GLOBAL ECONOMIC SLOWDOWN AND THE AFRICAN CONTINENT: RETHINKING EXPORT-LED GROWTH.

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Abstract

Africa's development strategies since independence has focused on import substitution strategy and structural adjustment programme (SAP) with disappointing outcomes. However, since the late 1990s, growth has resumed due mainly to favourable primary commodity prices fueled by high demand by emerging economies. Nevertheless, the recent economic slowdown has shown that export-led growth can make fragile economies very vulnerable and can lead to major negative shocks. Since the economic slowdown, all growth indicators are pointing to the fact that growth expectations may not be met. The deterioration in economic performance has opened the export-led growth model to challenge suggesting that there is a need for a rethink and the need for a shift on the new development policy agenda that focuses on domestic demand-led growth. Domestic demand-led growth rests on four pillars: improved income distribution, good governance, financial stability and an adequate fairly priced supply of development finance. Thus, this paper seeks to examine the relevance of the export-led growth paradigm on African countries in the context of current global economic outlook. The paper observes that the very fact that Africa's recovery from a crisis it did not cause seems conditional on the recovery of those that caused it means that the current growth strategy is neither optimal nor appropriate. The paper proposes a new development policy agenda in Africa that focuses on domestic demand-led growth.

Keywords: Global Economic Slowdown, Export-led growth, Africa.
JEL Classification: F01, F13

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1. Introduction

At independence, the focus of most African countries was on Import Substitution Industrialization (ISI) strategy with the objective of producing goods previously imported from developed countries locally, and also as a means of achieving rapid economic growth while diversifying productive structures. The strategy advocated was to start with the production of final consumer goods and gradually moving on to the production of intermediate goods and capital goods. To ensure the workability of the strategy, high tariff barriers, import controls, credit and exchange rate subsidies were used extensively, particularly to protect the so called domestic infant industries. However, macroeconomic performance of many African countries over this period could not have been said to be encouraging compared to that of East and South-East Asian countries. Over this period (1965-73; 1980-91) per capita GDP growth in Africa declined from 1.7 per cent to -1.2 per cent compared to East Asian and South Asian countries whose GDP growth increased from 5.2 per cent to 6.1 per cent and from 1.2 per cent to 3.1 per cent respectively. Similarly, export volume which declined from 14.2 per cent to -1.08 per cent in African region increased from -0.2 per cent to 6.06 per cent over the same period for East Asian and South Asian countries. (Onafowora, Owoye and Nyatepe-Coo, 1996). Consequently,

the better economic performance of the East and South-East Asian countries prompted the International Monetary Fund (IMF) and the World Bank (WB) to suggest an outward-oriented development strategy to African countries as part of their structural adjustment and reform programmes (Onafowora and Owoye 1998). The adoption of this type of developmental strategy, it is argued, would enable African countries to attain higher economic growth propelled by a dynamic and more robust external sector. In particular, African countries would be able to raise the required external resources for development financing.

As a result, from the mid-1980s, many African countries adopted the structural adjustment programme (SAP) aimed at liberalizing their economies particularly the external sector. The structural reforms focused on supply and its redirection in the context of export promotion strategies. This new development option, which marked Africa total departure from the import substitution strategy, sought to redirect growth-promoting strategies towards the external market (Hammouda, 2004). The main purpose of trade policy reform over this period was to promote economic growth by capturing the static and dynamic gains from trade through a more efficient allocation of resources; greater competition; an increase in the flow of knowledge and investment and, ultimately, a faster rate of capital accumulation and technical progress. It was the belief that barriers to trade and anti-export bias would reduce export growth below potential (Santos-Paulino and Thirwall, 2004). As a result, the adoption of trade policy reform measures would reduce anti-export bias and make exports (especially non-traditional ones) more competitive in international markets, mainly by reducing exchange rate distortions and export duties.

Consequently, trade policies in most African countries went through major changes within the context of SAP during this period. Foreign trade was liberalized through the reduction of tariffs and non-tariff barriers and reduction of import duties applied to imports in a large number of African countries. Import permits were abolished and duty rates as part of tariff liberalization were also lowered in many African countries. Currencies were devalued to encourage exporters, with the aim of boosting exports and growth and fostering the integration of Africa into the global economy. A sizeable number of African countries virtually eliminated parallel market premiums, with buying and selling of foreign exchange then becoming market-based, while abolishing previous restrictions on currency transactions. This new policy strategy attempted to promote greater openness in order to boost growth and encourage the competitive integration of the African economies into the globalizing world. In summary, the growth focus of African countries was on export-led framework. Exports were meant to serve as one of the, if not the, main determinants of growth. The successes of East- and South-Asian countries in the use of this export-led growth strategy were just to compelling and convincing. Thus, it is argued that, the only way out for African countries is to wholesomely copy this model. It became a condition for getting any financial assistance from multilateral lending institutions.

Growth recovered in the 1990s, with average annual rates of four percent in 1996, 2.9 percent in 1997 and 3.3 percent in 1998. These results were positive because they were higher than population growth rates and resulted in an increase in per capita income. However, the growth remained unstable (Hammouda, 2004). Nevertheless, growth resumed once again in the continent. The average growth rates of per capita real GDP increased from 5.6 percent in 2004 to 5.9 percent in 2007 (UNCTAD,2008). Africa indeed had a bright growth outlook many arguing

that the continent had turned the corner from decades of economic stagnation and structural macroeconomic imbalances. However, this new trend in growth in the continent can be attributed to favourable primary commodity prices fueled by high demand by emerging economies like China and India. China is currently receiving about 9 percent of Africa's total export while India source about 24 percent of its crude oil from the continent (Hanson, 2008; Beri, 2009). It can therefore be inferred that growth in Africa is being driven by primary commodity exports. Thus, the export-led growth hypothesis (ELGH) that postulates that export expansion is one of the main determinants of growth seems to found support in Africa.

However, today the picture is drastically different. The continent is faced with severe uncertainties about its growth prospects and its chances of reaching its development goals. The main drivers of recent growth performance are threatened by the current financial and economic crisis. The demand and price of African primary commodities are declining, the recent upward trend of capital inflows appears to be losing steam, and promised increases in aid have not been materialized. Furthermore, inflationary pressures have increased in many countries, and the service sector is facing pressures with declining demand, especially for tourism. Already, growth forecasts have been revised downward as a result of these risks. Analysts are of the opinion that, while immediate effects of the crisis may have been limited, medium and long term effects are likely to be larger.

Thus, the recent economic slowdown has shown that export-led growth can lead to major negative shocks. Although, export is required to earn foreign exchange, but the recent experience of some African and even ASEAN economies has revealed that export dependent economies can be vulnerable to external demand shocks, with unintended devastating consequences. The current economic slowdown and accompanying contraction in global trade has manifested in the form of weakened demand for African exports and reduced inward investment. Frozen credit markets, large losses in financial wealth, and shaken investor and consumer confidence have reinforced each other to depress aggregate demand. The contraction in demand has been led by the developed countries, most of which are by now in recession. The sudden stop of capital flows that first manifested at the outset of the crisis has been followed by a wave of immediate decline of export demand that is affecting severely both developing and developed economies. Companies are responding vigorously to the decline in exports and domestic sales by cutting production, in many cases by a larger margin, as suggested by the decline in orders.

All theses are happening at a time when inflationary pressures hamper the usual monetary and fiscal remedies. Thus, these advanced economies have suffered macroeconomic instability, with obvious implications for the demand for exports from developing economies such as Africa. Unfortunately, the global financial crisis and recession were totally unpredicted by African countries, hence they were not prepared at all for such shockers. As expected, researchers, policy analysts, and other policy observers are already re-thinking existing development strategy for African countries by questioning the prescriptions of the Bretton Wood institutions and the idea of wholesome liberalization and globalization. In particular, there is now strong doubt on whether export-led growth is the appropriate way to go for Africa?

Thus, this paper seeks to examine the relevance or otherwise of the export-led growth strategy in the context of global financial and economic crisis and further examine if the export-led growth strategy is responsible for making Africa a victim of the crisis it is not responsible for.

The sequence of this paper is as follows. Section two presents a review of growth strategies in African countries and the background to the recent economic slowdown. The actual and potential impact of the crisis is highlighted in section three. The policy responses of Africa countries to the crisis and the way forward is the focus of section four while section five summarizes and concludes.

2. Review of Growth Strategies in African Countries

Import Substitution Industrialization (ISI) strategies were at the heart of Africa development strategies during the 1960s and 1970s. The import-substitution strategies adopted were meant to produce locally the consumer goods, which had previously been imported from developed countries, so as to promote the diversification of their economies. This strategy was aimed at beginning with the production of final goods, and moving gradually towards the production of intermediate goods and capital goods. The strategy also involved the introduction of restrictive external trade policies and considerable protection for emerging infant industries. Complex systems of tariffs and non-tariff protection, exchange control and import licensing were set up to defend local production. Protection was designed to assist emerging industrialists move up the learning curve during a transitional period when the domestic price of production exceeded international prices. The justification for the ISI strategy was based on the historical development of countries such as France, Germany, United States of America, China, and USSR who took advantage of high levels of protectionism to achieve strong growth rates. Secondly, it was also justified by the infant industry argument as well as the deterioration of the price of commodities exported by developing countries from the 1930s upwards.

Many countries in Africa established industries to produce consumer goods, mostly intended for the new urban middle class. The ISI strategy enabled Africa countries to begin the modernization of production structures inherited from the colonial period. The results were initially seen in an average annual industrial growth rate of 5.5 per cent during the 1970s but which fell to 2.5 percent between 1980 and 1984 and 0.4 percent between 1984 and 1987 respectively. Manufacturing as a proportion of GDP increased rapidly and there was a rise in industrial employment and in its share of overall employment (Hammouda, 2004). Nevertheless, this strategy soon ran into problems (Bruton, 1998). The development of final goods production led to rapid increase in imports of intermediate and capital goods, leading to worsening trade imbalances and balance-of-payments deficits. Small domestic markets did not generate sufficient demand for the products of emerging industries, industries were prevented from reaping the advantage of economies of scale, and import substitution was biased towards elite urban consumers to maintain political support while focusing on consumer goods for the middle class. It therefore generated rent seeking behaviour by firms, as they took advantage of insulation from international competition. The disappointing outcome of import substitution strategy in Africa was seen most starkly in the poor productivity performance of the new enterprises[1]. Import

[1] Mayer (1996) shows that in general, import substitution will lead to a shift of the workforce to formerly imported goods and rapid learning effects will occur. However, this shift represents a one-time stimulus to learning, while thereafter the production mix of the closed economy will change only slowly, i.e. at the pace of the economy's shift

substitution delivered very poor results in terms of productivity improvement, structural transformation of the economy and export diversification.

The failure of the ISI, the success of South- and East-Asian countries, and the debt crisis in the early 1980s led to a new consensus on the importance of trade policy reform and exports in growth strategies. This new consensus was the main focus of the reforms initiated by African countries and the developing world in general from the early 1980s, within the framework of SAPs.[2] As a result the mid-1980s witnessed the formulation and implementation of wide-ranging trade policy reforms by most African countries with the support of the IMF and the World Bank.[3]

The end result is that starting from the mid 1980s, and especially in the 1990s, most African countries liberalized their trade regimes, with many countries reducing trade barriers significantly more than others (especially restrictions on imports). These reforms were aimed at making it easier to import, by reducing tariffs and non-tariff barriers, and encouraging exports, by eliminating export taxes and providing export incentives. For example, there was a partial or complete conversion of quantitative restrictions to tariffs (except for moral, health security, and environmental restrictions in some cases) in most African countries. A study by Oyejide, Ndulu and Gunning (1999) revealed that in line with this new strategy, Mauritius abolished import permits in 1991, Ghana in 1989, Tanzania by 1993, Zambia by 1992, Kenya by 1993 and South Africa reduced 85 per cent of restrictions by 1990. Also, Mauritius compressed its tariff structure from 60 to10 tariff categories, Kenya from 25 to 6, Cote d'Ivoire from 10 to 6, and Zambia and Tanzania compressed their categories to 3. Mostly, this involves a switch from a positive list of permitted imports to a small negative list of mostly prohibited items or items considered to be luxury goods for the country. The sequence was first to levy import surcharges and then to adjust the minimum and maximum tariff prior to abolishing restrictions. Import permits were abolished in Mauritius, Ghana, Tanzania, Zambia and Kenya in the 1990s. In addition, duty rates as part of tariff liberalization were also lowered in some African countries. Mauritius reduced its rates from 250 per cent to 100 per cent; Tanzania from 200 per cent to 60 per cent; Zambia from 150 per cent to 50 per cent and in Kenya from 170 per cent to 40 per cent. In Zimbabwe and Ghana the rates ranged from 5 per cent to 30 per cent and 10 per cent to 40 per cent respectively. Tariffs are now the main trade policy instruments of most African countries. While the overall variation or spread in tariffs has been reduced, progress varies across the regions of African.

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in consumption pattern. This means that import substitution may stimulate growth in the short run but will be detrimental to long term- growth. Entering into competition with foreign firms is likely to generate more learning effects than living in autarky, and being active in the world, rather than only in the domestic market, is likely to give rise to more spillover effects.

[2] Other reasons identified by Oyejide, Ndulu and Gunning (1999) as stimuli for the liberalization of trade regimes include the conditions imposed for gaining access to external finance, positive external shock, specific country own initiative, and membership in a sub-regional economic integration scheme.

[3] According to Oyejide (2004) trade liberalization implies the transformation of the trade regime from an inward –oriented stance that discriminates in favour of (and thus protects) import-competing activities into a neutral regime whose incentive structure does not distinguish between exportables and importables or into an outward-oriented trade policy regime that discriminates in favor of and thus actively promotes exports. The adoption of trade liberalization measures should therefore produce either a neutral or an outward oriented trade regime and allows certain productivity enhancing and growth promoting features on the liberalized economy.

Exchange rate regimes in most of the African countries were also liberalized. A good number of African countries stopped fixing exchange rates and overvaluing their currencies in order to stimulate exports and make the economy more competitive. Kenya, Uganda, Ghana, Tanzania, Zambia, Nigeria, and Cote d'Ivoire virtually eliminated exchange rate premiums, where buying and selling of foreign exchange is now market-based and abolishing previous restrictions on current transactions. The system of multiple exchange rates was abolished in Burundi. From 1996, Ethiopian currency, the Birr, was allowed to float, thereby resulting in the convergence of the official, auction and parallel market exchange rates. After liberalizing its external sector in 1990, Benin Republic's currency was devalued and its black market premium averaged only 2 per cent between 1990 and 1999. We can therefore conclude that most African countries witnessed a significant relaxation of trade barriers. Import restrictions are now lower and export barriers have been significantly reduced.

Table 1: Annual Average Growth Rates of Total and per Capita Real Gross Domestic Product of Regions

Region	Total Real Gross Domestic Product (Percentage)					
World	**1980-1990**	**1990-2000**	**2000-2005**	**2005**	**2006**	**2007**
Developing Economies	3.2	2.8	2.8	3.4	4.0	3.8
Economies in Transition	3.9	5.0	5.4	6.7	7.1	7.3
Developed Economies	3.2	2.5	1.9	2.3	2.8	2.5
Developing Economies: Africa	**2.3**	**2.8**	**4.8**	**5.7**	**5.6**	**5.9**
Developing Economies: America	1.7	3.2	2.7	4.7	5.4	5.7
Developing Economies: Asia	5.7	6.3	6.5	7.5	7.9	8.1

Source: UNCTAD Handbook of Statistics, 2008. Table 8.2.1

The reforms were not, however, entirely successful in Africa. Nevertheless, Growth recovered in the 1990s, with average annual rates of four percent in 1996, 2.9 percent in 1997 and 3.3 percent in 1998 (Hammouda, 2004). On the average, the total real GDP growth rate which averaged 2.3 percent between 1980 and 1990 increased to 2.8 percent in the 1990 and 2000 period (See Table 1). These results were positive because they were higher than population growth rates and resulted in an increase in per capita income. The growth rates were nevertheless lower than the growth rate recorded by economies in transition and the developing economies of Asia during the same period.

The outcome of these reforms fell below expectations if we examine the continent's sectoral performances. The agricultural sector, which employs nearly half of the African population, dropped from 22.3 percent of GDP in 1980 to 19.4 percent in 1997. The performance of the industrial sector was no better, with a decline in its contribution to GDP from 39 percent to 32 percent during the same period. The sector's productivity also decreased from 3.8 percent in 1997 to 3.2 percent in 1998. The proportion of manufactured products in total exports increased from 6.4 percent to 22 percent between 1980 and 1995, but the increase was due to the fact that a few countries such as Tunisia, Mauritius, Egypt and Morocco had succeeded in diversifying their industrial structures and negotiating for international integration based on the export of manufactured products (Hammouda, 2004)..

The downward trend in agriculture and manufacturing was accompanied by a strengthening of the mining and energy sectors. These strengthening reflect Africa's new type of integration into globalization, an integration increasingly based on the mining and energy industries. Thus,

growth in Africa rebounds in the last three years as a result of the increasing trend in commodity prices in which African economies has comparative advantage. Between early 2003 and mid-2008, oil prices climbed by 320 percent in dollar terms, and internationally traded food prices by 138 percent. Specifically, growth increased from 5.7 percent in 2005 to 5.9 percent in 2007. The favourable primary commodities prices were also driven by the high demand for these commodities by emerging economies like China and India.

Africa holds a fraction of the world's proven oil reserves—9 percent compared to the Middle East's nearly 62 percent. China's booming economy, which has averaged annual 9 percent growth for the last two decades, requires massive levels of energy to sustain its growth. Though China relies on coal for most of its energy needs, it is the second-largest consumer of oil in the world behind the United States. Once the largest oil exporter in Asia, China became a net importer of oil in 1993.China's biggest suppliers in Africa as of 2006 were Angola, the Republic of Congo, Equatorial Guinea, and Sudan. It has also sought supplies from Chad, Nigeria, Algeria, and Gabon. Similarly, currently around 24 per cent of India's crude oil imports are sourced from Africa. Indian national oil companies like the Oil and Natural Gas Corporation Videsh Limited (OVL) has invested in equity assets in African countries.

However, the recent sharp declines in oil and food prices mark the end of what has been the most historic commodity price boom of the past five years. Following a historic five-year boom during which energy prices, metals and minerals prices and food prices soared, these commodities prices plunged in late 2008. In December, the World Bank predicted that real food prices would fall by 26 percent between 2008 and 2010, oil prices by 25 percent and metals prices by 32 percent (AfDB, 2009). (See Table 2 and Figure 1).

Like earlier booms, it was driven by strong global economic growth and has come to an end with the abrupt slowdown in the global economy precipitated by the financial crisis. The exceptional duration of this five-year commodity boom, the number of commodities involved, and the heights that prices reached reflect the resilience of developing country growth during this period. The prolonged boom is clearly over, even as the social and human consequences of historic favorable trend in prices linger. Commodity prices across the board have fallen, giving up much of their earlier gains, due to slower GDP growth, increased supplies, and revised expectations. Since the economic slowdown, all growth indicators are pointing to the fact that growth expectations in Africa may not be met. This is because the outlook for economic growth in sub-Saharan Africa in 2009 actually worsened in recent months. Growth in Africa has been projected to slow from just over 5 percent in 2008 to about 3_ percent in 2009—over 3 percentage points less than forecast a year ago. Fiscal balances are expected to deteriorate significantly as tax revenues, especially those that are commodity-related, come under pressure because governments face additional demands for social spending. The negative terms of trade shock to commodity exporters is also widening current account deficits.

Although, African economies are not responsible for the crisis, yet they are bearing a disproportionate percentage of the crisis. There are three main factors at work. Commodities are Africa's bread and butter and commodity prices have been dropping fast thanks to falling demand due to the global downturn. The first thing to implode has been commodity prices. Excluding gold and cocoa, raw-material prices have dropped across the board. For African

countries reliant on export of primary commodities, this spelled economic disaster. Botswana's economy is almost wholly dependent on diamonds. De Beers, which has largely financed Botswana's growth, last month shut down its mining operations for several weeks and said it would reduce production by about 50 percent through April. Several large coal-mining projects in Mozambique recently shut down as the bottom fell out of fuel production. In South Africa, annual gold production plummeted 13.6 percent to levels last seen in 1922. A plummeting copper price—down by about 60 percent—has led to mine closures and thousands of job losses in the Copperbelt region of Zambia, where copper accounts for 80 percent of foreign earnings and has been the major driver of economic growth.

Next to be affected will be the aid-dependent countries like Rwanda and Tanzania (Mozambique, which, aside from being commodity-dependent, gets 20 percent of its GDP from aid, will suffer a double blow). Investment is also shrinking. The Institute of International Finance estimates that investment flows to developing countries, many of which are in Africa, could drop by as much as 80 percent in the next year (Johnson, 2009).

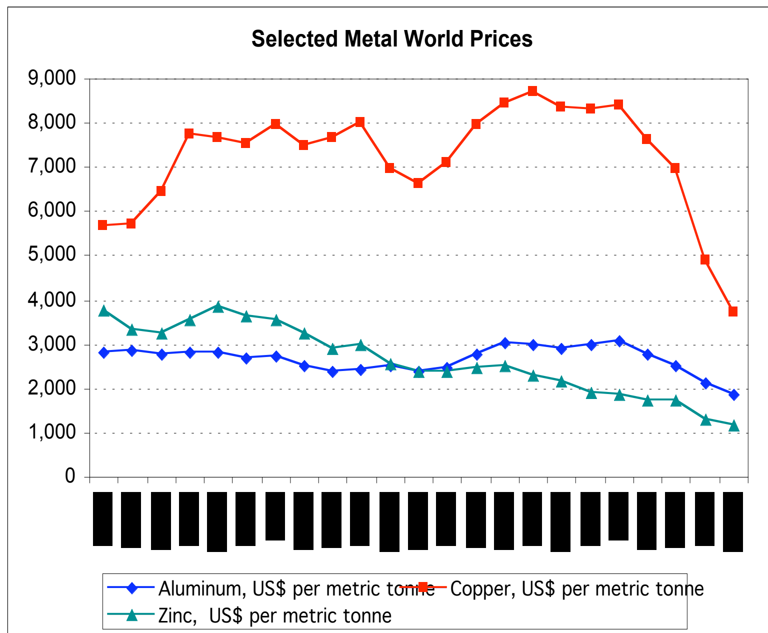
Table 2: Change in Some Commodity Prices between January 2007 and December 2008

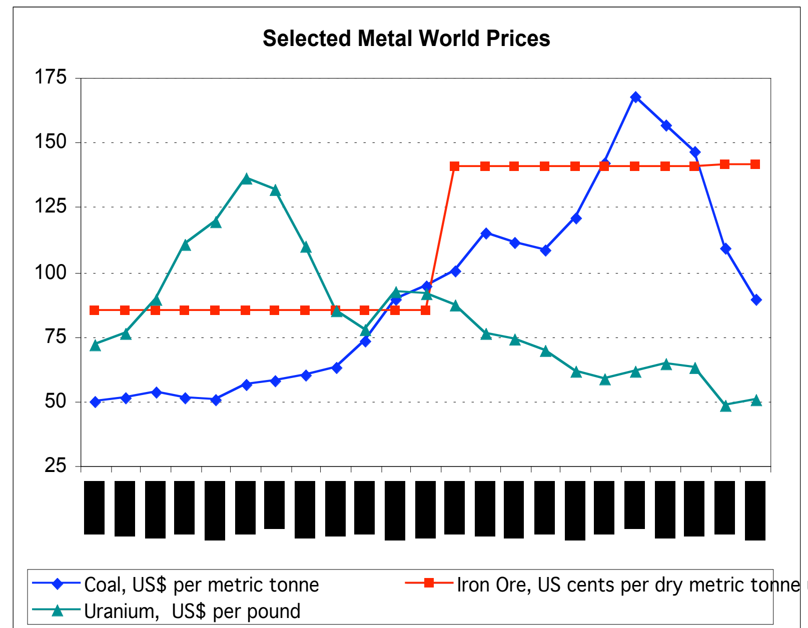
	Brent (US. Dollars Per Barrel)	Gold $/g	Phosphate $/ton	Iron $/ton	Aluminum $/ton	Manganese $/ton	Cocoa beans, US$ per metric ton	Tea, US cents per kilogram	Coffee, Arabica, US cents per pound	Coffee, Robusta, US cents per pound	Cotton, $/ton
Jan-07	53.7	22.3	45.5	84.7	2809.3	158.8	1702.0	249.7	124.5	80.6	1302.1
Dec-07	92.1	28.3	135.0	84.7	2382.0	202.4	2113.1	206.0	136.5	91.4	1535.0
Dec 08 (or latest)	40.3	28.5	350.0	140.6	1852.0	107.2	2067.7	282.0	116.9	84.0	1020.0
% change Jan 07 to Dec 07	71.6%	27.3%	196.7%	0.0%	-15.2%	27.5%	24.2%	-17.5%	9.6%	13.4%	17.9%
% change Dec 07 to Dec 08	-56.2%	0.4%	159.3%	66.0%	-22.3%	-47.0%	-2.1%	36.9%	-14.4%	-8.1%	-33.6%

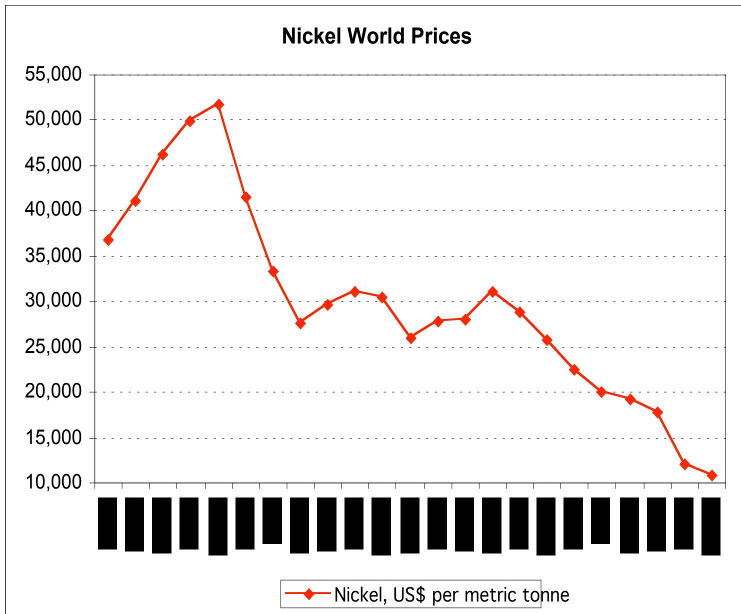
Note: latest data are for November for phosphate, iron, aluminum, and cocoa beans; and October for gold, manganese and tea.

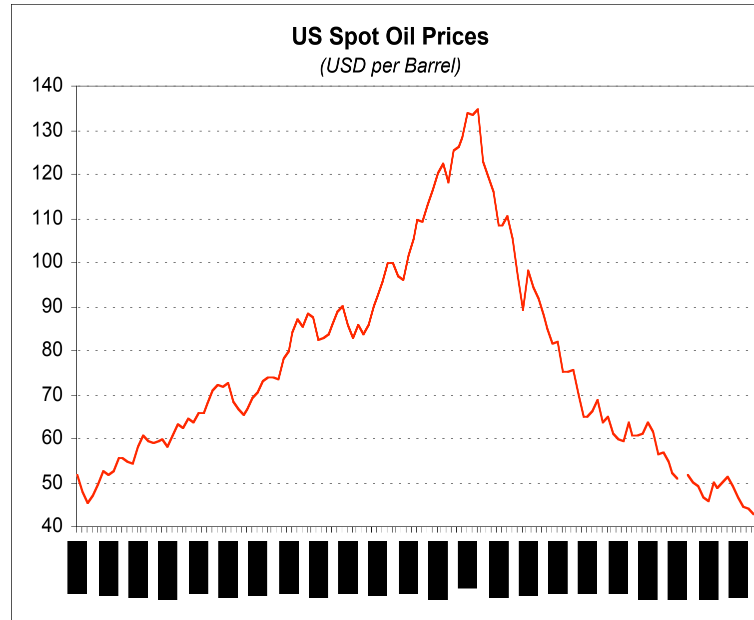
Source: AfDB, 2009

Figure 1: Commodity prices Jan 2007-Nov 2008









Source: AfDB, 2009.

The global financial crisis started in the U.S. sub-prime mortgage market. The financial turmoil then spread to other developed countries in early 2008, especially after the government-sponsored sale of investment bank Bears Stearns in March 2008 to JPMorgan, and fully impacted developing countries after the failure of Lehman Brothers in September 2008. As the decline in housing and equity prices hit consumers, companies and banks, the price of risk surged, leading investors in developed markets to liquidate portfolio investments at home and in emerging markets. As governments implemented a series of policy measures to prevent a financial meltdown and a deep and protracted global recession, they must now also work forcefully to prevent the current financial and economic crisis from turning into a human crisis.

Frozen credit markets, large losses in financial wealth, and shaken investor and consumer confidence have reinforced each other to depress aggregate demand. The contraction in demand has been led by the developed countries, most of which are by now in recession. Countries far from the epicenter of the crisis have been hit as hard as the U.S., underlying the global reach of financial markets and putting to rest any claims of "decoupling". The global financial crisis initially affected advanced economies, emerging markets, and low-income countries in very different ways. Advanced economies were first hit mainly by the systemic banking crisis in the United States and Europe. Emerging markets with well-developed financial systems were initially mostly affected by cross-border financial linkages through capital flows, stock market investors, and exchange rates. In financially less-developed countries the growth and trade effects dominated, with lags. In Africa, frontier and emerging markets were hit first; by now indirect channels are fully at work in all countries, and risks are mounting that other channels may gain in importance, especially in the financial sector (IMF, 2009). According to the World Bank, the "sudden stop of capital flows" that characterized the first wave of the crisis has been followed by the second wave of a "sudden stop of export demand" that is affecting severely both developing and developed economies. Companies are responding vigorously to the decline in exports and domestic sales by cutting production, in many cases by a larger margin, as suggested by the decline in orders .The economic slowdown has amplified investor worries about risk, sustaining tensions in equity, credit, and inter-bank markets worldwide.

In summary, we have to acknowledge the poor results of the growth strategies initiated since the early 1960s up to the present period in the continent. Particularly in Africa, the dropping of import-substitution strategies and the choice of greater openness did not markedly boost growth or ensure more competitive integration into the global economy. Rather, economic growth that was witnessed in the recent period could be attributed to favourable commodity prices of comparative advantage to Africa and the increasing demand by emerging economies of China and India—which made proponents of the export-led growth hypothesis to shout Eureka!!. Unfortunately, the celebration seems short-lived, no thanks to the global financial and economic crisis which has cast serious doubt on the long-term sustainability of such a growth and development strategy.

3. Economic and Financial Crisis and the African Economy

The cause of Africa's current economic despair is the very growth/development model that was the source of its prior success: its heavy dependence on exports. By deciding to hitch their wagons to primary exports, African countries left themselves inherently vulnerable to a drop-off in external consumption. The growth model was also built on weak social and political foundations, from underinvestment in public education, health care, and social services to poor governance and a weak rule of law.

3.1 Transmitting the Slowdown

With respect to the financial crisis and global economic slowdown, African countries are exposed to four main risks. The first is a capital outflow risk, that is, private capital reversal and amplified volatility of private capital flows with the resulting impact on the exchange rate and ability to finance the current account deficit. The second is fiscal risk, stemming from falling revenue and increasing expenditure occasioned by the need to support financial institutions and the need to meet public debt service commitments. The third major risk is export risk, related to slowing demand and declining prices of export commodities. The fourth risk bothers on liquidity risk affecting the domestic banking sector and the government arising from the weakening of global financial market.

Variation among African countries however exists on the degree of exposure to these risks as well as the magnitude and speed of the impact of the financial crisis and the global economic downturn. This depends on each country's economic structure and particular circumstances. Consequently, certain countries are more vulnerable than others. Nevertheless, two major factors of vulnerability include the country's initial macroeconomic fundamentals and the degree of its integration into the global financial system. Pertaining to macroeconomic fundamentals, a number of African economies exhibit a high level of vulnerability due to poor macroeconomic balances, namely high current account deficits, high debt levels, and budget account deficits. For these countries, a decline in exports, capital inflows, and government revenues exposes them to high fiscal risk with the threat of insolvency. Many African countries can therefore be classified as high risk countries on the basis of these macroeconomic balances considerations (Table 3). In 2007, eleven African countries have current account deficits above 10 percent of GDP and 8 countries have debt service to export ratios above 20 percent, which are considered high by conventional standards.

Table 3: Some indicators of vulnerability (2007 values)

Current account (%GDP		TDS% exports	FL&FA (%GDP)	Reserves months of import cover	% of foreign bank assets
Seychelles	-38.7	10,04	90.4	0.39	36
São Tomé & Príncipe	-35.5	114,66	43.0	3.81	NA
Liberia	-30.7	0	660.0	2.2	NA
Djibouti	-25.2	8.1	69.3	NA	NA
Congo, Republic of	-19.5	5.0	4.9	7.34	NA
Madagascar	-15.1	1.3	4.7	2.94	100
Ghana	-12.8	3.3	NA	NA	65
Burundi	-12.4	69.1	11.3	4.52	36
Sudan	-11.8	4,5	2.9	1.54	20
Gambia, The	-10.7	198.8	12.2	4.86	NA
Cape Verde	-10.1	9.3	14.4	4.43	NA
Burkina Faso	-9.9	5.8	8.8	7.34	65

Mozambique	-9.4	17.2	0.0	4.79	100
Tanzania	-9.2	132.8	5.5	6.42	66
Guinea	-9.2	8.1	NA	NA	NA
Senegal	-8.1	7.4	9.4	3.89	48
Mauritius	-7.9	3.9	335.4	4.54	37
Niger	-7.7	2.2	5.0	4.22	59
South Africa	-7.3	9.0	28.9	3.94	0
Mauritania	-6.7	2.4	NA	NA	5
Zambia	-6.7	1.3	7.6	3.53	77
Mali	-6.6	3.9	10.0	5.62	57
Togo	-6.4	0.5	10 .9	3.9	0
Benin	-5.7	6.3	12.1	12.19	40
Rwanda	-4.8	1.4	NA	NA	70
Eritrea	-4.7	30.3	11.9	NA	NA
Ethiopia	-4.5	5.7	5.0	2 .6	0
Central African Rep.	-4.5	0.0	3.4	4.49	NA
Chad	-4.3	2.1	3.5	4.29	NA
Congo, Dem. Rep. of	-4.0	8.1	5.1	NA	47
Sierra Leone	-3.8	4.1	7.0	4.5	NA
Kenya	-3.5	5.8	5.6	3.9	41
Malawi	-3.2	5.6	2.3	1.95	22
Tunisia	-2.5	13.3	12.8	4.91	NA
Uganda	-2.0	6.5	5.1	8.46	80
Guinea-BiAfricau	-1.7	8.0	7.8	7.16	NA
Zimbabwe	-1.0	8.2	22.9	NA	51
Morocco	-0.1	9.3	5.0	9.12	NA
Cameroon	0.4	9.7	4.7	4.83	63
Nigeria	0.7	3.7	5.1	12.56	5
Swaziland	1.2	0.0	4.1	3.56	100
Côte d'Ivoire	1.4	9.9	4.5	3.38	66
Egypt	1.5	6.6	23.4	8.38	NA
Equatorial Guinea	1.8	0.4	3.0	7.41	NA
Comoros	1.9	70.0	4.2	8.3	NA
Lesotho	4.8	4.4	21.4	6.27	NA
Angola	11.0	8.0	6.2	5.58	53
Gabon	12.8	10.2	13.9	4.25	NA
Botswana	16.8	15.4	7.0	31.75	77
Namibia	18.4	3.6	5.2	3.34	50
Algeria	23.2	3.1	0.9	34.66	NA
Libya	42.5	NA	3.1	37.35	NA

Red: High risk: CA< -7.7%; TDS>15%; FL&FA >20%; Reserves <4 ; % of foreign bank assets (FBA)>60%
Yellow: Moderate Risk: -7.7%<CA< -2%; 5%<TDS<15%; 10%<FL&FA<20%; 4<Reserves<6 ; 30%<FBA<60%
Green: Low Risk: CA > -2%; TDS<5%; FL&FA <10%; Reserves>6 ; FBA<30%
Source: AfDB, 2009.

The stocks of foreign exchange reserves are also deteriorating. For example, in the DRC, reserves can only take care of only a few weeks of import cover. Going by the trend many countries will not be able to afford even basic commodity imports such as food, medical supplies, and agricultural inputs. The degree of financial integration varies widely across African countries. The ratio of liquid assets and liabilities to GDP is in the excess of 20 percent for 9 countries in 2007, but it is generally low for most African countries. Another measure of integration is the degree of foreign bank presence, which is a potential channel of contagion of financial distress. Foreign bank assets in Africa represent over 70 percent of total bank assets in 7 countries while nearly over 70 percent of banks are foreign in 11 African countries.

The crisis is also affecting the countries that had been experiencing several years of sustained growth built upon improved economic fundamentals and prudent fiscal policies. Botswana and Tunisia provide two instructive examples. Botswana has experienced a sharp decline in industrial production, export and government revenues. It has proved to be highly vulnerable to shocks due to its high dependence on diamond exports (representing 35 to 50 percent of government revenues). Its foreign reserves are falling rapidly, and the fall in mineral revenues is expected to be prolonged, limiting the government's ability to finance economic recovery plans. Its growth rate is expected to remain below 3 percent in 2009 and 2010. The crisis has underscored the critical role of export diversification in reinforcing the resilience of economies to external shocks. Tunisia has one of the most diversified economies in Africa. Nevertheless, it has experienced the full spectrum of the economic downturn from contraction in industrial production and exports to sharp declines in government revenues and foreign reserves. Key sectors of the economy have been affected, from manufacturing to tourism. As a result, its growth projections for 2009 have been revised downwards by 1.5 percentage points between November 2008 and February 2009.[4]

According to the African Development Bank (2009) the large, financially developed and open economies were the first to be hit by the crisis through financial markets (South Africa, Egypt) and exports (oil for Algeria and Nigeria, the mining sector for South Africa). For instance, in the early days of the crisis, the effects were mostly observed on the financial markets, with stock indexes losing substantially due to outflow of funds. Among African stock markets, the Nigeria Stock Exchange (NSE) lost 45.9 percent of its value, the All Share Indices for Mauritius (36.2%), Nairobi stock exchange (34.1%), and the Johannesburg Stock Exchange (25.7%) among others.[5] The crisis also was accompanied by widespread currency depreciations in the continent, on expectation of lower export revenues due to declining commodity prices, lower inflows of capital and short-term capital outflows. By the end of the year, nearly all African currencies except for the Angolan New Kwanza were at values below their levels at the end of 2007 in USD terms. Although many have appreciated recently, this has not been enough to fully offset the losses incurred earlier in the year.

For the African continent as a whole, inflation ended at higher levels in 2008 relative to 2007, at 8.8 percent compared to 7.4 percent. The 8.8 percent was 1.3 percentage point higher than anticipated before the financial crisis. In contrast, inflation is expected to be lower in 2009 (6.2%). This is attributable to the decline in oil prices, which will ease pressure in oil importing countries. However, despite the fall in oil prices, inflationary pressures remained in many countries. This could be attributed to persistent high food prices and supply side bottlenecks. Inflation seems to have increased faster among non-resource rich countries compared to oil exporters and minerals exporters (Figure 2).

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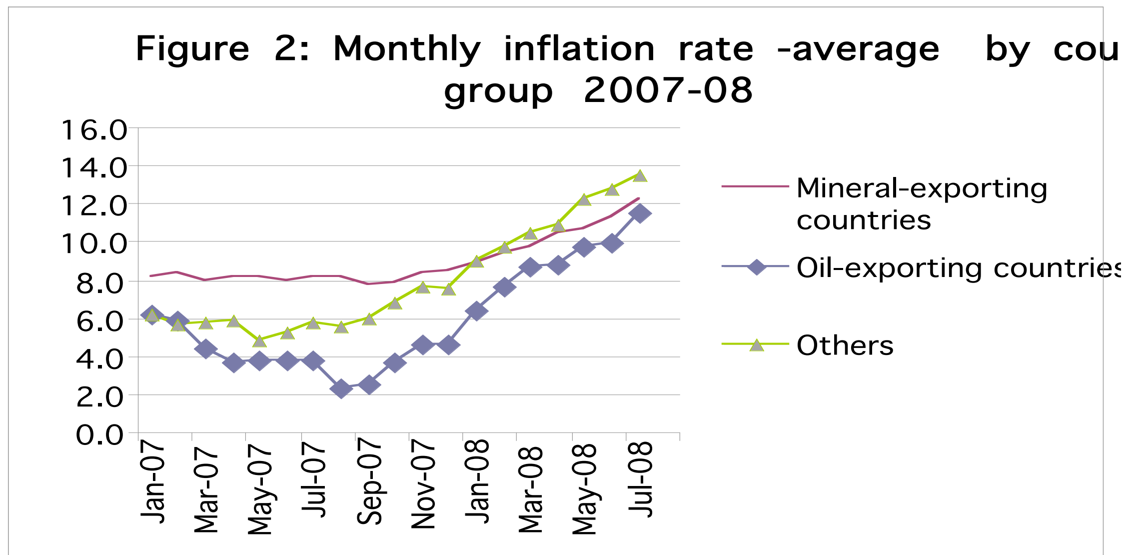
[4] Committee of African Finance Ministers and Central Bank Governors (2009).

[5] Between May 2008 and March 2009, South Africa's JALSH index has fallen by about 46 percent and the Rand depreciated by 23 percent against the US dollar.



Source (AfDB, 2009)

Expectedly, the crisis has led a slowdown in capital inflows into the continent and substantial constant outflows of short-term capital. Capital inflows in the form of foreign direct investment (FDI), which have been another important driver of recent growth, are also declining. In addition, migrant remittances, which have become an important source of external financing for African countries, have been affected by the economic downturn in developed countries. Intra-Africa remittances are declining as well due to job losses following the decline in the mining sector. The decline in remittances has direct negative effects on household welfare given that, unlike other transfers, remittances are directly used for covering basic needs such as food, education, and health (AfDB, 2009). Individual countries are also experiencing a slowdown in migrant remittances. Remittances in Kenya have been steadily falling since October 2008 from USD 61 million to USD 39 million in January 2009. Tourism receipts were down 13 percent in the 4th quarter of 2008 compared to 2007, further undermining the country's efforts to build up its foreign exchange reserve base (CFM&CBGs, 2009).

Public finances are being affected by the financial and economic crisis through lower revenue, which is making it difficult for countries to maintain the planned levels of public expenditures, including long-term infrastructure investment as well as social expenditures. The decline in revenues manifested especially among oil and mineral resource exporters due to the decline in prices.[6] Several oil-producing countries have been forced to severely curtail their public expenditure plans, including public infrastructure investment, due to lower fiscal revenues. The AfDB (2009) report noted that in Angola, government revenue for 2009 is expected to be 24 percent lower compared to 2008. The non-oil sectors, such as construction, manufacturing and services, are heavily dependent on public sector demand and are also expected to slow down considerably. The Angolan economy is expected to contract by 7 percent in 2009, following a double digit growth rate in 2008 (15.8%), a reversal of almost -23 percent.

[6]Between 2007 and 2008 many primary commodities experienced drastic decline in prices. Nevertheless, the prices of some commodities increased overall on a year-on-year basis, notably phosphate, iron, and tea (See Table 1).

3.2 Are Primary Commodity Exports the Culprit?

The recent economic slowdown being witnessed can however be attributed to the declining trade flows. The dependency on (narrow range of) primary commodities for export is largely responsible for the impact of the slowdown on African countries. Primary commodities dominate African exports. Except for Botswana, Lesotho, South Africa and Mauritius that had a significant part (over 50 per cent) of their export being dominated by manufactured good, virtually all the other African countries have their exports being dominated by the all food item and agricultural raw materials (Table 4). Nigeria, Cameroon, Gabon and Angola had a significant part of their exports in fuels with a low percentage share in the manufactured exports category.

The decline in demand for major export products which are of crucial importance to African countries and the reliance on a narrow range of unprocessed primary commodity exports have made African countries vulnerable to market fluctuations and weather problems[7] (See Table 5). For example, Nigeria's investment, output and government revenues have fallen significantly due to declining prices for hydrocarbons (oil and gas). Oil and gas extraction account for 30 percent of the economy's GDP, over 90 percent of its exports and a large share of government revenues. Also, in the late 1990s, 39 African countries depended for more than half of their export earnings on just primary commodities. In addition, the collapse of world commodity prices in 1998 was equivalent to a real income loss of 2.6 percent of African GDP between 1997 and 1998 (UNCTAD, 1999). Thus, supply shocks with its attendant problem of price volatility, and the resulting terms of trade losses have culminated in heavy income losses, indebtedness, lack of investment, poverty and underdevelopment among African countries.

Excessive specialization in minerals has proven to be even more disastrous for countries with poor governance and weak state institutions. This is the case with the DRC and the Central African Republic. Lower demand and prices for commodities are compounded by high economic and political uncertainty. Risk aversion has induced investors to relocate to lower risk countries, resulting in sharp decline in foreign direct investment (FDI). The combination of falling export revenues, weak governance capacity, and a prolonged retrenchment in investment aggravates already widespread poverty and threatens the stability of these fragile states.

Table 4: Export Structure of Selected Africa Countries by Major Commodity Groups

Country/ Year	Total value (millions of dollars)	All food items	Agricultural raw materials	Fuels	Ores and metals	Manufactured goods	Chemical products	Other manufactured goods	Machinery and Transport equipment
Angola									
1990	3910	0.2	0	93.5	6.2	0.1	0	0.1	0
Benin									
1995	333	11.8	38.9	2.8	38.9	6.6	0.2	4.9	1.5
2000	188	20.1	69.7	0	0.1	7.1	0.7	5.1	1.3
2002	304	37.2	45.1	0.4	0.1	8.5	0.7	6.5	1.2

[7] Drought, famines and natural disasters have been prevalent in many African countries. These phenomena divert scarce resources from directly productive activities. Examples of countries that have suffered unmitigated natural disasters include Niger, Burundi, Cote d'Ivoire, Kenya and Ethiopia among others. The government should mitigate this problem by putting structures in place to anticipate such natural disasters.

Botswana									
2000	2763	2.8	0.3	0.1	7	89.5	0.9	85.1	3.5
2001	2533	3.1	0.5	0.1	5.5	90.6	1.2	86.5	2.9
Burkina Faso									
1995	171	22.1	59.1	1.6	0.3	8.6	0.4	5	3.1
2000	184	18.8	58	3.2	0	18.1	1.7	11.8	4.6
2002	171	19.4	61.5	0	0.1	0.1	18.3	0.6	12.3
Cameroon									
1990	2081	20.4	14.3	49.9	6.9	8.5	1.5	4.7	2.3
1995	1539	27	27.5	29.2	8.4	7.9	1	5.8	1.1
2000	1833	14.9	21	54.2	5.6	4.3	0.4	3.3	0.5
2003	2246	19.9	19.5	49.4	4.2	6.9	0.9	4.8	1.2
Congo									
1995	1090	1	8.3	87.6	0.3	2.7	0.3	2.1	0.4
Côte d'Ivoire									
1995	3737	58.7	16	9.8	0.2	14.2	4.2	8.6	1.4
2000	3628	49.8	13.8	20.3	0.2	14.4	4.1	9.2	1
2003	5493	55.6	9.2	12.8	0.2	20	4	6.2	9.7
Ethiopia									
1995	422	72.5	13.4	2.9	0.1	11.2	0.3	10.8	0
2000	482	66.5	17.6	0	0.9	9.2	0	9.1	0.1
2003	513	62	25.9	0	0.7	11.4	0	11.3	0
Gabon									
2000	2602	0.8	11.8	83.3	1.7	2.3	0.1	1.8	0.4
2003	2826	0.5	5.5	88.4	1.1	4.6	0.1	2.4	2.2
Gambia									
1995	19	58.8	0.5	0.2	1	36.8	2.4	27.5	7
2000	16	80.8	1.2	0.1	0.2	17	9.6	2.6	4.7
2003	5	63.3	7.3	0.8	1.6	27	1.3	11.4	14.4
Ghana									
2000	1671	30.7	6.5	4.9	11.9	9.3	0.6	7.5	1.2
Guinea									
1995	702	7.4	1.1	0.5	63.7	24.9	18.2	4.6	2.1
2000	522	2.5	2.4	0	51.7	24.7	10.9	12.9	0.9
2002	525	1.5	0.6	0.1	53.9	19	17.1	1.8	0.1
Kenya									
1990	1028	48.8	5.5	13.1	2.9	29.7	4.2	14.9	10.6
1995	1826	56.1	7.3	6.1	2.8	27.6	6.5	19.5	1.6
2000	1571	59	8.6	8.1	3.2	20.7	5.5	14.6	0.5
2004	2686	39.6	12	22.9	4.2	21	4.2	15.2	1.7
Lesotho									
2000	336	4.7	0.1	0	0	94.9	0.3	86.9	7.7
2002	358	7.1	5.1	0	0.1	87.4	0.6	81.7	5.1
Madagascar									
1990	292	72.8	3.7	0.5	7.7	14.4	1.5	11.1	1.8
1995	360	67.3	5.8	4	6.8	14.1	2.1	11.1	0.9
2000	817	32.8	3.4	3.3	1.8	58.2	0.8	56.6	0.8

2003	766	55.5	3.6	0.4	1.5	38.4	1	36.9	0.5
Malawi									
1990	412	90.8	1.9	0	0	7.1	0.4	3.8	2.8
1995	433	88	2.1	0.1	0.1	9.7	0.4	7.3	2
2000	369	89.4	3	0.2	0.2	7.1	0.7	5.5	1
2003	457	86.1	2	0	0.1	11.8	1	10.2	0.6
Mali									
1990	330	36.1	62.3	0	0	1.6	0	0.6	0.9
2000	473	1.7	34.4	1	0.2	4.8	0.5	1.5	2.8
2001	519	1.6	3.7	1.9	0	9.2	0.6	1.9	6.7
Mauritius									
1990	1221	31.9	0.5	1.4	0.2	65.8	0.9	63.5	1.4
1995	1538	28.6	0.7	0	0.2	70.2	0.8	67.1	2.3
2000	1490	17.8	0.5	0	0.2	80.8	0.9	78.6	1.3
2004	1925	26.9	0.5	0.1	0.4	70.9	1.7	64.5	4.7
Mozambique									
2000	364	42.9	11.3	21	17.3	6.8	0.2	3.5	3
2002	663	19.1	5.6	16.4	54.7	3.1	0.1	1.7	1.3
Nigeria									
2000	27079	0.1	0	99.6	0	0.2	0	0.1	0.1
2003	24078	0	0	97.9	0	2.1	0.1	0.2	1.8
South Africa									
2000	26075	8.5	3.8	10.2	10.7	53.9	7.8	28.6	17.5
2004	40206	8.7	2.8	9.1	22	56.5	7.8	29	19.7
Uganda									
1995	575	86	4.4	0.1	0.6	4.2	1	2	1.2
2000	402	60.1	12.5	7.1	4.1	5.3	1.1	1.8	2.5
2004	639	58.1	14	4.2	0.3	13.8	2.6	7.2	4
Zambia									
1995	1055	2.7	0.6	3.3	86.5	6.9	0.2	5.2	1.5
2000	666	10.2	3.6	1.6	55.5	27.7	0.5	23.7	3.4
2002	930	9.2	2.8	2.1	63.6	19.2	1	13.3	4.9

Source: UNCTAD Handbook of Statistics (2004). Table 3.2.1a, 3.2.1b, 3.2.1d, 3.2.1h.

Table 5: Major Exports of Selected African Countries

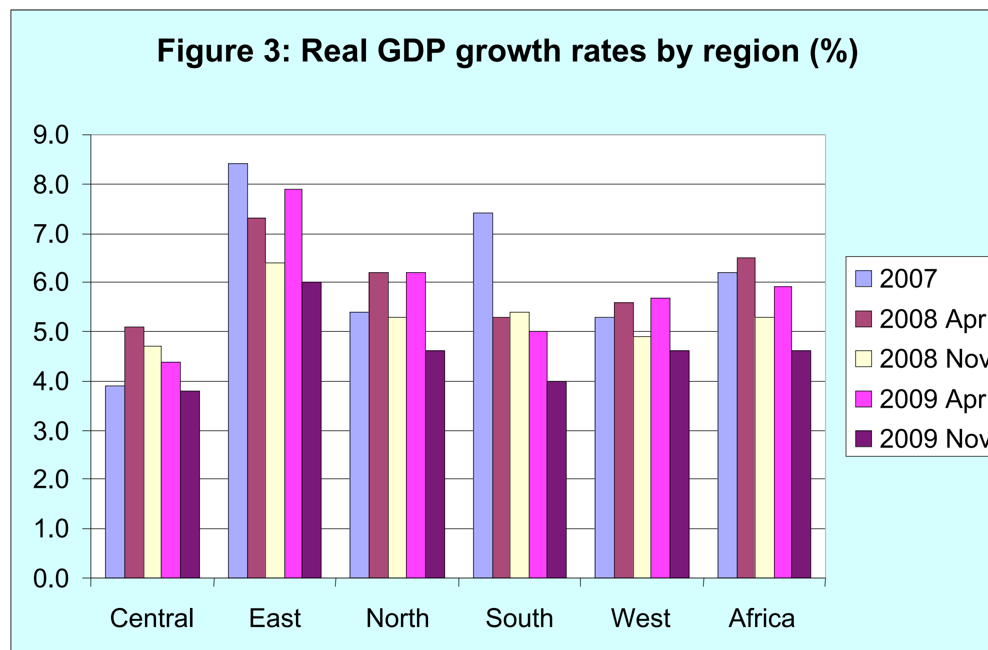
Country	Commodity Exports
Benin	Cotton, Crude oil, Palm products, Cocoa
Botswana	Diamonds, Copper, Nickel, Soda ash, Meat, Textiles
Burkina Faso	Cotton, Livestock, Gold
Burundi	Coffee, Tea, Sugar, Cotton, Hides
Cameroon	Crude oil and petroleum Products, Lumber, Cocoa beans, Aluminum, Coffee, Cotton
CAR	Diamonds, Timber, Cotton, Coffee, Tobacco
Cote d'ivoire	Cocoa, Coffee, Timber, Petroleum, Cotton, Bananas, Pineapples, Palm oil, Fish
Ethiopia	Coffee, Qat, Gold, Leather products, Live animals, Oilseeds
Gabon	Crude oil (77%), Timber, Manganese, Uranium (2001)
Gambia	Peanut products, Fish, Cotton lint, Palm kernels, Re-exports
Kenya	Tea, Horticultural products, Coffee, Petroleum products, Fish, Cement
Malawi	Tobacco (60%), Tea, Sugar, Cotton, Coffee, Peanuts, Wood products, Apparel

Mali	Cotton, Gold, Livestock
Nigeria	Petroleum and petroleum products (95%), Cocoa
South Africa	Gold, Diamonds, Platinum, Other metals and minerals, Machinery and equipment
Zambia	Copper/cobalt (64%), Cobalt, Electricity; Tobacco, Flowers, Cotton
Zimbabwe	Cotton, Tobacco, gold, ferroalloys, textiles/clothing
Uganda	Coffee, fish and fish products, tea, cotton, flowers, horticultural products; gold

Source: CIA World Fact book, 2005.

3.3 Impact of the Crisis: Matters Arising

The greatest worry with respect to the impact of the financial crisis on African economies is its negative impact on growth and the resulting consequences on living standards. The crisis will reverse the achievements by African countries in raising growth rates, a key condition to reducing poverty. Real GDP growth is expected to fall to 4.6 percent in 2009 from 6.2 percent in 2007 as a result of the slowdown (Figure 3). The growth forecast of 4.6 percent for 2009 has been revised downward by 1.3 percent point from 5.9 percent. Compared to the 2007 benchmark, Southern Africa region will be hit the hardest with its forecast growth rate falling to 4.0 percent in 2009, which is a full percentage point lower than projected before the crisis (5% and down from 7.4% in 2007). This reflects Angola's growth declining from 20.9 percent in 2007 to 7.6 percent in 2009. The second sub-region to be hit most relative to 2007 is East Africa, with a projected growth rate of 6 percent in 2009 down from 8.4 percent in 2007 (AfDB, 2009). The breakdown of the countries real GDP growth performance before and after the crisis is presented in Table 6.



Source :AfDB, 2009.

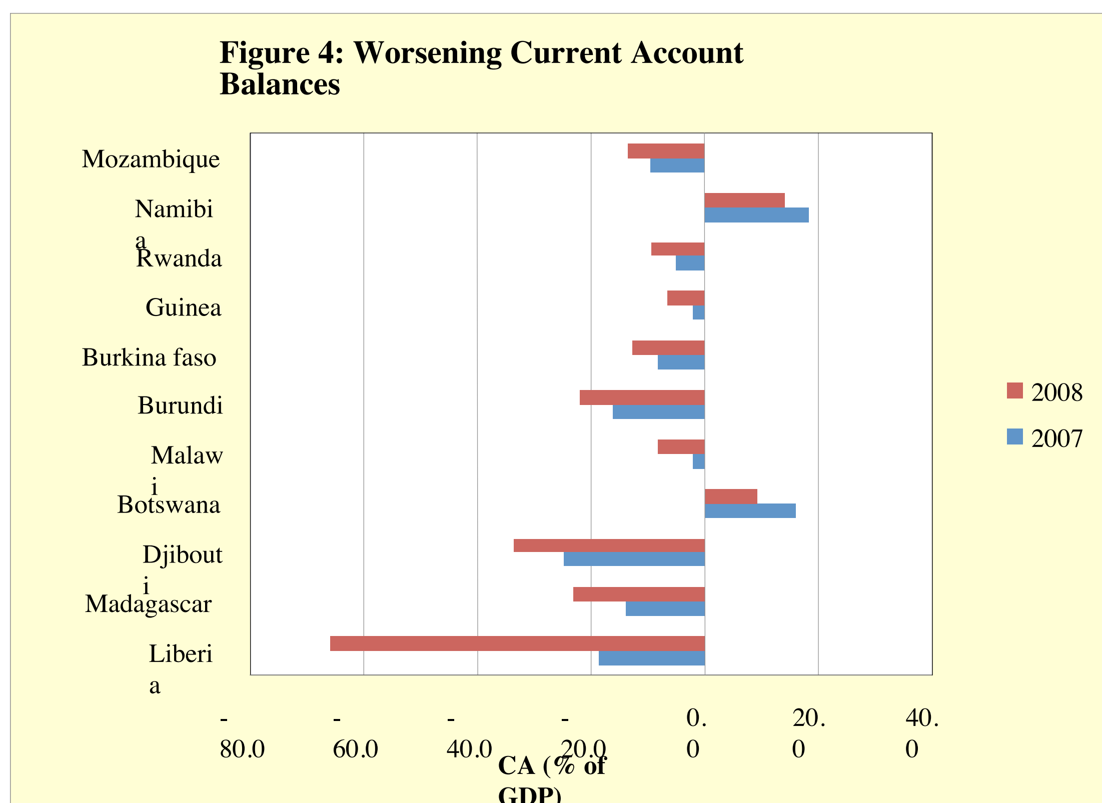
Table 6: Real GDP Growth (%): Data before and after Crisis

	Real GDP growth				GDP change
	Before crisis		After crisis		
	2008 (e)	2009 (p)	2008 (e)	2009 (p)	2008-2009
Algeria	4.8	4.8	3.3	0.2	-3.1
Angola	11.5	5.1	15.8	-7.2	-23.0
Benin	4.9	5.3	5.0	5.3	0.3
Botswana	5.3	5.2	3.9	2.6	-1.3
Burkina Faso	4.7	5.8	4.2	6.0	1.8
Burundi	5.8	5.6	3.2	2.9	-0.3
Cameroon	4.8	4.6	4.1	3.1	-1.0
Cape Verde	7.6	7.0	6.1	3.6	-2.5
Central African Rep.	4.0	4.5	2.6	3.2	0.7
Chad	3.2	-0.7	0.2	-0.7	-0.9
Comoros	4.5	4.5	0.5	0.8	0.3
Congo, Republic of	6.4	6.4	7.0	7.7	0.8
Congo, Dem. Rep. of	6.6	7.1	5.7	-0.6	-6.3
Côte d'Ivoire	2.8	3.8	2.3	3.8	1.5
Djibouti	5.6	5.6	5.9	6.5	0.6
Egypt	6.8	6.7	7.2	4.3	-2.9
Equatorial Guinea	5.8	4.1	9.9	3.7	-6.2
Eritrea	1.3	1.1	1.2	1.6	0.4
Ethiopia	7.5	7.4	11.6	6.5	-5.1
Gabon	4.2	4.1	5.5	4.0	-1.5
Gambia, The	6.0	6.0	5.7	5.0	-0.7
Ghana	6.0	6.3	6.4	5.8	-0.6
Guinea	5.0	5.0	4.7	3.8	-1.0
Guinea-Bissau	2.1	2.2	3.2	3.1	-0.1
Kenya	4.0	6.5	2.6	5.0	2.4
Lesotho	5.2	5.4	4.2	3.8	-0.3
Liberia	9.2	11.0	7.3	10.8	3.5
Libya	8.0	7.8	6.5	3.4	-3.1
Madagascar	6.5	6.7	7.0	4.8	-2.2
Malawi	5.1	5.5	8.4	6.5	-1.9
Mali	4.7	4.8	3.6	4.2	0.6
Mauritania	5.0	5.0	5.2	3.4	-1.8
Mauritius	5.0	4.9	4.8	3.0	-1.8
Morocco	6.0	6.1	5.7	5.4	-0.2
Mozambique	7.0	6.8	6.2	4.0	-2.2
Namibia	4.4	3.3	3.4	2.7	-0.7
Niger	4.7	4.5	4.8	1.8	-3.0
Nigeria	6.2	6.1	6.1	4.0	-2.2
Rwanda	4.0	5.6	8.5	6.6	-1.9
São Tomé & Príncipe	6.0	6.0	5.8	6.0	0.2
Senegal	4.9	4.6	3.7	3.5	-0.2
Seychelles	5.9	4.2	1.5	-0.4	-1.9
Sierra Leone	6.5	6.5	5.4	6.3	0.9
Somalia	…	…	…	…	…
South Africa	4.0	4.9	3.1	1.1	-2.0
Sudan	10.7	11.0	8.4	5.0	-3.4
Swaziland	1.0	1.0	2.6	2.5	-0.2
Tanzania	6.5	6.7	6.8	6.1	-0.7

Togo	3.5	3.9	0.8	3.9	3.1
Tunisia	5.5	5.6	5.1	4.1	-1.0
Uganda	6.2	6.3	7.0	5.6	-1.3
Zambia	6.3	6.4	5.5	2.8	-2.7
Zimbabwe	-4.5	-4.0	-5.2	-5.6	-0.4

Source: AEO 2009 Projections. World economic outlook Database, October 2008 and FAO
Note: (p) Projections; (e) Estimation
Source: Committee of African Finance Ministers and Central Bank Governors (2009)

Macroeconomic balances in many African countries have also been worsened. This is evidenced in rising current account deficits, budget deficits, and inflation. The current account deficit has worsened between 2007 and 2008 in 32 countries, some experiencing deep declines (Figure 4). This is especially the case for Liberia (from 18.7% of GDP to -65.9% of GDP), Madagascar (from -13.9 to -23.1%), Djibouti (from -24.8% to -33.5%), Malawi (from -2.1% to -8.2%) and Burundi (from -16% to -21.9%). More detailed countries evidence is reported in Table 7. These countries will experience difficulties financing these widening current account deficits in the context of declining capital inflows.



Source: AfDB, 2009.

Furthermore, the crisis seems to be hitting some of the key sectors that have driven growth over the past years, especially those that are predominantly export oriented. This is especially the case for the mining sector, tourism, and sections of the manufacturing sector. Mining companies have

been forced to scale back production and lay off workers due to decline in demand. The African Development Bank (2009) reported that in the Democratic Republic of Congo (DRC), most of the 61 foreign mining companies were forced to scale back, postpone or abandon their investment plans. Affected mining firms have taken various actions, including suspension of operations (copper and cobalt) and withdrawal of exploration agreements (diamond). Similar difficulties are observed in other countries where mining activities constitute large shares of economic activity, such as South Africa, Botswana, and Zambia. The slowdown in the mining sector is causing employment losses. For example, by December 2008, the DRC Ministry of Mines had reported that more than 200,000 jobs had been lost in the mining sector. A further 200,000 were expected to lose their jobs in the early months of 2009.

In the Democratic Republic of Congo, 100,000 jobs have been lost due to smelter closures. Also, in the Central African Republic exports of wood and diamonds have collapsed, causing large losses of employment. The Société d'Exploitation Forestière en Centrafrique (SEFCA) has laid off half of its employees as its orders were cut by half. The economy is basically on life support. Regional neighbors have contributed CFA 8 billion (more than USD15m) as the government was unable to pay the salaries of civil servants. Debt arrears are accumulating, further undermining the country's capacity to mobilize external resources. This situation is clearly threatening the stability of a country that is just coming out of conflict.

Nevertheless, the expected short fall in export revenues for Africa is immense: USD 251 billion in 2009 and USD277 billion in 2010. Oil exporters will take the biggest hit, with a shortfall of USD 200 billion in 2009 and USD220 in 2010 (Table 7). With exports declining faster than imports, the trade balance will deteriorate in most countries. Exports for 2009 and 2010 have been revised downwards by 40 percent. As a result, from a comfortable overall current account surplus of 2.7 percent of GDP for both 2008 and 2007, the continent will record an overall deficit of 4.3 percent of GDP in 2009.

Table 7:Export Revenue and Current Account Balance: Data Before and

Country	**Exports of Goods (USD Billion)**						**Current Account Balance (As % of GDP)**			
	Before crisis		**After Crisis**		**Estimated Shortfall**		**Before crisis**		**After Crisis**	
	2009(p)	**2010(p)**	**2009(p)**	**2010(p)**	**2009(p)**	**2010(p)**	**2009(p)**	**2010(p)**	**2009(p)**	**2010(p)**
Algeria	84.42	86.35	46.87	43.62	40.79	39.48	19.84	18.01	5.60	7.00
Angola	78.63	90.52	40.43	45.91	38.19	44.61	15.91	16.44	-8.13	-7.00
Benin	0.45	0.51	0.33	0.34	0.12	0.17	-8.14	-6.86	-7.82	-8.32
Botswana	5.31	5.45	4.77	4.77	0.54	0.68	7.61	6.34	11.54	10.14
Burkina Faso	0.90	1.03	0.74	0.78	0.17	0.25	-12.13	-10.23	-8.69	-8.69
Burundi	0.06	0.07	0.06	0.06	0.01	0.01	-14.83	-13.27	-8.36	-12.38
Cameroon	4.75	4.60	4.09	4.35	0.66	0.25	-1.10	-2.40	0.22	0.24
Cape Verde	0.12	0.12	0.08	0.08	0.04	0.04	-10.87	-10.73	-9.62	-6.63
Central African Rep.	0.24	0.26	0.15	0.15	0.10	0.11	-5.91	-5.62	-7.38	-8.09
Chad	4.53	4.38	2.00	2.24	2.54	2.13	-1.84	0.89	-3.75	1.44
Comoros	…	…	…	…	…	…	-9.55	-9.12	-9.55	-9.12
Congo, Dem. Rep. of	7.23	9.26	4.33	4.76	2.91	4.51	-12.58	-5.29	-27.40	-22.59
Congo, Republic of	14.57	16.69	7.28	8.10	7.30	8.59	21.41	25.27	-2.95	-2.24
Côte d'Ivoire	11.45	12.16	7.85	8.38	3.60	3.78	-0.58	-0.95	-0.33	-1.33

Djibouti	0.11	0.13	0.09	0.09	0.02	0.04	-32.86	-27.50	-20.69	-19.23
Egypt	35.03	37.90	24.36	25.21	10.68	12.69	-0.86	-1.67	-1.24	-1.78
Equatorial Guinea	15.22	14.77	7.71	8.57	7.51	6.21	2.78	0.87	-0.03	1.06
Eritrea	0.03	0.12	…	…	…	…	-2.15	-0.27	-2.15	-0.27
Ethiopia	1.68	1.78	1.22	1.37	0.46	0.41	-5.25	-4.73	-5.04	-3.74
Gabon	11.19	11.14	6.49	7.11	4.71	4.02	18.09	16.02	-3.54	3.36
Gambia, The	0.11	0.11	0.07	0.08	0.03	0.04	-12.50	-11.98	-8.84	-9.96
Ghana	5.66	5.92	4.72	4.84	0.94	1.08	-13.17	-12.68	-13.15	-17.86
Guinea	1.63	1.78	1.18	1.27	0.45	0.51	-6.73	-5.51	-1.63	-1.20
Guinea-Bissau	0.12	0.13	…	…	…	…	-11.56	-10.55	-11.56	-10.55
Kenya	5.64	6.32	5.03	5.08	0.61	1.25	-4.49	-4.85	-0.39	0.08
Lesotho	0.91	1.04	0.69	0.75	0.22	0.28	-1.41	-2.86	8.94	1.39
Liberia	0.73	1.18	0.37	0.41	0.36	0.77	-43.91	-29.27	-5.70	6.98
Libya	67.90	78.13	30.80	34.30	37.10	43.83	29.45	28.33	3.31	6.52
Madagascar	1.78	2.87	1.05	1.24	0.73	1.63	-21.15	-9.68	-21.03	-22.90
Malawi	1.00	1.11	0.69	0.72	0.31	0.39	-5.40	-6.42	-2.82	-5.88
Mali	1.76	1.78	1.81	1.73	-0.06	0.05	-6.92	-6.59	-0.95	-3.67
Mauritania	2.17	2.08	1.50	1.49	0.66	0.59	-2.97	-11.23	-13.18	-14.52
Mauritius	2.72	2.85	2.30	2.38	0.42	0.48	-6.58	-5.72	-6.14	-6.37
Morocco	21.52	22.71	17.11	19.13	4.41	3.58	-0.34	-0.79	-1.97	-3.15
Mozambique	2.93	3.05	2.39	2.94	0.55	0.11	-13.27	-13.05	-14.02	-11.22
Namibia	3.58	3.65	2.32	2.49	1.25	1.16	12.41	10.20	2.69	1.42
Niger	1.03	1.19	0.54	0.58	0.49	0.61	-20.56	-22.52	-15.40	-16.30
Nigeria	89.08	99.47	50.40	55.31	38.68	44.16	0.61	-0.50	-9.05	-6.44
Rwanda	0.26	0.29	0.22	0.25	0.05	0.04	-12.43	-11.47	-5.87	-6.23
São Tomé &Príncipe	0.00	0.00	0.00	0.00	0.00	0.00	-34.49	-33.44	-34.49	-33.44
Seychelles	0.41	0.42	0.39	0.40	0.02	0.02	-35.11	-38.40	-21.54	-20.03
Senegal	2.83	2.97	1.67	1.71	1.17	1.26	-11.44	-12.10	-8.72	-9.76
Sierra Leone	0.40	0.45	0.44	0.48	-0.04	-0.03	-4.18	-4.29	-4.37	-4.55
Somalia	…	…	…	…	…	…	…	…	…	…
South Africa	96.12	101.82	68.25	70.84	27.87	30.98	-8.15	-8.33	-6.36	-7.64
Sudan	13.15	15.23	7.64	8.82	5.51	6.41	-6.73	-6.80	-13.83	-15.86
Swaziland	1.74	1.80	1.53	1.64	0.21	0.17	-2.02	-2.64	15.38	7.94
Tanzania	2.77	3.10	2.21	2.23	0.56	0.87	-9.97	-9.74	-9.69	-10.43
Togo	0.96	1.05	0.77	0.80	0.20	0.25	-8.48	-7.13	-1.08	-2.19
Tunisia	22.02	24.55	16.99	18.60	5.03	5.95	-3.46	-3.29	-3.23	-2.53
Uganda	1.91	2.05	1.79	1.82	0.13	0.23	-5.83	-6.17	-7.30	-8.90
Zambia	5.76	5.62	2.73	3.00	3.04	2.62	-6.60	-7.00	-17.01	-17.28
Zimbabwe	…	…	…	…	…	…	…	…	…	…
AFRICA	**634.56**	**691.95**	**383.17**	**414.45**	**251.24**	**277.25**	**1.90**	**1.56**	**-4.37**	**-4.12**

Note: AEO 2009 Projections. World economic outlook Database, October 2008;
Notes: Data for Zimbabwe, Somalia, Sao Tome, Guinea Bissau, Eritrea and Comoros are not available.
Negative shortfall implies a surplus position. (p) Projections

Source: Committee of African Finance Ministers and Central Bank Governors (2009)

The manufacturing sector has been affected by both declining global demand and increase in the cost of import of inputs due partly to currency depreciation. Thus factories are running at lower capacity and employment is threatened severely. For example, in Uganda**,** the Manufacturers Associations (UMA) reported that 15 factories closed in 2008 due to the high cost of doing business. Most of these firms were in fish, leather processing, grain and tobacco dealing. Lesotho is also experiencing a decline in clothing and textile exports after a recovery from the end of the MFA in 2005. Tourism has suffered substantially from the crisis as well, with substantial declines in tourism arrivals and receipts, hotel bookings, and air travel. Kenya Airways reported a decline in profits by 62.7 percent for the six months ending September 2008. The decline in tourism activity will reverse the recent gains by the service sector which is

becoming an important driver of growth. This calls for efforts toward more diversification within the service sector as well as economy wide.

The drying up of liquidity in international financial markets has hit the private sector as well as governments. For governments, attempts to raise long-term finance through sovereign bond issue have failed (South Africa), been canceled (Ghana Telecom bond issue for USD300 million) or delayed (Eurobond issues for Kenya, Nigeria, Tanzania and Uganda). This has caused costly delays in the implementation of planned public infrastructure programs. The impact of the crisis on the private sector has been worsened by the tightening of credit markets due to shortage of bank liquidity as well as the rise in uncertainty. Thus, African banks are having difficulties securing lines of credit on international markets. Similarly, governments that had planned to raise long-term finance through sovereign bond issues have had to hold back their plans due to the rise in risk and costs. The shortage of financing is particularly affecting trade financing and financing for large infrastructure investment, both of which will have drastic effects on the continent's growth prospects (AfDB, 2009).

A number of private sector projects across Africa have actually been suspended or delayed because some investors withdrew and the funding conditions became more constraining due to higher spread and lower debt-to-equity exposure (Table 8). A gas project in North Africa was suspended after its approval by the Bank in October 2008 because the financing could not be closed. Moreover, seven infrastructure projects, where the African Development Bank (AfDB) has been approached to provide funding, are currently delayed because of the crisis. The financial crisis has led to an increase in the demand for AfDB's funding for private sector operations. The AfDB has been asked to step in several projects, some of which where it was already involved, to provide additional funding. The Bank has recently granted two loans extensions of EUR 70 million and USD 48.75 million, and a proposal for another UA 229 million loan extension will be considered soon (CAFM&CBGs, 2009).

With respect to agriculture dependent economies, the financial crisis has amplified the impacts of the food crisis. The depreciation of national currencies against major reserve currencies has raised the cost of food imports. This impact will be particularly harder on economies that have large deficits in food trade. Urban populations have been particularly affected as job opportunities shrink. Attempts to subsidize food and oil prices are unsustainable due to low government revenues and falling foreign exchange reserves. Ethiopia, for example, has been steadily losing its reserves in the past few months. In turn, credit to the private sector has declined considerably since the third quarter of 2008 as the government increased its domestic borrowing to finance the oil subsidy bill. In just six months (August 2008 to February 2009) Kenya's total usable reserves (official plus commercial banks holding) fell from USD 5,287 million in to USD 4,726 million. Over the same period Kenyan Central Bank's reserves holding declined from 4.1 months of imports to 3.1 months (below the statutory requirement of 4 months). By end February 2009, the Kenyan shilling had depreciated by 15.7 percent against the US dollar relative to September 1, 2008 (AfDB, 2009 and CAFM& CBGs, 2009).

Taking a brief overview of the issues raised above, it is obvious that the fall in international demand for primary commodities has made their prices to collapse with government revenue being affected negatively. In addition, current account and fiscal positions had become negative while support for agriculture (and other social services) in actual fact had decline further

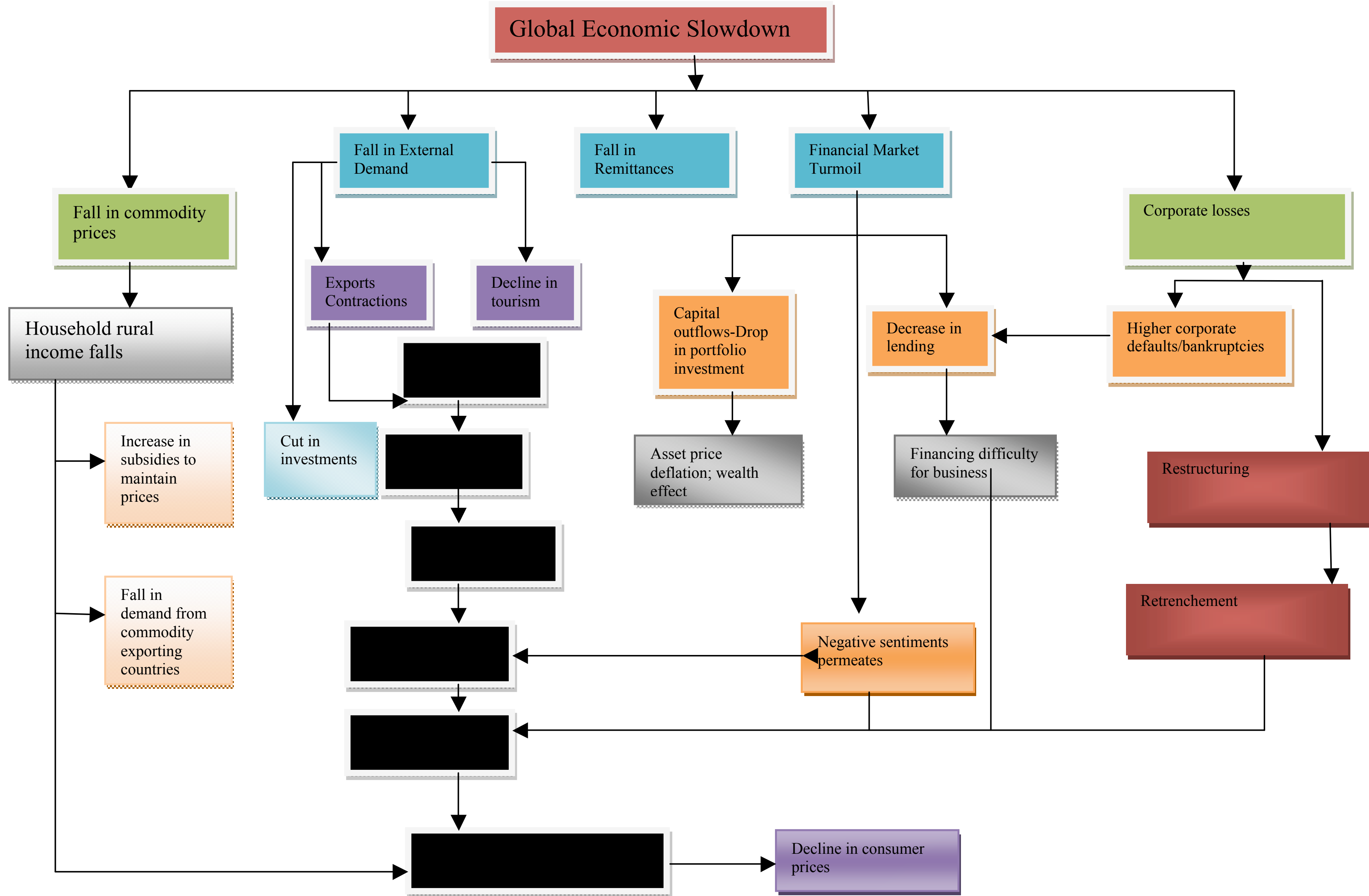
reducing agricultural productivity (and therefore export), which has further aggravate the crisis- this has turn into a cycle of economic decline for Africa.

Table 8: Selected Projects Expected To Be Cancelled or Postponed

Country	Detail on project
Algeria	In December 2008 the Government postponed the date of submission of tenders for the modernization of Skikda and El Harrach refineries to 1Q 2009. These projects could be delayed.
Botswana	A USD 6 billion coal fired power project delayed.
Burkina Faso	Out of six mines scheduled to start in 2009, three mining companies are having difficulties mobilizing funds needed to begin operations.
Ethiopia	Non-sovereign financing of a large hydropower project of EUR 1.5 billion is lagging. A private investment bank had earlier expressed interest but has withdrawn due to the crisis impacting its appetite for emerging markets.
Ghana	Attempted sale of Volta Aluminum Company Limited (VALCO), an aluminum smelter, collapsed due to withdrawal of one party to the deal
Guinea	Investments delayed in mining projects
Kenya	- A renewable energy project for 300MW delayed - A Toll Road in Kenya of a total cost of around USD800 million delayed.
Senegal	- A Toll Road delayed - A new greenfield airport of EUR 400 million cost delayed.
Sierra Leone	Construction projects may be delayed
Sudan	Petronas decided to put its Port Sudan refinery project on hold.
Tanzania	Rio Tinto and Vodacom have postponed investments in mining projects
Tunisia	Gas field development project being restructured (total project cost is USD1.2 billion) Transshipment deep sea port project likely to be delayed
Uganda	14 medium scale companies closed in 2008 and 15 more expected to close in 1Q 2009. The government will divert money from planned road projects to other sectors.
West Africa(regional project)	A telecommunication project in West Africa for USD240m: One of the potential shareholders may withdraw and cost of commercial debt has increased sharply.

Source: Committee of African Finance Ministers and Central Bank Governors (2009)

Figure 5: Transmission Framework of the Global Slowdown from Developed economies to Africa[8]



[8] ADB (2009) and Authors' expression

4. Policy Response of African Countries to the Crisis and Way Forward

The adverse developmental impact of the financial and economic crisis is large and might likely outlast the crisis. In particular, the deceleration of income growth will undermine the modest gains in poverty reduction that many African countries have recorded over the past few years. Efforts to sustain these gains will involve a combination of strategies at the national and sub-regional level and the support from Africa's development partners in terms of delivery of committed aid as well as incentives to encourage private banks and companies in developed and emerging countries to invest in Africa. In the short run, Africa's recovery from the current global downturn will depend on the ability to mitigate effects of procyclicality, revitalize domestic drivers of growth, reduce vulnerability on the external sector and boost domestic resource mobilization to support investment and trade. However, long-term strategies must be oriented toward building more resilience to crisis and sustaining growth.

Nevertheless, African governments have taken a number of initiatives to mitigate the impact of financial and trade shocks. However its limited resources are inadequate in relation to the scale of the impact. Many governments have set up special monitoring units to identify the advance of the crisis and to formulate targeted responses. In addition, governments have introduced a range of policy measures including fiscal stimulus packages, targeted assistance to sectors, capital and exchange controls; new regulations in the banking sector and expansionary monetary policies (see Table 9).

Table 9: Crisis Mitigation Strategies in Selected Countries

Countries	Mitigating Measures by Government
Botswana	• The Central Bank cut its rate by 50 basis points to 15 percent in December 2008. • In the face of uncertainty as to the duration of the global economic slowdown, the cushion provided by the foreign exchange reserves may not be sufficient; some increase in borrowing is expected. • Reductions in spending targeting not only the development budget, but also some recurrent expenditure items, such as personnel emoluments and the cost of travel.
Cape Verde	• Dialogue with the IMF which adjusted the criteria of performance of the PSI • Careful management of the interest rates and the budget • Development of the Treasury bills to encourage the saving to remain in the national financial system.
Egypt	• Ministry of Trade & Industry EGP7 billion to boost exports and local production • Crisis package for tourism sector, including tax-exemption for charter flights, offering of free nights in hotels, etc. • Establishing deposit insurance fund (to boost confidence in banking sector) • Parliament approved legislation on integrated supervision of non-bank financial sector (i.e., capital market, insurance, mortgage finance, financial leasing, and factoring) in January 2009 • 2nd phase of the Financial Sector Reform Program, with expected joint ABD-World Bank financing, discussed between the Prime Minister, the Minister of Investment, and the Governor of the Central Bank in January 2009. Program at strengthening role of the financial sector by expanding the volume of bank lending, and enhancing SME's access to credit. • Egyptian Central Bank cut its benchmark interest rate for the first time since April 2006. The overnight deposit rate was lowered by 100 basis points to 10.5 percent, while the lending rate was cut by the same amount to 12.5 percent.
Kenya	• The Central Bank reduced the threshold for investments in Treasury Bills in the primary market from the current Kshs 1 million to Kshs 0.1 million from January 2009 to induce small investors. • The Kenyan government issued infrastructure bond that amounted to 18.5 billion shilling (USD 232.6 million) with 12-year maturity in February 2009.
Mauritius	• Government announced in January 2009 a stimulus package to bolster economic growth,

	increase jobs and boost purchasing power as a response to the global financial crisis. The package will provide Mauritian Rupees 10.4 billion, equivalent to about 3 percent of GDP.
Morocco	• In a bid to stimulate trade, the Moroccan government has taken a series of measures to re-energize the markets: • Allowing companies to buy back their own shares without a minimum set price in the event that their share prices drop below a certain level. • The possibility for insurance companies to hold up to 60 percent of their listed shares to cover their liabilities, as opposed to the previous ceiling 50 percent.
Nigeria	• The 2.8 trillion naira (22.6 billion dollar) 2009 budget submitted to the National Assembly is noticeably heavy on recurrent expenditure and light on capital spending and investment. The government is now mulling to use its USD 52 billion foreign exchange reserves to shore up the economy through a stimulus package. • Launch of a Presidential Steering Committee on the Global Economic Crisis in January 2009. The Committee is responsible for developing a framework to respond to the global crisis. • Government announced plan to suspend the 5 percent excise duty on some goods manufactured such as juices, instant noodles and nonalcoholic drinks, aiming to support its stressed industry and avert job losses. • Government decided to inject N70 billion into the textile industry through guarantees in February 2009. • Nigerian government imposed foreign exchange controls to stem off the slide in the Naira. These measures include: • All foreign exchange purchases from the central bank window are only to be used for customers, and not on the interbank foreign exchange market. • The net open foreign exchange position of banks reduced to 1 percent of shareholders' funds, down from 20 percent in mid-December 2008.
South-Africa	The recent Presidential State of the Nation address (6th February, 2009) has taken note of the impact of the ongoing financial crisis to the economy. The government has flagged measures underway to avert the crisis that include: • Increased funding for public investment projects with allocation of R 690 billion (about USD 80 billion) over the next three years; • Intensification of public sector employment programs; • Adoption of industrial financing and incentive instruments to assist firms in distress, and lastly; • Sustained and expansion of government social expenditure. • Financing of these measures includes support from development finance institutions as well as partnership with the private sector • Proposed tax adjustments to personal income tax providing middle and lower income earners with R13.6 billion in tax relief. • The South African Reserve Bank cut the repurchase rate, its benchmark interest rate, by 100 basis points to 10.5 percent, the biggest reduction in more than five years.
Sudan	• The Regional Government of Southern Sudan has ordered a 10 percent salary cut for all senior government officials and a clampdown on the payment of hotel costs for officials who do not have their own housing.
Tunisia	• A Commission to ensure crisis surveillance has been established • 2009 budget includes a significant increase in public investments along with measures to increase external competitiveness and employment and strengthen social protection • Central Bank relaxing monetary policy stance, with Dinar money market rate falling from about 5.2 percent in December to 4.65 percent in January 2009 • Central Bank reduced its key interest rate by 75 basis points, from 5.25 percent to 4.50 percent in February 2009.
Uganda	• Government has assisted the troubled Uganda Transport Operators and Drivers Association (Utoda) by writing off nearly half of the accumulated Shs1.7 billion debt that it owes Kampala City Council (KCC).

Source: Committee of African Finance Ministers and Central Bank Governors (2009)

Following the example of developed and emerging economies, some African governments have implemented fiscal stimulus plans. This includes increases in public investment expenditures as well as tax reductions. However, in some countries, the severity of the crisis has forced the governments to retrench and undertake a contractionary fiscal policy. For example, in Mauritius, the Government announced in January 2009 a stimulus package to boost domestic demand and increase job creation. This package is worth 10.4 billion of Mauritian Rupees (USD 0.3 billion), or approximately 3 percent of Mauritius GDP.

Similarly, the Liberian Government undertook a comprehensive revision of its Revenue Code, proposing a 10 percent reduction in corporate and income tax rates in a bid to stimulate private sector activity. In addition, the Government is planning to cut regional trade tariffs by one quarter of a percentage point with a view of fostering trade within ECOWAS. The South African government has proposed an adjustments to personal income tax that should provide middle and lower income earners with R13.6 billion (USD 1.35 billion) in tax relief. Also, in Senegal the government lowered budgetary expenditure by 4 percent of GDP and priority expenditure by 0.6 percent of the GDP. Similar actions were taken in Cape Verde, Sudan and Uganda. In Tunisia, the 2009 budget includes a significant increase in public investments in line with its plan to increase external competitiveness and employment and strengthen social protection. Similarly, in South Africa, the government increased funding for public investment projects with allocation of R 690 billion (about USD 80 billion) over the next three years (CAFM&CBGs, 2009).

Certain targeted assistance has also been made to some strategic sectors. Many countries have implemented targeted sectoral assistance plans to support sectors that are considered as key growth drivers. These measures are intended to reduce job destruction and the loss of sector specific capital and know-how. In Nigeria, the Government injected N70 billion into the severely weakened textile industry. The Rwandan Government announced plans to reduce the quantity of its tea sold through auctioning at Mombasa and improve direct sales to reach a target of USD 54 million tea sales in 2009. In Uganda, the Government provided assistance to the transportation sector by writing off public loans to companies.

In the areas of banking regulation and capital account controls, prudential capital controls in most African banking systems have helped to minimize contagion effects on African banks. These controls also reduced capital outflows during the crisis. In addition, some governments have introduced deposit insurance schemes. In Tanzania, profit repatriation has been regulated to minimize contagion, as bank subsidiaries cannot automatically transfer funds to compensate for losses in parent banks. The Egyptian government has established a deposit insurance fund to boost public confidence in banking sector. In response to the large depreciation of their national currencies, governments have undertaken a variety of measures to defend their currency or to boost competitive. Some have attempted to defend a managed exchange rate. In some countries with fixed exchange rate regimes, governments have devaluated their currencies to boost competitiveness. Also, the Nigerian Central Bank had aggressively intervened in the foreign exchange markets to stem the slide of the Naira. However, defending the Naira has proven unsustainable in the context of declining export revenues. Other central banks have also attempted to defend the national currency but have run out of reserves.

On monetary policy, several countries have eased their monetary policy by cutting interest rates to stimulate consumption and encourage borrowing. Examples include Botswana where the Central Bank has cut its bank rate by 50 basis points to 15 percent in December 2008. Similarly the Egyptian Central Bank has cut its benchmark interest rate for the first time since April 2006. The Namibia's Central Bank and the South African Reserve Bank also reduced their repurchase rate to stimulate

borrowing and boost private investment and consumption. Furthermore in the area of bond financing of public expenditure, some countries have financed counter-cycle expenditures via the emission of treasury bills and bonds. In Cape Verde, the Central Bank introduced Treasury bills to encourage private saving to remain in the national financial system. The Kenyan government issued an infrastructure bond that amounted to 18.5 billion shilling (USD 232.6 million) with 12-year maturity in February 2009. The bond was oversubscribed, a testimony to the existence of a substantial untapped domestic saving capacity. Nevertheless, government stimulus programs, albeit vital, have largely focused on short-term fixes, in an environment in which the quality of spending is as important as the quantity. Asia's business model has atrophied, and it is unclear what will replace it.

4.2 Export-Led Growth: Why is Africa an Innocent Victim?

Although the immediate effects of the crisis seem to have been mitigated, African economies are faced with severe threats of growth deceleration, which would undermine the progress in reducing poverty. Substantial negative effects have been already observed in terms of losses on stock markets, currency depreciation, and worsening of macroeconomic balances (current account deficits, budget deficits). The crisis is hitting the very same sectors that have been driving growth over the past years, namely natural resources and services. Growth prospects are therefore, much less optimistic than before the crisis. The very fact that Africa's recovery from a crisis it did not cause seems conditional on the recovery of those that caused it means that the current growth strategy is neither optimal nor appropriate. This is obviously a manifestation that export-led growth strategy has failed African countries. Is it because of the nature of commodities export? Is it because of over reliance on exports markets that can fail disastrously? Is it because of a global trading system that is inherently hostile to the continent? Is it because of Africa's understanding of growth as defined by neo-liberal economic thinking? One thing that is certain is that Africa has become a laboratory for experimenting with different development strategies of some development thinkers that hardly understand Africa. Even while prices of primary commodities are falling, there is no evidence that demand will pick up. Market failure now seems to be more costly for Africa than government failure. Only the heavens know what next will be prescribed for Africa. It has become clear that insofar export is important in generating external financing, it is not the most stable and sustainable source of development financing. Africa should start looking for its more sustainable drivers of growth elsewhere.

Over-reliance on primary exports has a source of development financing has therefore posed a potential drag on future growth. Thus, this focus on exporting and trade liberalization has harmed developing countries in several ways. First, it has tilted the focus away from development rooted in domestic market growth. Second, it has placed developing countries in race-to-the-bottom competition with each other. Third, it has placed workers in developing countries in conflict with workers in industrialized countries. And fourth, it has harmed the global economy by creating an environment of excess capacity and deflation. Exporting will remain essential for development to enable countries to pay for imports of capital goods and other needed resources. However, the challenge is to avoid exports becoming such a dominant focus of policy that it distorts and retards development. The growth was also built on weak social and political foundations, from underinvestment in public education, health care, and social services to poor governance and a weak rule of law. These concerns were ignored by the business and political elites who benefited

the most from rapid economic growth, and the masses generally did not quibble so long as their incomes increased year after year (Palley, 2002).
Consequently, it can be argued that the Washington consensus of the Bretton Woods institutions, with its emphasis on export-led growth, had failed. It is definitely time for a new development policy agenda in Africa that focused on domestic demand-led growth. In place of export-led growth, with its shallow and exploitative characteristics, African countries must look to growth based on domestic market development. Exports will remain essential as developing countries will still need to export to earn the funds needed to pay back loans incurred to finance growth. Moreover, almost all countries lack large enough domestic markets to sustain self-sufficiency. But that said, the global trading system must be made the servant of domestic development, and domestic development must not be foregone for the sake of international competitive advantage.

The key to unlocking domestic development is solving the problems of income distribution and imbalance of political power. Deep domestic development requires growing wages and an improved distribution of income. Together, these provide the foundation of a virtuous circle of growth in which rising wages encourage market development, and market development promotes rising wages. There is now growing recognition that development depends on good governance. Labor standards (prohibitions on discrimination, forced labor, exploitative child labor, and the rights of freedom of association and collective bargaining) and democracy are both key to this new model. Depressed wage growth is one reason why household income as a proportion of GDP has actually declined across Asia in recent years. Likewise, the high saving rates in the continent is due in part to income insecurity. Most job arrangements in Africa are informal.

First generation reform was predicated on a hydraulic model of economics which had the international monetary finance (IMF) asserting that all that was needed for growth and development was for countries to get their exchange rates, interest rates, and budget deficits right. Presently, it has been argued that institutions are essential for development. Transparency, accountability, and good governance help prevent mis-allocation of resources and guard against kleptocratic government. Domestic demand-led growth also requires that countries get the macroeconomic environment right. This is where design of the international financial architecture and provision of adequate development financing becomes critical.

Under current arrangements developing countries are subject to damaging "stop-go" cycles of boom and bust. This pattern results in huge risk premia that are required to compensate investors for the danger of "sudden-stops," and these huge risk premia then become self-fulfilling by making an eventual sudden stop almost inevitable. In this fashion, market forces have locked developing countries into a permanent high cost of capital trap. Further compounding the damage, capital markets also require that governments pursue policies of fiscal austerity or face punishment of even higher interest rates (Palley, 2002).

In addition to a domestic demand-led growth model, there may also be a need for African policy makers as suggested by AfDB (2009) to:

- Strengthening the *financial regulatory framework* at the national and regional level: The reform of the regulatory frameworks should especially focus on issues of *financial supervision, risk management, and systematic disclosure* of information by financial

institutions. The key is to ensure *transparency and comprehensiveness* in the regulation of financial institutions and transactions. While preserving the special role of banks, regulators need to ensure that adequate regulation and supervision is established for banks as well as non-banks, on-balance sheet as well as *off-balance sheet financial operations*. Regulation also needs to establish mechanisms for *mitigating procyclicality* of bank lending.

- Supporting domestic growth drivers: Economic policy at the macroeconomic and sectoral level needs to target support for *domestic growth drivers* depending on each country's circumstances. Thus it is encouraging that some African countries have already undertaken initiatives – such as cuts in tourism levy on hotel (Egypt) to support sectors that have been exposed to the crisis. Similar measures should be investigated for the mining sector and other export oriented activities.
- Increasing investment in infrastructure: It is critically important that African countries keep an adequate level of infrastructure investment to support private sector activity in general and enhance *competitiveness* and *diversification* in particular. Hence, financing for infrastructure must be considered as a priority by governments, donors and other financiers, including the MDBs.
- Preparedness and targeted responses by MDGs: MDBs will play a critical role in assisting African countries to devise strategies for preventing and mitigating the impact of financial crises. In particular, it is important to evaluate the *resource requirements* for assisting countries affected by the crisis, including *recapitalization of banks* and provision of targeted finance such as *trade financing.*
- Ensuring adequate flows of development aid: Despite the economic downturn in developed and emerging countries, it is important that donors honor their aid commitments. Any reduction in aid will amplify the negative impact of the crisis, which in turn will delay global economic recovery by depressing demand.

5. Summary and Conclusion

Africa's development strategies since independence has focused on import substitution strategy and structural adjustment programme (SAP) with disappointing outcomes. However, since the late 1990s, growth has resumed due mainly to favourable primary commodity prices fueled by high demand by emerging economies like China and India. However, the recent economic slowdown has shown how export-led growth can make countries highly vulnerable and lead to major negative (external) shocks. Since the economic slowdown, all growth indicators are pointing to the fact that growth expectations may not be met. Although, African countries are not responsible for the crisis, yet they are bearing a disproportionate percentage of the crisis. The impact of the crisis has led to falling international demand for primary commodities making their prices to collapse. Government revenue is negatively affected, while current account and fiscal positions has also become negative. Support for agriculture (and other social services) has decline, further reducing agricultural productivity (and thus export), which further aggravate the crisis. This has turned into a cycle of economic decline.

The export-led model countries adopted has ironically left them more dependent than ever on the whims of the developed countries now, that growth is shriveling. While the economic slowdown cannot be said to be entirely responsible for this precarious situation, it has compounded problems that already existed due to weak economic, social and political foundations on which

the model was built. This deterioration in economic performance has opened the export-led growth model to challenge, just as it had earlier challenged the import-substitution model. The Washington consensus, with its emphasis on export-led growth, has failed. It is time now for a rethink on the new development policy agenda that focuses on domestic demand-led growth. Achieving such an outcome will require a new constellation of policies. Domestic demand-led growth rests on four pillars: improved income distribution, good governance, financial stability and an adequate fairly priced supply of development finance.

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