC members, China, India and Saudi Arabia are the most important providers of concessional loans and grants to Africa. Developing country partners tend to combine commercial with developmental interests and financing modalities. For example, export credits do not fall within the ODA definition, but they play an increasingly large role in relations between Africa and its developing country partners.

Trade Policies and Regional Integration

African trade has rebounded in 2010 spurred by the recovery of global trade and in particular demand from emerging markets. A growing services trade has also been consistent with global trends over the past years, signalling Africa's increasing potential and prospects in different services subsectors.

Progress under the Doha Development Round (DDR) and the Economic Partnership Agreements (EPA) negotiations continues to be slow and highly contingent upon compromises between the parties, which aim to balance policy space, developmental goals and deeper market access. Further, the dynamics of other trade relations for Africa, notably under trade preference schemes such as the African Growth and Opportunity Act (AGOA) and South-South co-operation through trade and investment with China have gained increasing importance in the African economic development and diversification agenda over the past years.

African leaders have taken a number of initiatives aimed at advancing the regional integration process in Africa. In particular, the development of Minimum Integration Programmes, the rationalisation of the Regional Economic Communities (RECs), and the recognition of eight RECs as the main building blocks of the African Union, have helped these Communities to continue to play a significant role in achieving Africa's regional integration vision.

Some RECs such as Economic Community of West African States (ECOWAS), Economic Community of Central African States (ECCAS), Common Market of Eastern Southern Africa (COMESA), Southern African Development Community (SADC) and East African Community (EAC) have established Free Trade Areas while others such as Community of Sahel-Saharan States (CEN-SAD) are steadily working towards this objective. Furthermore, EAC and COMESA launched their customs unions in 2005 and 2009, respectively, while, SADC and ECCAS are expected to do so soon and ECOWAS is expected to follow suit in 2015. The Arab-Maghreb Union (UMA), CEN-SAD, and the Intergovernmental Authority Development (IGAD) are to implement their customs union projects in the near future. In addition to these strides, some RECs seek also to harmonise their agendas for establishing Free Trade Areas (FTA) to create larger trading blocs, such as a grand FTA between SADC, COMESA and EAC.

Despite these promising developments, challenges which significantly affect the RECs include: the prevalence of political instability in some parts of the continent, lack of economic diversification, continued multiple and overlapping memberships, inadequate financial resources to buttress the integration processes, and poor implementation of commonly agreed protocols and decisions.

There are also challenges concerning connectivity. *Regional infrastructure development in Africa* is crucial for economic growth and sustainable development. Despite efforts to implement a coherent programme of activities in the areas of energy, transport and communications, Africa remains one of the continents with weak infrastructure networks; this contributes significantly to higher production and transaction costs, and undermines the competitiveness of businesses.

The current status of infrastructure developments in Africa remains mixed. Some sectors have recorded significant progress while others are lagging. The situation in the continent is characterised by insufficient and low quality infrastructure on the one hand, and inefficient and expensive services on the other. For example, only 20% of road networks in Africa are paved and transport services are expensive due to supplier cartels. To overcome these shortcomings, continental efforts in the field of roads development include trans-African highways.

Even less satisfactory is the situation of the railway network, which in comparison to other regions and continents shows a very low density. In addition, the network is generally old and technically out-dated, resulting in a low share of rail freight in intra-African trade.

Finally, the global picture of Africa's share in air transport remains modest, relying mostly on three major hubs, namely, Johannesburg, Nairobi and Addis Ababa. South African Airways, Kenya Airways and Ethiopian Airlines remain the three major airlines in Africa. In 2004, Africa's share was 5.2% of passenger traffic and approximately 3.6% of freight.

Human Development

The international community set the goal of eradicating extreme poverty and hunger in the Millennium Declaration adopted in 2000. The community specified two targets in the Millennium Development Goals (MDGs): over the period 1990-2015, halving the proportion of people whose income is less than 1 US dollar a day using 1993 purchasing power parities (PPP), and halving the number of people suffering from hunger. The poverty line was revised to USD 1.25 in 2005 PPPs after estimates for purchasing power parity exchange rates were revised in late 2007. From 54% in 1981, the rate of poverty increased to 59% in 1996 before declining to 51% in 2005, the last year for which comparable data is available. It has been estimated that as a result of slower growth in the wake of the global crisis and the rebound of food prices, poverty might have increased in 2009 and 2010.

While Africa has made progress in reducing poverty between 1996 and 2005, the rate of poverty reduction has been slow relative to other developing regions, due to three main factors: First, Africa experienced relatively high levels of economic growth only since the 2000s, so the growth rates during the 1990s were not high enough to make a substantial impact on poverty. In order to halve poverty by 2015, a cross-country econometric analysis established that African economies would need to grow by 7% per year on average. Despite a clearly improved growth performance in the first decade of the new century with average growth of 5.3%, Africa remained below this mark. Second, growth in Africa has not been high enough in sectors where the poor live or work. Although this situation has improved in many countries since 1996, Africa's growth often originated from sectors with weak linkages to the rest of the economy, such as the mineral and oil sectors, so that the economic expansion has had little impact on job creation and poverty reduction. Third, relatively high inequality in Africa reflects that growth benefited a small part of the population and the benefits to the poor were limited. In this regard, poverty reduction policies will need to combine high economic growth with a reduction in inequality, while ensuring that the sources of economic growth are broad based.

The limitations of income-based measures of progress and wellbeing motivated the creation of the Human Development Index (HDI) by UNDP in 1990. This measure reflects a people-centred understanding of development. It measures human development by integrating indicators of education and health with income. Although by 2010 Africa as a whole had the lowest HDI of any region, the trend between 2000 and 2010 shows that all African countries, except Zimbabwe, improved their human development score. Sub-Saharan Africa made, on average, the most rapid progress of any region. The regional HDI increased by 23%, followed by South Asia, where the increase was 17% over the same period. This improvement was due to rising income per capita in the 2000s in most African countries, and to genuine progress in access to knowledge and better health outcomes.

As expected, an Inequality-Adjusted Human Development Index (IHDI) shows that relatively high levels of income inequality are associated with low human development. In contrast, the Gender Inequality Index (GII) shows a few African countries performing much better than on the other dimensions of human development. The implication is that some dimensions of human development (e.g. gender equality) can be significantly improved even in very poor countries, as they do not necessarily require financial resources, which constitute one of the most binding constraints to development in such countries.

To sustain progress in human development, Africa will need to take simultaneous actions on several fronts rather than focus on only one objective. For example, economic growth will improve human development if it is inclusive and pro-poor. Similarly, investing in social sectors will produce sustainable human development if investment is accompanied by efforts to create more economic opportunities that benefit a large segment of the population. Moreover, some dimensions of human development, for example gender equality, will improve if African governments make the deliberate choice to pursue policies that promote gender equality. In this regard, the quality of economic policy will probably be as important as the resources used to advance the cause of human development in Africa.

Political and Economic Governance

The first quarter of 2011 has been among the most turbulent in Africa's history. Peaceful popular uprisings toppled long-standing authoritarian regimes in Tunisia and Egypt. Neighbouring Libya descended into a civil war in which the international community intervened with military force. The future development in Libya and the repercussions on its neighbours are difficult to predict.

In 2011, the continent will experience a record number of 28 national-level elections in 20 countries. An outstanding electoral event has been Southern Sudan's peaceful January referendum in favour of separation from Northern Sudan. This will come into force in July 2011.

In 2010, 13 countries held largely peaceful elections. The presidential election in Guinea that put an end to the institutional crisis generated by the coup d'état in 2008 and the peaceful constitutional referendum in Kenya were significant milestones after the post-election violence in 2008. The crisis and widespread violence in Côte d'Ivoire after a contested presidential election in November marked the low point.

The report takes stock of Africa´s political and economic governance in 2010 based on the same measures as in last year´s AEO. The main findings of this stocktaking are:

- 2010 was a year of intensifying civil protests, as measured by the number of demonstrations and strikes, pointing to the high level of economic and other grievances felt by many African populations. Yet 2010 was also a year of decreasing violence, which points to a positive trend of more peaceful and democratic expressions of demands that bodes well for Africa's development.
- Violence erupted in several countries, most prominently the post-election violence in Côte d'Ivoire and inter-religious conflicts in Nigeria and Egypt. However, of the 13 legislative and presidential elections held, only the one in Côte d'Ivoire was followed by large-scale violence. Violence around other elections was significant but of minor scale.
- Despite an increase in public protests, government responses in the form of violence and restricting political measures (bans of press, demonstrations, etc.) continued their downward trend. Our indicator of political hardening, which combines various means of government oppression into a single variable, indicates that 2010 was the year with the most relaxed stance of governments since the beginning of the series in 1996.

- The Political Freedom Index (PFI) from Freedom House, which measures political rights and civil liberties, classifies nine African countries as "free", 24 as "partly free" and 20 as "not free" in 2010. All countries that experienced revolts in 2011 had very low values for civil liberties and political rights and were classified as "not free". Concerning freedom of the press, progress was mixed with 21 countries improving their rating while in 22 countries the situation for the press worsened.
- Despite significant efforts to fight piracy around the Horn of Africa, it increased significantly over the last years. The pirates' radius now reaches from the coasts of Oman to Tanzania and almost reaches the Maldives and causes significant economic costs to international traders and the countries in the region.
- Corruption remains a serious problem in Africa with 27 out of 47 African countries classified as having "rampant corruption". Additionally, in 17 countries corruption is perceived as a "serious challenge" by country experts and business people. As in 2009, only in Botswana, Mauritius and Cape Verde is corruption perceived as a lesser challenge.
- A number of African countries registered remarkable economic improvements with respect to *economic governance.* According to *Doing Business 2011*, among the top thirty most improved economies, a third of them are in sub-Saharan Africa. In the top ten are three sub-Saharan African countries: Rwanda, Cape Verde and Zambia. The improved conditions are generally attributed to better regulations and continued ease of doing business in many African countries. Measures focused on facilitating the process to start a business, improving access to bank credits, and better enforcing contracts. However, much remains to be done in Africa to upgrade conditions for doing business to international standards.

Africa and its Emerging Partners

The 2011 edition of this *Outlook*'s thematic chapter investigates the rise of Africa's emerging partners. It analyses policy options for African policy-makers to make the best out of Africa's rapid integration into the global economy. The decade that began at the onset of the new century saw emerging partners swiftly rise from a relatively marginal position to one of fully fledged partners. Africa's trade volumes with its emerging partners have doubled in nominal value over the decade and now amount to 37% of Africa´s total trade. While China represents Africa's leading emerging partner, having surpassed the United States in volume, the continent's trade with its other emerging partners, taken together, is even larger than its trade with China alone. China represents more than a third of Africa's trade with emerging partners.

The EU and the US remain the most important sources of Foreign Direct Investment (FDI) for African countries. When it comes to Official Development Assistance (ODA), traditional partners also dominate, although the share of emerging partners is growing fast. However, those are only the tip of the iceberg: emerging partners provide Africa with a range of alternative finance modalities that defy FDI and ODA definitions. They tend to adopt a more holistic approach to promoting their exports, supporting direct investment, and offering development assistance.

Africa's business relations with emerging partners are often complementary to those with traditional partners. Because of their diversity, emerging partners offer African countries new opportunities to exchange goods, technology and development models. They make mass consumption goods affordable to the nascent African middle-class and supply production goods adapted to the productive conditions of developing countries. These goods have the potential to help African firms increase their productivity and move up global value chains.

The co-operation activities of emerging partners are also typically complementary to those of traditional partners. The latter have focused their assistance, mostly through ODA, on poverty reduction, health, education and governance. Emerging partners, not only China, are more focused on removing infrastructural bottlenecks.

African manufactured exports have roughly doubled over the last 10 years, mostly driven by the demand of emerging partners. Fears that the intensifying co-operation with emerging partners is boosting Africa´s indebtedness are not supported by available evidence. However, a risk of re-indebtment persists, particularly for the weakest African states. Similarly, existing aggregate governance indicators show no sign of a worsening of corruption. Policy autonomy is affected differently for different groups of African countries: the resource-abundant ones stand to widen their policy space more than others.

However, these general benign trends do not guarantee economic diversification and, thus, policy has a role to play. African countries have to frame their engagement with their emerging partners within a home-grown strategy of national development, particularly with respect to longer-term industrial and agricultural policy. Where absorption capacity is low, large infrastructure investments need to be accompanied by proper budgeting of maintenance costs and consistency with the country's development strategy.

Most African countries still need to enhance their bargaining position vis-à-vis traditional *and* emerging partners to ensure that these partnerships are actually mutually beneficial and African countries get their fair share of the benefits. Policy options include leveraging the rise in commodity prices to negotiate the supply of infrastructure for diversification, industrialisation and economic development, and holding traditional partners to account on their aid promises.

Faster progress in regional integration is imperative, so that African countries do not engage in "incentive wars", trying to outbid each other for FDI and aid. Better co-ordination means more bargaining power. Besides, from a financing perspective, regional, larger-scale projects would attract more consideration from emerging partners, especially those using Sovereign Wealth Funds (SWFs).

To promote regional integration, African countries can leverage complementarities between partners: traditional partners have the mechanisms to support the Regional Economic Communities (RECs) secretariats, while emerging partners can give additional impetus to build cross-border infrastructure. They would thereby help to boost intra-regional trade, in turn contributing to a virtuous circle of deeper economic integration that would bring closer together the visions of regional actors.