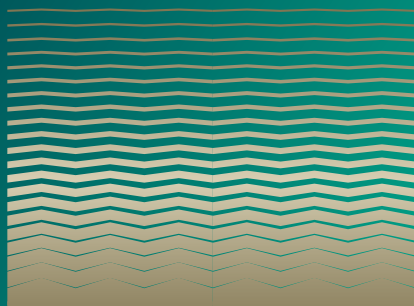




# Africa's 2023 Growth Prospects: Securing growth resilience in a 'polycrisis' world

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# Table of contents

<b>1 Policy normalisation and global volatility</b>	<b>03</b>
<b>2 Recent developments and global economic outlook</b>	<b>07</b>
<b>3 Africa's growth resilience amid risk of stagflationary debt crisis</b>	<b>13</b>
<b>4 Regional distribution of growth</b>	<b>18</b>
<b>5 Internal drivers of growth resilience</b>	<b>26</b>
<b>6 External drivers of growth resilience</b>	<b>34</b>
<b>7 Risk to the outlook</b>	<b>42</b>
<b>8 References</b>	<b>46</b>

# I.

## Policy normalisation and global volatility

**Following the lifting of Covid-19 containment measures that had precipitated sharp global demand and supply shocks, the world closed 2021 on an extraordinarily strong economic note.**

Global output rebounded strongly, expanding by 6.2% on the back of highly effective counter-cyclical monetary and fiscal stimulus measures (IMF, 2023a). 2022, however, struck a discordant tone, as rising geopolitical tensions and macroeconomic policy malpractice exacerbated the consequences of the pandemic downturn (El-Erian, 2022; Fofack, 2022a). Supply-chain disruption intensified, setting the stage for globally-synchronised growth deceleration and torrid price rises that overshot thresholds in almost all inflation-targeting economies (World Bank, 2023).<sup>1</sup>

The world economy expanded by 3.4% in 2022 (IMF, 2023a). Even accounting for the base effect, this represented a drop of 1.5 percentage points from earlier forecasts of 4.9% released before Russia's invasion of Ukraine (IMF, 2021) and the subsequent imposition of sanctions by the West.<sup>2</sup> These created more uncertainty and aggravated supply-chain bottlenecks, compounding

inflationary pressures. Across Africa, aggregate output decelerated, with the region's combined gross domestic product (GDP) expanding by just 3.9% in 2022, above the world average but down significantly from earlier forecasts. For Africa, where the post-pandemic rebound was not exceptionally strong, this deceleration will make it even more difficult in the near term for per capita incomes to converge with pre-crisis trend growth (World Bank, 2023).<sup>3</sup>

The globalisation of the Ukraine crisis following the implementation of sanctions against Russia inflamed volatility and macroeconomic risks, derailing the nascent post-pandemic recovery (Fofack, 2022b). Systemically important central banks initiated their 'big pivot', transitioning from accommodative monetary policy to one of the most aggressive tightening cycles on record in a bid to bring inflation back to target and prevent it from becoming entrenched (Exhibit 1). Inflation, which hit multi-decade highs and is raising the spectre of stagflation, is likely to emerge as the dominant macroeconomic story, eclipsing the short-lived globalisation of growth resilience post-pandemic (Exhibit 2).

<sup>1</sup> For too long the European Central Bank and the US Federal Reserve, the two most important systemically important central banks, erroneously assumed inflation was transitory. For more details, see <https://www.forbes.com/advisor/investing/transitory-inflation/#:~:text=The%20Fed%20Promised%20Inflation%20Would%20be%20Transitory&text=Fed%20Chair%20Jerome%20Powell%20and,when%20economies%20were%20shut%20down>

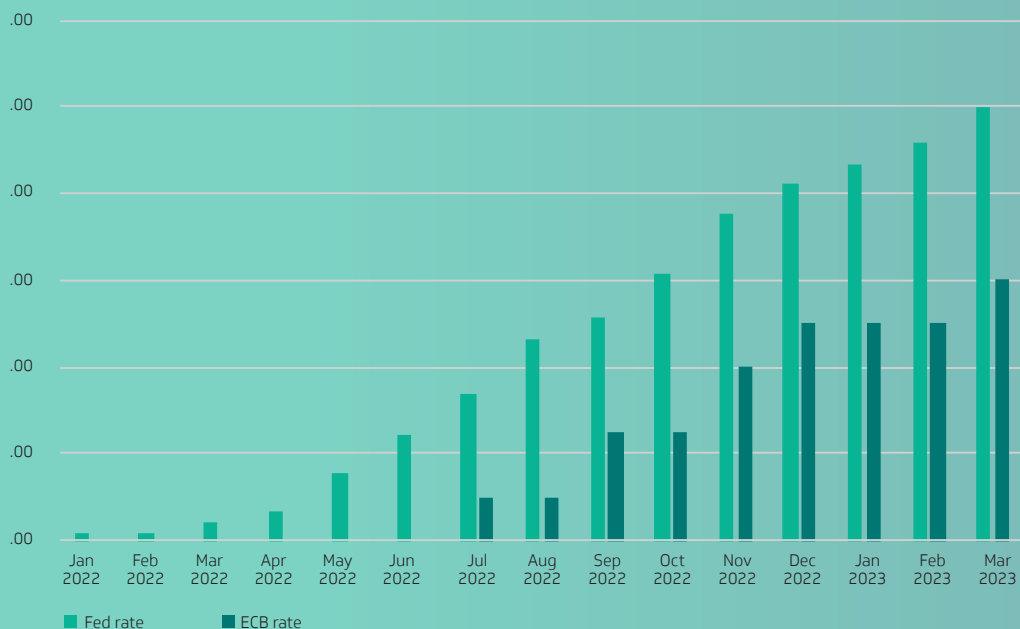
<sup>2</sup> For more details, see <https://www.imf.org/en/Publications/WEO/Issues/2021/10/12/world-economic-outlook-october-2021>

<sup>3</sup> Unlike other regions where per capita income is expected to return pre-pandemic trend growth this year, most countries across Africa are set to suffer a huge income gap. For more details, see <https://openknowledge.worldbank.org/server/api/core/bitstreams/254aba87-dfeb-5b5c-b00a-727d04ade275/content>

Although the economic consequences of heightening geopolitical tensions were felt globally—albeit to varying degrees, with Europe, which depends heavily on Russia energy, suffering most in the first half of the year—tighter global financial conditions disproportionately affected emerging markets and developing economies. These countries are highly vulnerable to capital flow volatility and sudden stops, with Egypt offering one case in point. Global investors pulled out around US\$20bn from local debt in Q1 2022 (FT, 2023a), putting more pressure on the country's exchange rate, which depreciated by more than 55% over the course of the year. Most developing countries' currencies depreciated against the US dollar in 2022, which only served to throw more fuel on the inflationary flames.

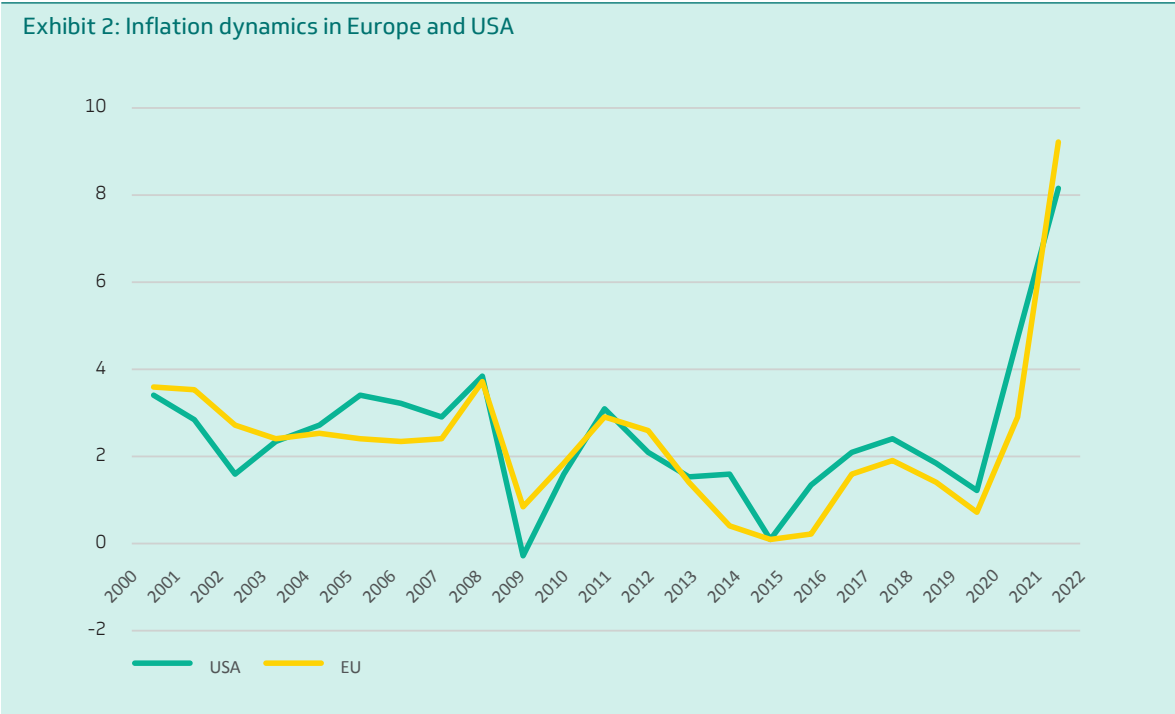
According to the Institute of International Finance, emerging market net issuance of hard currency debt was negative in 2022 (Exhibit 3). After navigating the high levels of risk aversion engendered by the pandemic, bond issuances by African sovereigns collapsed in 2022, falling to US\$6bn from around US\$20bn in 2021 (Fofack, 2022b). Even though spreads—which skyrocketed at the height of the geopolitical crisis in 2022, shutting most African countries out of international capital markets—narrowed later in the year, they remain elevated. In fact, they received another boost recently in light of the US banking crisis, which again raised global volatility, increasing the fiscal incidence of sovereign debt and external debt servicing costs.

Exhibit 1: Dynamics of interest rates in US and Europe



Sources: IMF and Afreximbank Research

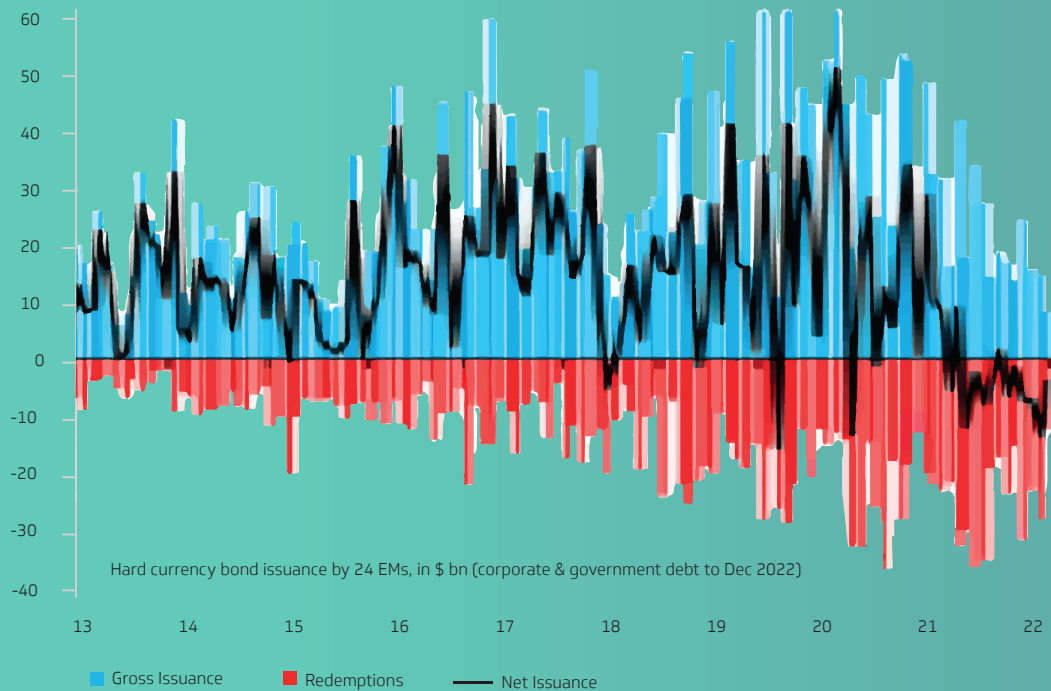

 Inflation, which hit multi-decade highs and is raising the spectre of stagflation, is likely to emerge as the dominant macroeconomic story, eclipsing the short-lived globalisation of growth resilience post-pandemic.



Sources: IMF and Afreximbank Research

In the age of geopolitical rivalries, the combination of heightening geopolitical tensions and policy malpractice post-pandemic have created a perfect storm of overlapping crises, opening the door to a 'polycrisis' world.

Exhibit 3: Hard currency bond issuance by 24 Emerging markets to December 2022 (in \$bn)



Source: IIF (Institute of International Finance)

# II.

## Recent developments and globaleconomic outlook

In 2016 Mark Carney, while Governor of the Bank of England, included geopolitical risk—alongside economic and policy uncertainty—among an ‘uncertainty trinity’ that posed potentially significant adverse economic effects (Caldara and Iacoviello, 2018; Astvansh et al., 2022).<sup>4</sup>

The following year the International Monetary Fund (IMF), in the October 2017 edition of its World Economic Outlook, highlighted geopolitical uncertainties as a salient risk to macroeconomic prospects. Since then, geopolitical risks have climbed to stratospheric levels—the US Federal Reserve’s monthly index of geopolitical risk reached an all-time high in 2022—undermining economic growth and investor confidence.<sup>5</sup> Empirical analysis shows that high geopolitical risk leads to a decline in real economic activity, lower stock returns and movements in capital flows away from emerging markets and towards advanced economies. In the age of geopolitical rivalries, the combination of heightening geopolitical tensions and policy malpractice post-pandemic have created a perfect storm of overlapping crises, opening the door to a ‘polycrisis’ world. In addition to climate change and trade wars, which have become persistent risks to long-run growth, geopolitical strains exacerbated by the Ukraine crisis shifted global concerns away from pandemic-related health issues towards political, security, macroeconomic and financial risks.

Looking back at 2022, geopolitical tensions either amplified these risks—trade restrictions increased dramatically over the past year, unlike in the era of the 2008 financial crisis, when there was a strong commitment to international co-operation and a concerted effort to boost cross-border trade and drive output expansion—or raised others (Georgieva, 2023).<sup>6</sup>

In addition to the lingering effects of the pandemic downturn, the world is now contending with across-the-board inflation and a higher cost of living, as well as tighter financing conditions that have increased the risk of sovereign debt and financial crises (Roubini, 2023).

These crises are all related, and the outcome of their interaction may ultimately be even greater than the sum of their parts. Inflation, which was exacerbated by global supply-chain disruption, is eroding households’ purchasing power, causing domestic and global demand to contract and slowing aggregate output expansion. The tariff hikes that are sustaining the Sino-US trade war are affecting not only prices of imported goods, but also of parts and components bought from China, further driving up the cost of downstream products under the rather sticky just-in-time global supply chain model. Cross-border trade has lost momentum, leading the World Trade Organisation (WTO) to revise its 2023 forecast downward.

<sup>4</sup> For more details, see <https://www.federalreserve.gov/econres/ifdp/files/ifdp1222r1.pdf>

<sup>5</sup> In addition to their adverse short-term implications for economic growth, geopolitical risks also stifle innovation and may have adverse implications for long-run growth. For more details, see <https://hbr.org/2022/03/research-when-geopolitical-risk-rises-innovation-stalls>

According to its latest prognosis, global merchandise trade volumes will expand by just 1%, versus previous estimates of 3.4% (WTO, 2022).<sup>7</sup>

Simultaneously, policies implemented by central banks to bring inflation back to target are undermining investment growth, weakening the correlation between investment and trade. Moreover, by dramatically raising the fiscal incidence of sovereign debt, the aggressive normalisation of monetary policy has increased the risk of sovereign debt crisis, especially among developing economies with limited fiscal space or access to refinancing.

Another major consequence of the Covid-19 pandemic that is weighing heavily on developing and advanced economies alike is the overleveraging of sovereign and corporate entities. Even before the collapse of Silicon Valley Bank (SVB)—the second-largest bank failure in US history, following a run that saw around US\$42bn withdrawn by account holders in one

day—signs of increasing stress in the financial industry were intensifying, with the risks associated with maturity mismatch and the repricing of assets magnified by the aggressive pace and quantum of interest rate rises (Bella, 2023; Roubini, 2023).<sup>8</sup> SVB had invested heavily in long-dated securities (treasury bonds and mortgage-backed securities), the market for which fell as interest rates rose.

In addition to massive losses suffered by major US financial institutions late last year, a review of banks' balance sheets pointed to major problems in the industry. The concealed dollar debt uncovered on the balance sheets on non-US banks and shadow banks as of June 2022 was US\$65tn, significantly larger than what was observed in the lead-up to the 2008 financial crisis (Mun, 2023).<sup>9</sup>

The largest failure of a US bank since the height of that crisis has raised the probability of a financial crisis, coupled with the already-high risks of a stagflationary debt crisis emerging (Roubini, 2023).





## Similarly troubling has been the sharp increase in banks' exposure to domestic sovereign debt, the so-called sovereign-bank nexus.

Similarly troubling has been the sharp increase in banks' exposure to domestic sovereign debt, the so-called sovereign-bank nexus (IMF, 2022a). The increase in public debt in the wake of the pandemic reinforced the relationship between sovereigns and banks, with the latter's holdings of domestic sovereign debt surging to new records. This raised a fresh set of challenges for the financial system and global economy more broadly, most notably in respect of investment growth and macro-financial stability. In countries where banks are not well capitalised, an increase in sovereign risk can adversely affect balance sheets and lending appetite, stymieing private investment and growth.

In a world in which the biased distribution of liquidity has skewed the global distribution of refinancing risks, the hazards associated with the sovereign-bank nexus are most keenly felt in emerging markets and developing economies, where central banks lack the financial wherewithal to act as both lender of last resort and market maker of last resort.

The most recent available estimates show that bank holdings of domestic sovereign assets have increased sharply in these countries, reaching 17% of total banking sector assets in 2021 (IMF, 2022a).<sup>10</sup> This partly reflects the fact that additional financing requirements in these countries were met mostly by domestic banks amid a generally limited domestic investor base,

massive capital outflows and declining foreign participation in local currency bond markets.

And inflation, which was initially believed to be transitory, has turned out to be persistent. The latest readings show that downward pressure on inflation weakened considerably in February. For instance, the US all-items consumer price index rose by 6% year-on-year in February (BLS, 2023), and so-called core inflation (which excludes volatile food and energy prices) rose 0.5%, slightly above January's 0.4%.<sup>11</sup> On the other side of the Atlantic, the UK's inflation rate edged higher to 10.4% in February 2023 from 10.1% in January; pundits had predicted a decline (Milliken and Schomberg, 2023).<sup>12</sup> Given that bank collapses have already raised concerns about financial stability, these enduring inflationary conditions can only muddy the path forward for monetary policymakers.

In addition to the trade-offs between fighting price increases and encouraging growth—history shows that aggressive monetary tightening has been associated with economic downturns<sup>13</sup>—monetary authorities must now balance financial stability and price stability at a time when stubbornly high inflation is constraining their ability to respond (Fofack, 2022a; Stiglitz, 2023). And in Asia, China's economic reopening could spur another reflationary impulse. The release of pent-up domestic demand and sharp growth acceleration in the world's second largest

6 Between 2020-22 the total number of trade restrictions increased from 1,700 to around 2,500. For more details, see <https://www.imf.org/en/Blogs/Articles/2023/01/16/Confronting-fragmentation-where-it-matters-most-trade-debt-and-climate-action>

7 For more details, see [https://www.wto.org/english/news\\_e/pres22\\_e/pr909\\_e.htm](https://www.wto.org/english/news_e/pres22_e/pr909_e.htm)

8 SVB, which primarily served start-ups and venture capitalists, was the country's 16th-largest bank with around US\$209bn in assets. For more details, see <https://www.washingtonpost.com/business/2023/03/11/silicon-valley-bank-washington-mutual-failure/>

9 For more details, see <https://www.flymalaysia.org/watch-out-for-derivative-bombs-in-2023/>



Unquestionably, emerging markets and developing economies, which will account for the lion's share of projected output expansion, continue to be the engine of global growth.

economy may fuel global inflationary pressures, potentially driving up commodity prices and offsetting the deflationary effects of prospective supply-chain normalisation.

While some of the headwinds that buffeted economic output last year are cyclical, it is increasingly evident that most are structural and will shape growth prospects in the short and medium term. Heightened geopolitical tensions, besides preventing opportunities for international co-operation on global issues, have raised the risk of fragmentation. This could undermine macroeconomic stability and growth, given how globalisation has exerted downward pressure on prices (IMF, 2023). According to IMF research, the longer-term cost of trade fragmentation alone could range from 0.2% of the global output in a limited fragmentation scenario to almost 7% in a severe scenario (Georgieva, 2023).<sup>14</sup>

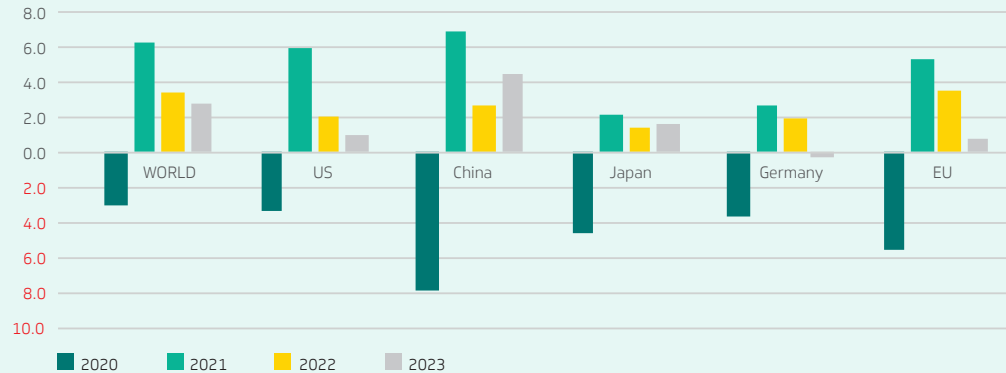
Hence, the global economic environment suggests continued slowing momentum, with the average world GDP growth expected to decelerate to 2.7% in 2023 (IMF, 2023b), significantly down from 3.4% last year (Exhibit 4). The projected output expansion is consistent with consensus forecasts<sup>15</sup>, which point to the global economy growing this year

despite fears of recession in parts of the world, especially in major economies within the European Union (EU) but also in the US, where the credit crunch caused by banking stress has raised the risk of hard landing (Powell, 2023). In effect, global output expansion is expected to be driven mostly by Asian economies as they benefit from ongoing reopening dynamics and less intense inflation (CB, 2023).

Asia will account for 46% of total global GDP growth in 2023, with China contributing more than 19%, propelled largely by the country's economic reopening boost following the termination of its stringent zero-Covid policy late last year, as well as monetary and fiscal stimulus as the country continues to ride the wave of low inflation.

This points to continued growth acceleration that will dwarf the performance achieved in other regions, including Europe and the US (Exhibit 5). Unquestionably, emerging markets and developing economies, which will account for the lion's share of projected output expansion, continue to be the engine of global growth.

**Exhibit 4: Trend of real GDP growth (annual percentage change)**



Sources: IMF and Afrexibank Research

**Exhibit 5: Contribution to global growth by leading economies**

	2020	2021	2022	2023*
China	18%	18.5%	19%	19%
USA	16%	15.5%	15%	15%
India	7%	7%	7%	7%
EU	15%	15%	15%	15%
<b>Others</b>	<b>44%</b>	<b>44%</b>	<b>44%</b>	<b>44%</b>
	100%	100%	100%	100%

Sources: IMF and Afrexibank Research

10 The IMF's April 2022 Financial Stability Report devoted a chapter to the sovereign-bank nexus in emerging markets. For more details, see <https://www.imf.org/en/Publications/GFSR/Issues/2022/04/19/global-financial-stability-report-april-2022>

11 For more details, see <https://www.bls.gov/news.release/cpi.nr0.htm>

12 For more details, see <https://www.reuters.com/world/uk/uk-inflation-rate-rises-104-february-ons-2023-03-22/>

13 Reflecting on the risk of a possible policy-induced recession, Fed Chairman Jay Powell recently recognised that "while higher interest rates, slower growth, and softer labour market conditions will bring down inflation, they will also bring some pain to households and businesses." For more details, see <https://www.federalreserve.gov/newsevents/speech/powell20220826a.htm>

14 For more details, see <https://www.imf.org/en/Blogs/Articles/2023/01/16/Confronting-fragmentation-where-it-matters-most-trade-debt-and-climate-action>

15 However, these estimates of global GDP growth are slightly higher than those released earlier by both Goldman Sachs (1.8%) or the Conference Board (2.3%). For more details, see <https://www.goldmansachs.com/insights/pages/gs-research/macro-outlook-2023-this-cycle-is-different/report.pdf> and <https://www.conference-board.org/topics/global-economic-outlook>

Africa's 2023 Growth Prospects:  
Securing growth resilience in a 'polycrisis' world



# III.

## Africa's growth resilience amid risk of stagflationary debt crisis

**In a sign of increasing growth resilience against a backdrop of synchronised global growth deceleration, our forecasts point to robust economic growth across Africa, with aggregate output projected to expand by around 4.1% this year, up slightly from the 3.9% recorded in 2022.**

These projections are consistent with growth estimates put forward by other institutions.<sup>16</sup> IMF estimates, which project growth acceleration in more than 60% of African countries, show aggregate GDP growth averaging 3.9% in 2023 (IMF, 2023a). This expansion will be broad-based, with both large and smaller economies, resource-rich and resource-poor, enjoying growth acceleration.

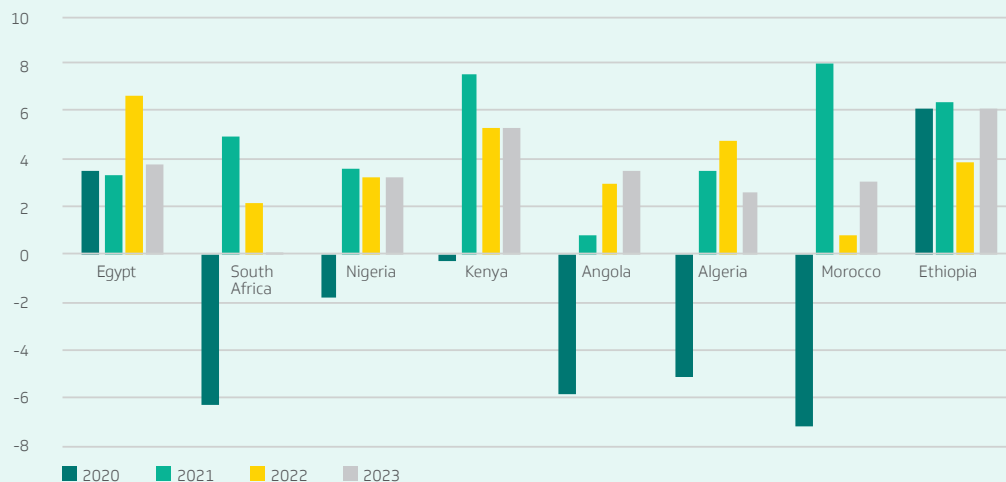
In addition to the region's trade performance—the WTO predicts that Africa's imports will remain strong<sup>17</sup>—such resilience signifies the influence of several factors. Chief among them is the performance of a few large economies, where output growth is forecast to accelerate even as the global economy remains on a decelerating path. This is especially the case among net-energy-exporting countries, which will benefit from commodity price tailwinds.

Oil prices are expected to remain buoyant, taking into consideration a strong rebound in China and pending the realignment of energy-sector supply chains triggered by the Ukraine crisis (IEA, 2023; Hatzius et al., 2022; FT, 2023b).<sup>18</sup> Angola offers a helpful example. After four consecutive years of recession, GDP growth in the country is forecast to accelerate from 2.9% in 2022 to 3.5% in 2023.

Among the net-oil-importing nations, Morocco is expected to enjoy one of the strongest rates of growth acceleration following a sharp slowdown caused by drought, rising energy prices and growth deceleration in the EU, its main trading partner. The EU was the destination of almost half of Morocco's goods exports in 2022, accounting for around 7.8% of its GDP. The country's GDP is forecast to expand by more than 3.1% this year, up significantly from the 0.8% recorded in 2022 (Exhibit 6).

<sup>16</sup> For instance, while the World Bank's forecasts point to the region's aggregate output expanding by 3.6%, the estimates of the IMF and African Development Bank are more upbeat, pointing to expansion of 3.9% and 4%, respectively (World Bank, 2023).

Exhibit 6: Growth dynamics of leading African economies



Sources : IMF and Afrexibank Research

That uptick will be fortified by a strong recovery in the services sector, especially tourism, as well as the continued growth of fixed capital accumulation, a rebound in manufacturing output and the implementation of structural reforms to unlock potential in the private sector (World Bank, 2022a).<sup>19</sup>

The recovery of the tourism industry will also provide a major boost to small island nations across the region. These countries, which have high levels of trade openness and a sizable proportion of their exports concentrated in tourism, were particularly affected by lockdowns and other Covid-19 containment measures (World Bank, 2023).<sup>20</sup>

After falling sharply to less than 5% of economic activity in 2020, average tourism-related expenditures rose to 7% of GDP in 2022 and are forecast to expand further this year boosted by reopening dynamics in China (FT, 2023b).<sup>21</sup>



After falling sharply to less than 5% of economic activity in 2020, average tourism-related expenditures rose to 7% of GDP in 2022 and are forecast to expand further this year boosted by reopening dynamics in China.

<sup>17</sup> Together, Africa and the Middle East are expected to post import growth of 5.7% in 2023, the fastest acceleration across all regions (WTO, 2022).

<sup>18</sup> According to the International Energy Agency, Brent crude oil futures have remained in a range of US\$80-US\$85 per barrel since the start of the year and some forecasters are predicting that the price of a barrel of oil will exceed US\$100 this year. For more details, see <https://www.iea.org/reports/oil-market-report-march-2023> and <https://www.ft.com/content/cb5365eb-0b52-45ac-9870-923878aeb910>

The output expansion of these countries is projected to remain strong—especially in Mauritius and Seychelles, where GDP growth is expected to exceed 5.0%—pointing to the robustness of the post-pandemic rebound and surplus of pent-up demand, even in the face of heightened geopolitical tensions and lower household purchasing power.<sup>22</sup> Africa's growth resilience is also greatly supported by the performance of two of its three largest economies, Egypt and Nigeria. Both countries are forecast to remain on a strong growth trajectory despite contending with various macroeconomic management challenges, especially sharp exchange rate depreciation and inflationary pressures.<sup>23</sup> Nigeria's GDP is forecast to expand by about 3.2% thanks to improved security and oil production, as well as a recovery in the agricultural sector after devastating floods which slashed agricultural production last year (EPRS, 2023).<sup>24</sup> In Egypt, which has consistently been one of the leading drivers of African growth, output is projected to expand by more than 3.7%.

Both countries could compensate for tepid forecasts in South Africa, where GDP expansion is set to decelerate sharply to less than 0.5% from 2.1% in 2022. The country continues to struggle with energy crises and 'load shedding'<sup>25</sup> (i.e. scheduled blackouts to control demand and prevent grid collapse) (Inglesi-Lotz, 2022; Gbadamosi, 2023). Meanwhile, record-high inflation has put the South African Reserve Bank on a path of extremely aggressive monetary tightening, which is set to further undermine growth through investment and curtail domestic demand in a country where unemployment rates have been at Great Depression levels for decades and went on to rise after the pandemic to more than 32% (SSA, 2022).<sup>26</sup>

19 Key components of the Moroccan government's ambitious structural reform agenda aim for robust, inclusive growth, including the historic move to universalise access to national health insurance and family allowance systems, the reform of large state-owned enterprises, as well as a review of the investment charter to stimulate the private sector. For more details, see <https://www.worldbank.org/en/country/morocco/overview>

20 On average, tourism expenditures pre-pandemic were equivalent to around 18% of economic activity in these countries, and substantially more in several of the 22 tourism-reliant small states (World Bank, 2023).

21 The recovery will be especially supported by ongoing developments in China where a surge in bookings on travel websites augurs well for an industry where growth has been largely driven by Chinese tourists. In 2019 they spent about US\$255 billion (FT, 2023b). For more details, see <https://www.ft.com/content/cb5365eb-0b52-45ac-9870-923878aeb910>

22 Even though Cabo Verde did not enjoy quite the same rate of growth, it is expected to remain on a strong growth trajectory, with its GDP forecast to expand by 4.8% in 2023 (IMF, 2023).

23 Both countries suffered one of the largest exchange rate depreciations in 2022, leading Nigeria's monetary authorities to resort to dollar-rationing (Onu, 2022). For more details, see <https://www.bloomberg.com/news/articles/2022-03-11/nigeria-banks-ration-dollars-as-regulator-signals-stopping-sales#xj4y7vzkg>

24 The 2022 seasonal floods, which were among the most devastating in a decade, caused more than 600 deaths and displaced 1.3m people. For more details, see [https://www.europarl.europa.eu/RegData/etudes/ATAG/2023/739363/EPRS\\_ATA\(2023\)739363\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/ATAG/2023/739363/EPRS_ATA(2023)739363_EN.pdf)

25 In February, Enoch Godongwana, South Africa's Finance Minister, attributed his country's unimpressive growth outlook to energy supply challenges. For more details, see <https://foreignpolicy.com/2023/01/25/south-africa-energy-crisis-corruption-anc/#:~:text=Rolling%20power%20cuts%20in%20South,executive%20director%20of%20ETM%20Analytics.>

26 Unemployment rates among South Africans of African descent are even higher, at around 36.8%. For more details, see <https://www.statista.com/statistics/1129481/unemployment-rate-by-population-group-in-south-africa/>



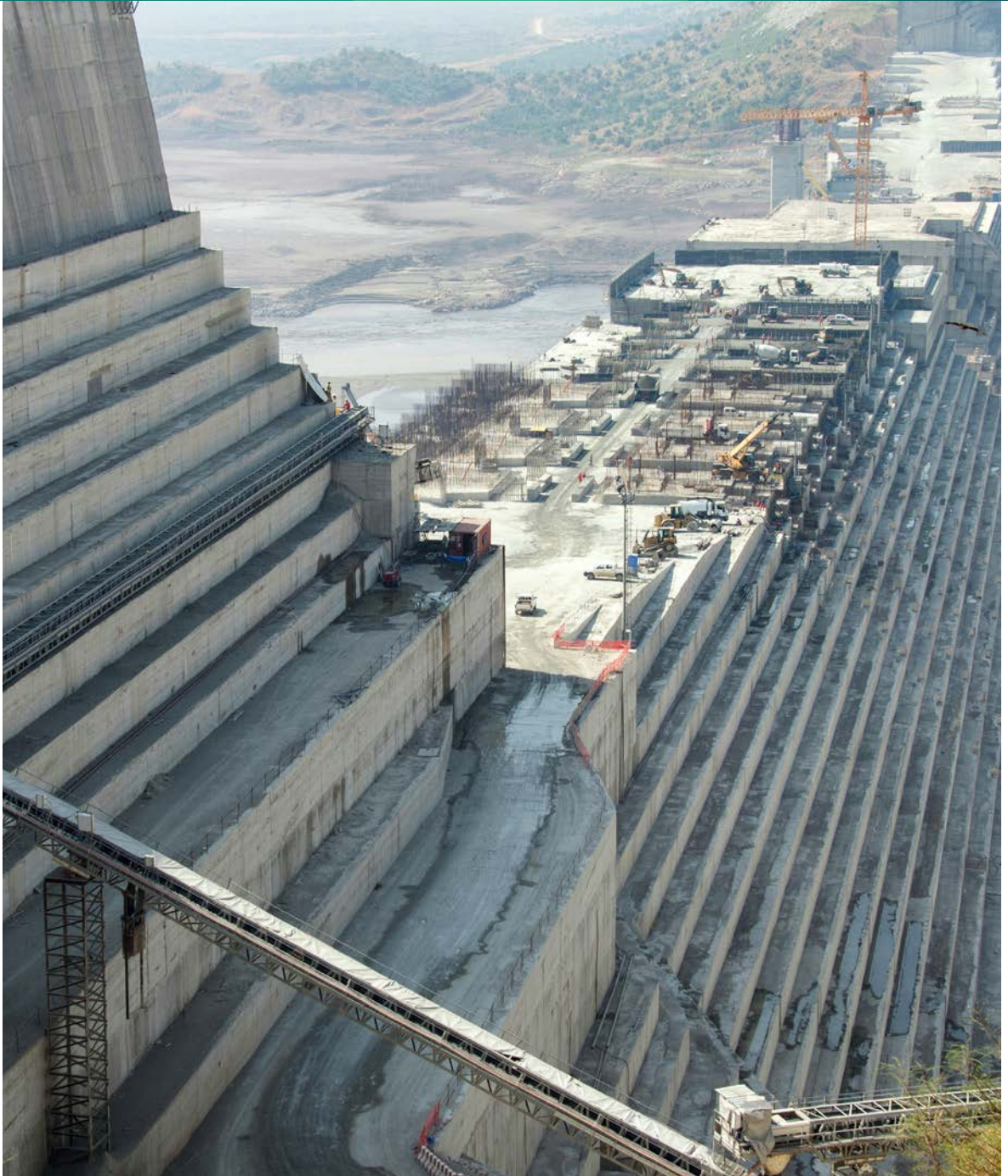


Image: Grand Ethiopian Renaissance Dam (GERD) or the Ethiopian dam

# IV.

## Regional distribution of growth

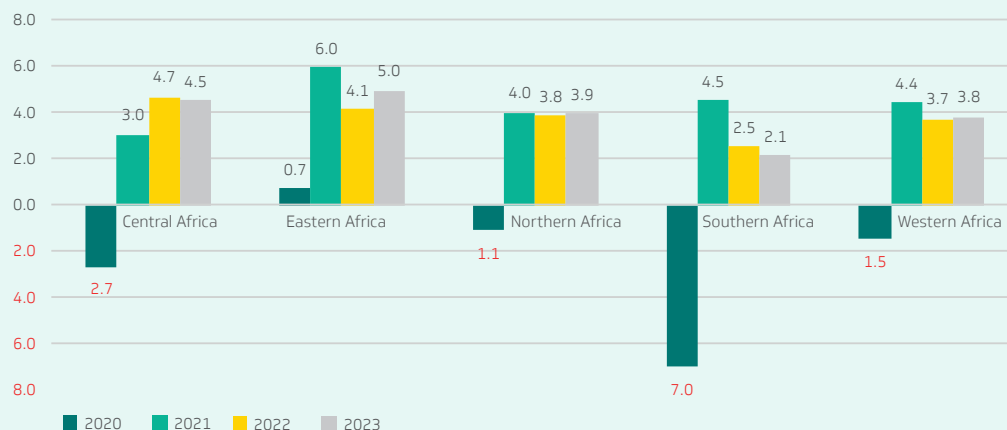
The continued expansion of Africa's headline output, however, masks important variations across subregions and individual nations. For example, GDP growth is projected to strengthen in East Africa, the fastest-growing subregion, to around 5% from 4.1% in 2022 (Exhibit 7).

The subregion is buoyed by strong growth in traditional high-performers such as Kenya (5.1%), Rwanda (6.7%), Tanzania (5.2), Uganda (5.9%), and Ethiopia (5.3%).

Almost all countries in this part of Africa are forecast to enjoy growth acceleration in 2023, the only exception being Kenya and Seychelles, though GDP growth is still expected to exceed 5% in both countries.

After deviating from trend growth last year, Ethiopia, which had been one of the subregion's fastest-growing economies over the last decade—its economy expanded by more than 6% even at the height of the pandemic downturn—is forecast to return to the crop of strong performers. Its GDP is expected to expand by 5.3% this year as security conditions improve

Exhibit 7: Dynamics of GDP growth by sub-region



Sources: IMF and Afrexibank Research

and sustained infrastructure investment accelerates the diversification of sources of growth and trade to help mitigate the country's exposure to global volatility.<sup>27</sup> East Africa as a whole is projected to account for around 15% of the continent's growth in 2023, up slightly from 14% last year.

In a major departure from historical trends, Central Africa is forecast to be the second fastest-growing subregion as oil-exporting countries, of which there are many in that part of the continent, capitalise on commodity price tailwinds and improving terms of trade in the energy sector. The subregion's aggregate GDP is forecast to expand by 4.5% this year, boosted by growth acceleration in a few countries, notably Cameroon (4.6%), Congo (4.7%) and the Democratic Republic of the Congo (6.7%), which has become one of Africa's fastest-growing economies. Still, Central Africa continues to lag behind other subregions in terms of its contribution to aggregate growth, being predicted to account for around 6% of forecast aggregate output expansion in 2023 (Exhibit 8).

North Africa is forecast to be the third fastest-growing subregion this year, with its combined GDP expected to expand by around 3.9%, shored up by still-robust growth in Egypt. As the only one of Africa's three largest economies (alongside Nigeria and South Africa) where GDP expanded strongly even at the height of the pandemic downturn, Egypt has become a beacon of growth resilience. In addition to its strong manufacturing sector, the ongoing diversification of sources of growth and trade will be further supported by a variety of forces. These include: implementation of economic reforms to boost private sector-led growth, expanded infrastructure development;

a buoyant gas extraction sector; and growing remittances, which have become a balance-of-payments stabiliser, helping to keep current account deficits under control.<sup>28</sup>

The subregion's forecast aggregate growth acceleration is also being supported by the strong performance of Morocco, where a recovery in the manufacturing sector and rebound in tourism are set to sustain the country on a healthy growth trajectory. In terms of its contribution to overall economic expansion, North Africa remains the most important driver of growth, being expected to contribute 29% of the continent's aggregate GDP in 2023. This is thanks mostly to Egypt, one of the most diversified and energy-intensive economies, which alone is projected to account for 18% of Africa's output expansion.

Despite the continued challenges posed by terrorist incursions and persistent insecurity risks—especially in the Sahel, where military expenditures have become one of the largest items in government budgets in several countries<sup>29</sup> (Fofack, 2022c)—members of the Economic Community of West African States (ECOWAS) are expected to remain on a firm growth trajectory in 2023.

The subregion's combined output is forecast to expand by 3.8% in 2023 (up marginally from 3.7% last year), lifted by strong growth acceleration in around 85% of countries.

The usual group of strong performers (Benin, Cote d'Ivoire, Senegal and Niger) will compensate for sharp growth deceleration in Ghana, which is contending with macroeconomic management challenges that have been exacerbated by the

<sup>27</sup> The successful diversification of sources of growth has emerged as a major driver of sustained output expansion in Ethiopia. In addition to positioning itself as a major logistics hub on the continent, investment in light manufacturing is boosting exports and expanding employment opportunities to drive domestic demand and growth.

<sup>28</sup> This expansion is also supported by a strong reform programme, which is set to boost competitiveness and drive private sector-led growth with the potential to significantly boost aggregate output and keep Egypt on a strong growth trajectory in the near term.

Africa's 2023 Growth Prospects:  
Securing growth resilience in a 'polycrisis' world



sharp depreciation of its currency, the cedi, and rising interest rates globally, both of which raised the fiscal incidence of sovereign debt. Before defaulting on its sovereign debt late last year, the Ghanaian government was devoting more than 50% of its revenues to servicing external debt (Inveen and Akorlie, 2022).<sup>30</sup>

Despite its relatively lower average growth rate, West Africa’s contribution to the region’s combined GDP growth remains relatively high. The subregion is projected to account for around 27% of forecast output expansion, underpinned by Nigeria’s sizable contribution, which alone will account for 18% of Africa’s aggregate output expansion in 2023 (up slightly from 17% last year).

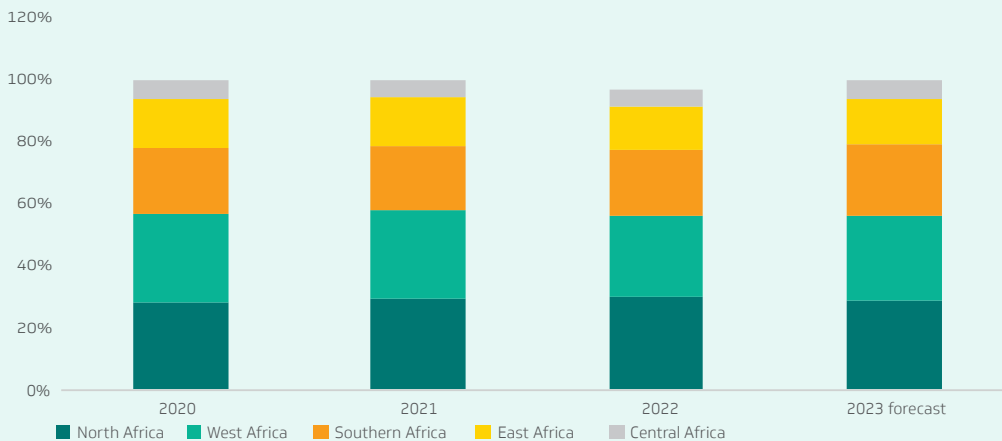
Despite the macroeconomic management challenges confronting Nigeria, including widening twin deficits and liquidity constraints which led several banks to prioritise import

obligations in the allocation of dollars, its growth prospects are supported by investment in several key sectors (Onu, 2022).<sup>31</sup> The country is emphasising development in telecommunications, financial services and e-commerce, as well as strategic industries including refineries, creative industries and logistics.<sup>32</sup>

The latter two in particular have become major growth industries for Nigeria. The value of the logistics and supply chain subsector stood at more than US\$60bn before the pandemic, and its growth potential will only increase over time, especially as the country positions itself as a hub within the African Continental Free Trade Area (AfCFTA) (Makinde, 2023).<sup>33</sup> Meanwhile creative industries have grown into the second-largest employer in Nigeria (Afreximbank 2022; Osasona, 2022).<sup>34</sup>

With their rising contribution to GDP, supporting creative businesses has become a priority for

**Exhibit 8a: Sub-regional contributions to GDP growth**



Sources : IMF and Afreximbank Research

29 For instance, over the last decade military expenditures have increased at the alarming rates of 339% in Mali, 288% in Niger and 238% in Burkina Faso. For more details, see <https://www.brookings.edu/wp-content/uploads/2022/05/Dawn-of-a-Second-Cold-War.pdf>



North Africa remains the most important driver of growth, being expected to contribute 29% of the continent's aggregate GDP in 2023.

Exhibit 8b: Sub-regional contribution to GDP growth

	2020	2021	2022	2023 forecast
North Africa	28%	29%	30%	29%
West Africa	29%	28%	26%	27%
Southern Africa	21%	21%	21%	23%
East Africa	16%	16%	14%	15%
Central Africa	6%	6%	6%	6%

Sources: IMF and Afrexibank Research

several countries across Africa, and they are receiving backing from governments and development finance institutions, including the African Export-Import Bank through its Creative Africa Nexus (CANEX).<sup>35</sup> E-commerce has also become a major economic driver, with great potential to boost competitiveness. Most recent estimates show that Nigeria's e-commerce sector is expected to be worth US\$90bn in 2023, representing annual growth of around 11.7% (Okereocha, 2023).<sup>36</sup>

However, in the short term, oil, which continues to be the major source of government revenues and foreign exchange earnings, will be the main growth driver in Nigeria. After the lowest historical record set by the country in 2022 oil production levels are expected to increase as

progress is made on the security front and commodity terms of trade remain favourable, with oil prices above the country's fiscal breakeven point of US\$75 per barrel (Okonkwo, 2023).<sup>37</sup>

The average growth rate of member countries of the Southern African Development Community (SADC) is forecast to remain relatively low, in fact the lowest across all subregions. Southern Africa's aggregate GDP growth is expected to decelerate to 2.1% in 2023, down from 2.5% last year. The subregion's growth prospects are weighed down by South Africa, which is contending with energy crises and where aggressive monetary tightening is expected to temper investment growth and domestic demand.

Nonetheless, the SADC subregion remains a heavyweight in spite of its weaker growth prospects, reflecting the importance of South Africa as well as the growing size of a few other economies, notably Angola. Even though South Africa's relative contribution to overall growth on the continent is forecast to decrease to 13% in 2023, the lowest level over the past few years, the Southern Africa subregion is still projected to account for 23% of African aggregate GDP expansion, up from 21% last year.

Despite the ongoing geographical diversification of growth drivers—with a growing crop of small African nations leaping up the tables of the world's fastest-growing economies (Exhibit 9)—the region's growth performance continues to be driven primarily by developments in its three largest economies, Egypt, Nigeria and South Africa.

Taken together, these countries are projected to account for around 50% of Africa's aggregate economic output in 2023 (Exhibit 10).

Simultaneously, patterns of growth and trade are still dominated by commodity market dynamics. According to the most recent State of Commodity Dependence Report released by the United Nations Conference on Trade and Development, more than 80% of African countries remain highly commodity dependent (UNCTAD, 2021).<sup>38</sup>

In a world where global trade has been driven largely by manufactured goods with increasing technological content, the excessive reliance on commodities has constrained the growth of African trade, which represents less than 3% of global trade. The AfCFTA, which is expected to accelerate the diversification of sources of growth to significantly boost African trade, has the potential to boost intra-African exchange and rebalance the distribution of growth across subregions. At present, the market is heavily skewed towards North Africa, the continent's most industrialised subregion.



Most recent estimates show that Nigeria's e-commerce sector is expected to be worth US\$90bn in 2023, representing annual growth of around 11.7%.

<sup>30</sup> Ghana defaulted on its debt in December 2022 and has applied to the G20 Common Framework for Debt Restructuring. For more details, see <https://www.reuters.com/article/ghana-economy-debt-idAFL1N32V0IE>

<sup>31</sup> As the Central Bank of Nigeria signals stopping sales several Nigerian banks resorted to rationing of US dollars last year. For more details, see <https://www.bloomberg.com/news/articles/2022-03-11/nigeria-banks-ration-dollars-as-regulator-signals-stopping-sales>

Exhibit 9: Top-10 fastest-growing economies in the world

Country	2020	Country	2021	Country	2022	Country	2023
Tuvalu	43.5	Libya	177.3	Guyana	57.8	Macao SAR	56.7
Libya	7.1	Maldives	33.4	Fiji	12.5	Guyana	25.2
Rwanda	6.1	Guyana	19.9	Caribbean	12.4	Libya	17.9
Ethiopia	5.9	Macao SAR	18	Seychelles	10.9	Palau	12.3
Bangladesh	4.8	Aruba	16.8	Barbados	10.5	Senegal	8.1
Uganda	4.5	Panama	15.3	Saint Kitts and Nevis	9.8	Niger	7.3
Armenia	3.8	Moldova	13.9	Iraq	9.3	Caribbean	7.3
Djibouti	3.6	Ireland	13.5	Saint Lucia	9.1	Fiji	6.9
Dominica	3.6	Peru	13.3	Georgia	9	Congo, DRC	6.7
Tajikistan	3.5	Botswana	12.5	Ireland	9	Rwanda	6.7

Sources: IMF and Afrexibank Research

The AfCFTA, which is expected to accelerate the diversification of sources of growth to significantly boost African trade, has the potential to boost intra-African exchange and rebalance the distribution of growth across subregions.

32 For more details, see <https://thenationonlineng.net/nigerias-e-commerce-industry-major-growth-driver/>

33 For more details, see <https://www.thisdaylive.com/index.php/2023/01/18/logistics-market-new-driver-of-economic-growth-in-nigeria/>

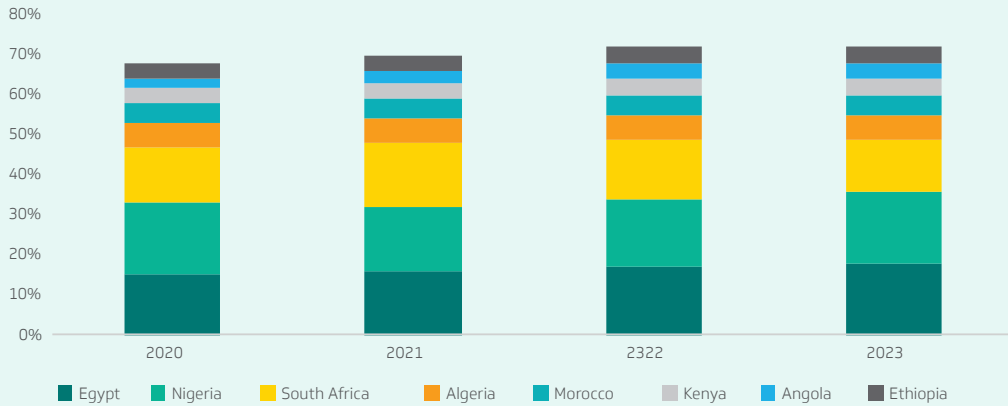
34 A recent study found that the creative industries employ 4.2m people across five sectors (media, entertainment, beauty and lifestyle, visual arts, and tourism and hospitality) and could add an additional 2.7m jobs by 2025. For more details, see [https://en.unesco.org/creativity/sites/creativity/files/qpr/contributions\\_of\\_cultural\\_industries\\_by\\_osasonaolutimi\\_james.pdf](https://en.unesco.org/creativity/sites/creativity/files/qpr/contributions_of_cultural_industries_by_osasonaolutimi_james.pdf)

35 For instance, through its Creative Africa Nexus, the African Export-Import Bank is supporting Africa's creative and cultural industries. For more details, see <https://www.afrexibank.com/the-creative-africa-nexus-canex-summit-kicks-off-on-day-5-of-iatf-2021/>

36 For more details, see <https://thenationonlineng.net/nigerias-e-commerce-industry-major-growth-driver/>



**Exhibit 10a: Relative contribution of large economies to regional growth**



Sources: IMF and Afrexibank Research

**Exhibit 10b: Top contributors to Africa's GDP**

	2020	2021	2022	2023
Egypt	15%	16%	17%	18%
Nigeria	18%	16%	17%	18%
South Africa	14%	16%	15%	13%
Algeria	6%	6%	6%	6%
Morocco	5%	5%	5%	5%
Kenya	4%	4%	4%	4%
Angola	2%	3%	4%	4%
Ethiopia	4%	4%	4%	4%

Source: IMF and Afrexibank Research

37 The Nigerian government expects US\$75 to be the average price for 2023, to balance the budget. For more details, see <https://nairametrics.com/2022/12/29/2023-budget-nigeria-raises-crude-oil-benchmark-to-75-per-barrel/>

38 Commodity dependence refers to countries that derive more than 60% of their foreign exchange earnings from the commodity sector. According to the most recent UNCTAD's State of Commodity Dependence study, 48 out of 54 countries—or 89% of African countries were commodity dependent in 2019, compared to 51% in Asia, 43% in the Americas and 12% in Europe. For more details, see <https://unctad.org/publication/state-commodity-dependence-2021>

## V. Internal drivers of growth resilience

**Africa's growth resilience and projected economic expansion are underpinned by various internal and external drivers that will continue to play key roles in both the short and medium term. Internally, several drivers have the potential to sustain and even accelerate growth prospects across the region, including: rising infrastructure investment; ongoing structural transformation and the diversification of sources of growth; an improving macroeconomic environment; and digitalisation.**

The latter in particular has become an engine of productivity growth and is expanding opportunities across a wide range of industries (Begazo et al. 2023).<sup>39</sup>

**Increasing commitment to macroeconomic stability:** Myriad global headwinds have given African governments which have made significant progress over the last few years, most notably in the area of budget framework and monetary credibility (IMF, 2022b), yet more opportunities to demonstrate their commitment to macroeconomic stability through the implementation of difficult reforms. After sharply dropping policy rates to support

economic recovery following the outbreak of Covid-19, African monetary authorities were in the vanguard of the global pivot to curb inflationary pressures in 2022. Despite suffering from Great Depression levels of unemployment, around two-thirds of countries pre-emptively increased their policy rates (World Bank, 2023), with several raising them to record highs, including double-digit levels in 10 countries (Exhibit 11).

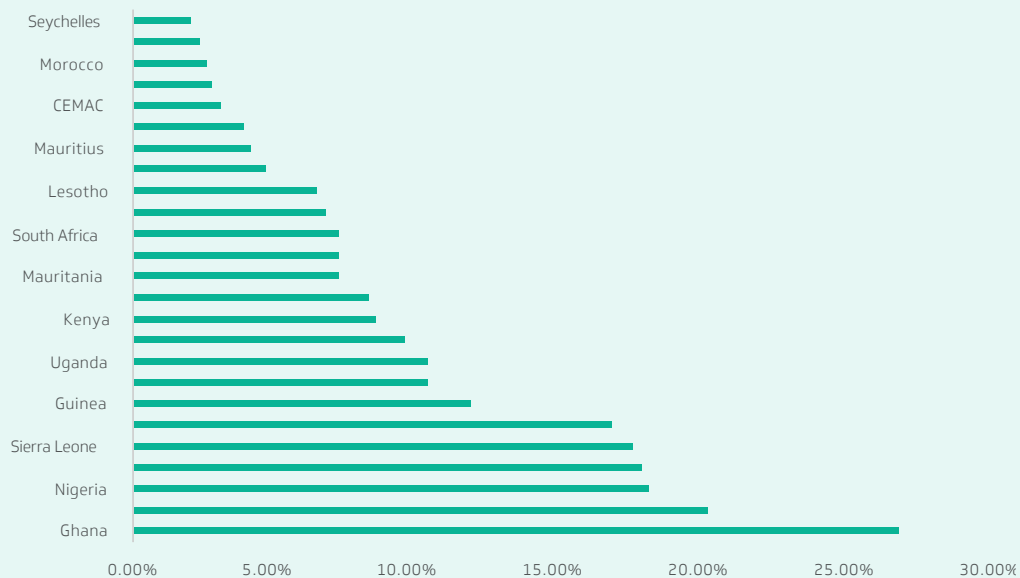
Although Angola's inflation rate slowed for the 11th straight month to close 2022 at 13.86%, the country's central bank maintained its policy rate at 20% throughout the year. That pre-emptive policy tightening cycle, a model that several countries across the region adopted, has more than paid off. Inflation peaked in most countries in 2022 and price pressures have eased. Forecasts suggest average inflation will fall to 12.4% in 2023 (down from 14.5% in 2022) and continue to decline sharply in 2024 to 8.7% (Exhibit 12).

<sup>39</sup> In its latest report, Digital Africa, the World Bank provides the best available evidence on the transformative effects of digital technologies in the region. For more details, see <https://www.worldbank.org/en/region/afr/publication/digital-africa>



Despite suffering from Great Depression levels of unemployment, around two-thirds of countries pre-emptively increased their policy rates.

Exhibit 11: Policy interest in Africa end-2022



Sources: IMF and Afrexibank Research

This should enable monetary authorities across the region to shift their focus away from the single objective of inflation targeting towards an approach that balances curtailing price rises with pursuing growth. Angola took the lead in that monetary rebalancing act earlier this year. After cutting its policy rate by 150 basis points in January to bring borrowing costs to their lowest level since June 2021, the National Bank of

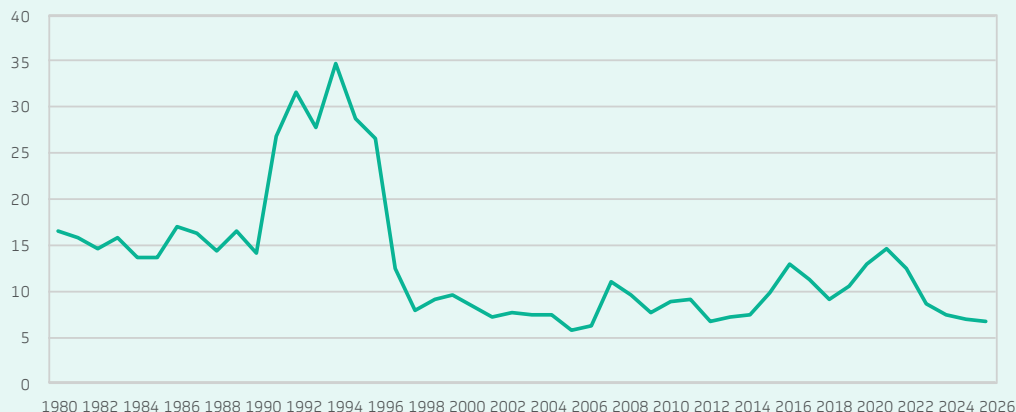
Angola cut its benchmark policy rate by a further 100 basis points in March.

**Harnessing the transformational power of digitalisation:** Africa is undergoing a digital revolution that is bolstering the business environment by raising productivity and competitiveness to drive investment. The results of digitalisation impact assessments are



Africa is undergoing a digital revolution that is bolstering the business environment by raising productivity and competitiveness to drive investment.

Exhibit 12: Dynamics of inflation in Africa (annual percentage change)



Sources: IMF and Afrexibank Research

encouraging, with evidence showing that when high-quality internet was available for at least three years, labour force participation increased by three percentage points in Nigeria and by eight points in Tanzania (Begazo et al. 2023).<sup>40</sup> The digital revolution will continue to drive growth in the coming years, especially as countries adopt innovative solutions established during the information and communications technology (ICT) era to help realise their development potential.

Mobile technology and services generated 8% of GDP in Sub-Saharan Africa in 2021, with indirect productivity benefits in non-ICT sectors accounting for 5% (GSMA, 2021). Africa's digital economy could contribute nearly US\$180bn to the region's growth by the middle of this decade (WEF, 2022). These figures reflect the wide-ranging upshots of digitalisation across various sectors and how technology empowers entrepreneurial thinking. Digitalisation has catalysed the growth of African start-ups, turning the region into one of the world's fastest-growing innovation ecosystems. Between 2015-22, the number of African start-ups rose more than fourfold from 125 to 564 (Tafese, 2022).

<sup>40</sup> High-quality internet refers to third- or fourth-generation (3G or 4G) mobile communication technology (Begazo et al., 2023).



## Digitalisation has catalysed the growth of African start-ups, turning the region into one of the world's fastest-growing innovation ecosystems.

These start-ups are driving opportunities across a broad array of industries, including agricultural supply chains, manufacturing, transportation, logistics, retail, entertainment and financial services. In addition to accelerating the formalisation and standardisation of Africa's predominantly modestly-sized and informal service and agricultural activities, digitalisation is generating much-needed scale and innovation to enable massive increases in productivity.

These start-ups are also attracting investors from around the world, leveraging additional resources to support growth even as African countries are shut out of international capital markets. Since 2015, the volume of venture capital funding flowing towards start-ups in the region has increased dramatically, climbing from just under US\$186m to more than US\$2.1bn, with the largest year-on-year increase taking place after the onset of the Covid-19 pandemic (Tafese, 2022). Meanwhile, no fewer than seven African tech start-ups have acquired 'unicorn' status, the term used to describe privately-owned start-ups worth more than US\$1bn. Last year Nigerian fintech Flutterwave was valued at US\$3bn, making it Africa's most valuable start-up (Tafese, 2022).

Just as significant has been greater investment in digitalisation by African governments, development finance institutions, the domestic private sector and multinational companies. Between 2003-20 the number of new ICT projects launched in Africa by multinationals increased almost fivefold from 93 (worth US\$3.7bn) in 2003-05 to 464 projects (worth US\$23.5bn) in 2018-20 (Tafese, 2022).<sup>41</sup> Beyond bridging the technology divide and lowering the cost of access to digital services, these investments will propel productivity growth in Africa and boost investor confidence.

**Raising power generation capacity to boost growth and reassure investors:** Africa's growth resilience has been buoyed recently by higher investment in physical infrastructure, particularly in the power sector. For decades, chronic electricity deficits have been one of the greatest binding constraints on productivity growth and industrial output expansion across the region.



Major projects that gained traction over the past few years are expected to bring more power generation capacity on stream in 2023 and in the near future.

Major projects that gained traction over the past few years are expected to bring more power generation capacity on stream in 2023 and in the near future.<sup>42</sup> Among these projects, two are especially significant: the Grand Ethiopian Renaissance Dam (GERD), and South Africa's Redstone concentrated solar thermal power plant.

Both ventures are part of a large pipeline of hydroelectric, solar and wind projects intended to boost the region's installed capacity of renewable energy. At full strength, the GERD will see its total installed power generation capacity rise to 5,000-5,500 megawatts (EIU, 2023). The growth and welfare benefits of better power generation capacity will be felt keenly across the region and especially in larger economies, including South Africa and Ethiopia.

Power deficits are chronic in most African countries—the 48 nations comprising sub-Saharan Africa, with a combined population of more than 800m, generate the same amount of power as Spain, home to fewer than 50m people.<sup>43</sup> Lately, however, these deficits' negative economic consequences have been especially damaging for South Africa, where load-shedding and power cuts to help balance the supply and demand of electricity and avoid national blackouts have reduced GDP by as much as 1.3% annually since 2007 (Gbadanosi, 2023).<sup>44</sup>

Beyond boosting output in the short term, these major initiatives designed to address chronic power deficits through a mix of hydroelectricity, solar and wind projects have the potential to revitalise industrial production and sustain the expansion of manufacturing output in the long term.

#### **Progress towards the implementation of the AfCFTA 45 augurs well for structural transformation and growth resilience:**

Several significant milestones on the AfCFTA's implementation path have been reached since this time last year. These include: the launch of the AfCFTA Adjustment Fund<sup>46</sup> to support sovereign and corporate entities to offset losses and smooth the transition process (Oramah, 2021); progress in the Trade in Goods Protocol, with 46 countries submitting provisional schedules of tariff concessions; and similar progress in the Trade in Services Protocol, with 47 countries submitting initial services offers in the five priority sectors of business services, financial services, communications, transportation and tourism.



The AfCFTA, which is expected to accelerate the diversification of sources of growth to significantly boost African trade, has the potential to boost intra-African exchange and rebalance the distribution of growth across subregions.



In addition to expanding fiscal space to bolster macroeconomic stability and diversify sources of growth, the AfCFTA is set to significantly boost and shift the composition of African trade to engender conditions for long-run growth.

Moreover, phase two negotiations delivered Protocols on Intellectual Property Rights and on Investment and Competition, as well as considerable progress towards the AfCFTA's rules of origin, of which more than 88% have been agreed, with only the automotive and textile sectors unresolved. To fast-track the transition towards trading under preferential rules, the Secretariat launched the Guided Trade Initiative (GTI), and eight countries agreed to start commercially-meaningful trade under the AfCFTA for at least 96 products.<sup>47</sup> Rolling out the GTI in 2023 will present a major incentive for the full operationalisation of the continental trade integration reform.

The rules of origin—which have been touted as an industrialisation accelerator, as they provide fiscal incentives for higher domestic production of manufactured goods—will reduce Africa's exposure to global volatility and recurrent adverse commodity terms of trade shocks. In addition to expanding fiscal space to bolster macroeconomic stability and diversify sources of growth, the AfCFTA is set to significantly boost and shift the composition of African trade to engender conditions for long-run growth. Preliminary estimates show that the agreement will boost intra-African trade by more than 81% and extra-African trade by 19%. Manufactured goods are expected to see the biggest gains, including a 110% increase for intra-African trade and 46% jump in extra-African trade (World Bank, 2020).

44 For more details, see <https://foreignpolicy.com/2023/01/25/south-africa-energy-crisis-corruption-anc/>

45 The AfCFTA brings together 55 African countries to create a market of around 1.4bn people with a combined GDP exceeding US\$3tn, making it the fifth largest economy in the world in GDP terms. For more details, see [https://www.brookings.edu/wp-content/uploads/2020/12/20.12.28-AfCFTA\\_Fofack.pdf](https://www.brookings.edu/wp-content/uploads/2020/12/20.12.28-AfCFTA_Fofack.pdf)

46 The African Export-Import Bank has committed an initial sum of US\$1bn to the Fund and will engage development partners to raise that amount to US\$8bn. For more details, see Oramah (2021), <https://www.atlantis-press.com/journals/jat/125966586>

47 These countries include Cameroon, Egypt, Ghana, Kenya, Mauritius, Rwanda, Tanzania and Tunisia. For more details, see <https://www.un.org/africarenewal/magazine/february-2023/au-summit-2023-powering-trade-through-afcfta>





## VI. External drivers of growth resilience

**On the 40th anniversary of her accession to the British throne, Queen Elizabeth II remarked that “1992 is not a year on which I shall look back with undiluted pleasure. In the words of one of my more sympathetic correspondents, it has turned out to be an ‘Annus Horribilis’.”<sup>48</sup>**

In the finance and economic development arena, 2022 may also be remembered as an *Annus Horribilis* in light of the extremely difficult operating environment, especially for emerging markets. When policymakers in systemically important central banks began to adopt aggressive monetary tightening, these developing economies had to contend with growth-crushing and default-driven borrowing rates (IMF, 2023).

In addition to lacklustre growth performance in China and Europe—which, combined, are the destination of more than 50% of all African exports—the constriction of global financial conditions in 2022 came at huge costs in terms of macroeconomic management, growth, access to financing and servicing of external debt (de Mello e Souza, 2022).<sup>49</sup> Moreover, the sharp appreciation of the dollar, by 25%, made the fight against rising prices even harder in emerging

markets and developing economies, where the exchange rate ‘pass-through’ exacerbated inflationary conditions.

For countries across Africa—several of which suffered from large-scale procyclical downgrades at the height of the pandemic and were shut out of international capital markets—aggressive monetary tightening greatly intensified refinancing risks 93% across the region (Fofack, 2021b),<sup>50</sup> coupled with the sharp depreciation of local currencies—more than 60% of African currencies suffered depreciation in 2022, with the Egyptian pound and the Nigerian naira depreciating by 55% and 10.2%, respectively—the fiscal incidence of sovereign debt increased considerably, raising the risk of debt distress.<sup>51</sup> While the procyclical downgrades shut out most countries, the few that could still access the capital markets did so only at a higher exchange rate and higher interest rate.

In comparison, we expect the operating environment to be more favourable and growth-friendly in 2023, owing to various factors.

<sup>48</sup> For more details, see <https://www.royal.uk/annus-horribilis-speech>

<sup>49</sup> For more details, see <https://www.dandc.eu/en/article/how-fast-appreciating-us-currency-causing-stress-developing-countries-and-emerging-markets>

<sup>50</sup> More than 56% of rated African countries suffered downgrades at the height of the pandemic downturn in 2020, raising the percentage of countries rated as sub-investment grade borrowers to 93% across the region (Fofack, 2021b). For more details, see <https://www.brookings.edu/research/the-ruinous-price-for-africa-of-pernicious-perception-premiums/>

<sup>51</sup> The Egyptian Pound has plunged almost 20% against the US dollar since the start of the year, extending a decline that saw it lose more than 50% of its value in 2022. For more details, see <https://www.cnbc.com/2023/04/05/the-egyptian-pound-is-amongst-the-worst-performing-currencies-in-2023.html>



## Dollar depreciation will also reduce the risk of sovereign and corporate defaults to maintain the most vulnerable countries on an expansionary trajectory.

**First, the depreciation of the dollar —which began in late 2022 as uncertainty surrounding inflation and volatility abated—will continue and even accelerate in the second half of this year as the downshift in US market yields takes hold.** Recent developments in the US banking sector, which led the Fed to back off from jumbo rate hikes and return to a more incremental approach in March, may demarcate a shift in monetary policy. The market is already pricing in a policy pivot, with the Fed projected to begin cutting rates later this year (Rajan and Acharya, 2023).

With the significant overvaluation of the dollar against most currencies having peaked last year, the greenback's accelerated depreciation as monetary policy shifts will act as a fiscally-neutral stimulus to emerging markets and developing economies. For Africa, where most countries are 'price-takers' and run structurally large current account deficits, this will reduce the fiscal incidence of external debt servicing as loans become less expensive measured in local currencies. This in turn will increase countries' fiscal space and alleviate pressure on foreign exchange reserves as the external account improves.

Dollar depreciation will also reduce the risk of sovereign and corporate defaults to maintain the most vulnerable countries on an expansionary trajectory. World Bank research shows that debt restructuring is costly and leads to lower short-

term output growth (Fan et al., 2022).<sup>52</sup> Moreover, the weakening of the dollar and a shift in monetary policy by systemically important central bank—the Fed is again providing liquidity through its discount window and other channels—could also increase appetite for African assets. This may facilitate the return of African sovereigns and corporate entities to international capital markets, enabling them to raise much-needed resources to boost investment growth after bond issuance collapsed last year (Exhibit 13). Only three African nations (Angola, Nigeria and South Africa) successfully accessed capital markets in 2022, raising US\$6bn, down from nine that raised almost US\$20bn in 2021 (Fofack, 2022b).<sup>53</sup>

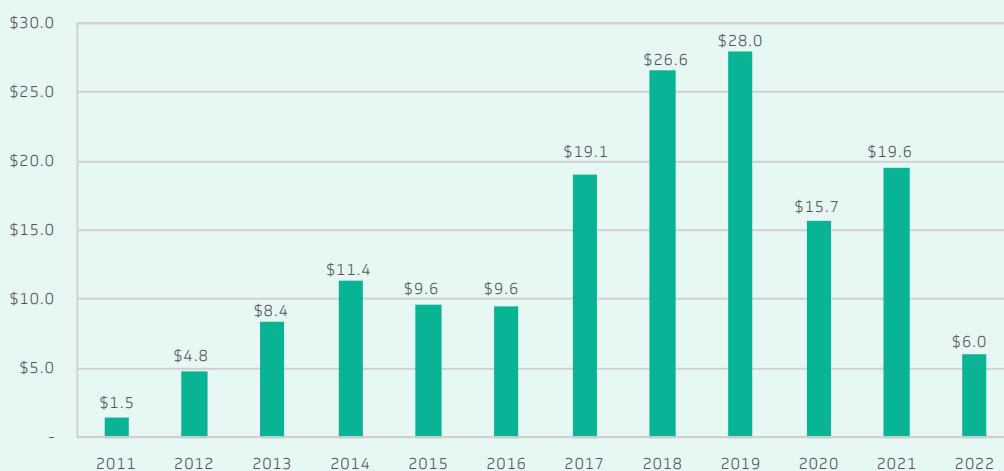
**Second, the region will benefit from a strong rebound in China, which has become Africa's single largest trading partner.** After decelerating sharply to just 3% in 2022, Chinese GDP is forecast to expand by at least 5.5% this year. This reversal in fortunes is being buoyed by strong consumer demand, which contributed 33% of GDP growth in 2022 and is set to play an even more pivotal role after the lifting of containment measures associated with the stringent zero-Covid policy (Yongding, 2023).<sup>54</sup> China's strong rebound could compensate for the sharp growth deceleration projected in most advanced economies and keep the world economy on an expansionary track.

<sup>52</sup> For more details, see <https://documents1.worldbank.org/curated/en/099321004252230289/pdf/0de4dbded0c5a20423d09daa0812ba37ea173.pdf>

<sup>53</sup> The list of countries that successfully issued sovereign bonds in 2021 includes: Benin, Cameroon, Egypt, Gabon, Ghana, Kenya, Nigeria, Rwanda and Senegal. For more details, see <https://media.afreximbank.com/afrexim/Africas-2022-Growth-Prospects.pdf>

China's strong rebound could compensate for the sharp growth deceleration projected in most advanced economies and keep the world economy on an expansionary track.

Exhibit 13: Trend of sovereign bond issuances in Africa (US\$bn)



Sources: Bloomberg and Afreximbank

Owing to deeper China-Africa trade channels, the degree of dependency between the two economies has strengthened markedly since the turn of the century. According to IMF research, a one percentage point increase in China's domestic investment growth is associated with an average 0.6 percentage point increase in Sub-Saharan countries' export growth (Drummond and Lin, 2013). The same study found the impact of China's investment growth is even larger for resource-rich African countries, and especially oil exporters.

Over the last two decades, China has been the rising tide lifting all African commodity-exporting boats. Beyond allaying any fears of a hard landing, including the risk of recession and rising unemployment, the strong rebound in China's economy—which has also recorded very low levels of inflation and maintained a strong fiscal position, enabling the government to enact fiscal and monetary stimulus after exiting its stringent zero-Covid policy—augurs well for Africa (IMF, 2023; Feld, 2023).<sup>54</sup> More than 80% of African countries remain highly commodity-dependent and could see a major boost in global demand for commodities, which remain the region's key driver of foreign exchange reserves.

<sup>54</sup> For more details, see <https://www.project-syndicate.org/commentary/china-strong-growth-2023-expansionary-monetary-and-fiscal-policy-by-yu-yongding-2023-02>



Over the last two decades, China has been the rising tide lifting all African commodity-exporting boats.

**Third, the relatively low procyclicality and volatility of remittance inflows, which have increased steadily over the last two decades, will continue to enhance growth.** Despite the challenging conditions that characterised 2022, remittance inflows to Africa increased by 4.3% to reach a record US\$100.3bn (Exhibit 14). World Bank projections show remittance inflows to Africa remaining on an upward trend, increasing by around 4% in 2023, with advances in digitalisation also steadily reducing transfer costs (World Bank, 2022b).<sup>56</sup>

In addition to welfare improvement and poverty alleviation through consumption smoothing, remittances are fuelling investment growth. In practice, they are a more reliable alternative financing source in the face of declining official development assistance (ODA) and volatile foreign direct investment (FDI). Remittances have also emerged as a balance of payments

stabiliser and were particularly helpful in 2022 when the sharp appreciation of the dollar exposed countries to significant macroeconomic management challenges.

Nigeria and Egypt offer two illustrative examples, with remittances inflows to both countries mitigating the threat of major current account reversals in 2022 associated with the depreciation of their currencies and dwindling stocks of international reserves (World Bank, 2022b).<sup>57</sup> But the growth and development impact of robust remittances inflows are perhaps even more important for smaller economies, where they account for a significant share of GDP, including 28% in Gambia and 21% in Lesotho for instance (Exhibit 15).

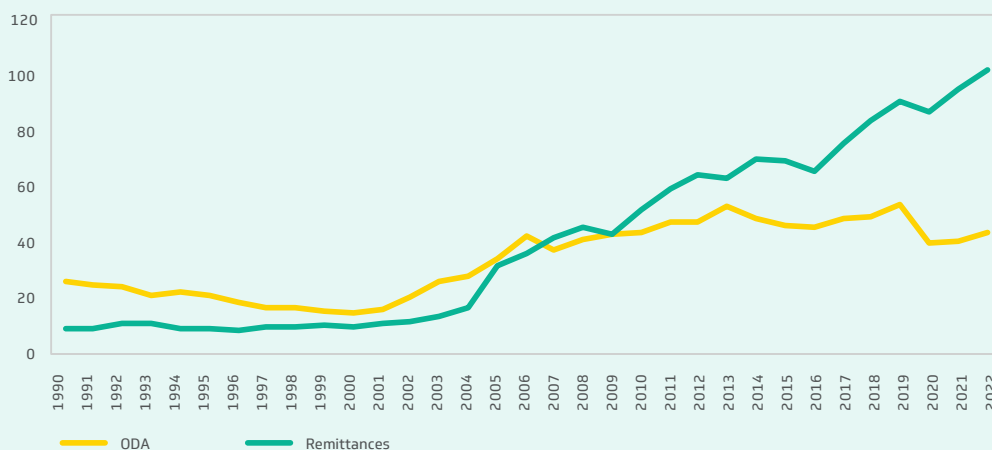


In addition to welfare improvement and poverty alleviation through consumption smoothing, remittances are fuelling investment growth.

<sup>55</sup> Among large economies, China and Japan are the only countries that have maintained price stability, with China's consumer price index averaging increases of less than 2%. For more details, see <https://www.project-syndicate.org/onpoint/inflation-persists-because-macroeconomic-problem-weak-fiscal-policy-by-lars-p-feld-2023-03#:~:text=Inflation%20tends%20to%20become%20persistent,passed%20through%20the%20value%20chain>

<sup>56</sup> For more details, see [https://www.knomad.org/sites/default/files/publication-doc/migration\\_and\\_development\\_brief\\_37\\_nov\\_2022.pdf](https://www.knomad.org/sites/default/files/publication-doc/migration_and_development_brief_37_nov_2022.pdf)

Exhibit 14: Trend of remittances inflows to Africa (in US\$bn)



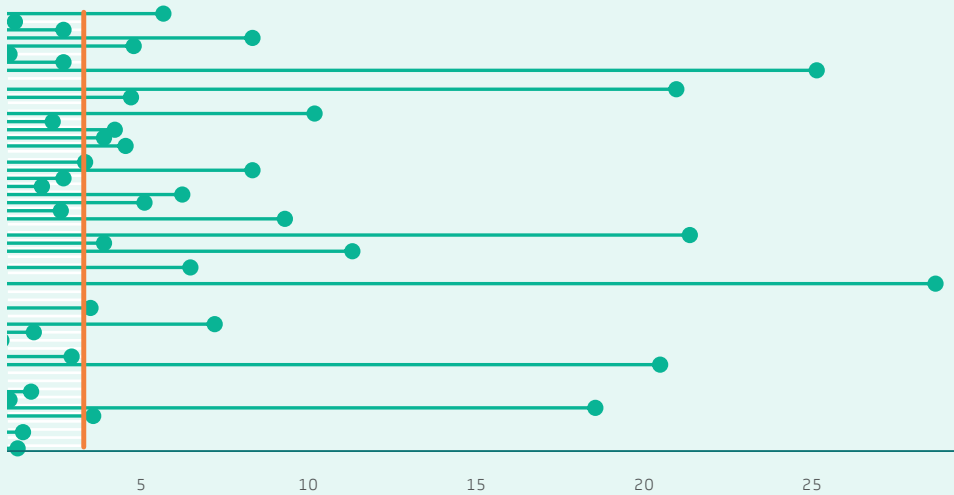
Sources: World Bank and Afreximbank

**Fourth, the geopolitical realignment of global supply chains will further strengthen the foundation of growth resilience in the region.** While the depreciation of the dollar and China's economic rebound will generate palpable positive spillover effects for Africa in the near term, other key factors will accelerate industrialisation and fortify the foundations for regional growth resilience in the medium and long term. Two are especially relevant: the realignment of global supply chains, and greater commitments to decarbonisation.

The promotion of 'friend-shoring' (i.e. shifting supply chains away from geopolitical rivals) will lead to the decentralisation of global supply chains, encouraging resilience. The inherent risks of relying excessively on just-in-time global supply chains became clear during the Covid-19 crisis, when countries found it increasingly difficult to source goods (including vital medical equipment). But a rise in geopolitical tensions also exacerbated ongoing efforts to mitigate the risk of this excessive concentration of global supply chains through 'friend-shoring' or 'near-shoring' (i.e. transfer processes or supply links to markets that are geographically closer to the core business).

<sup>57</sup> Egypt and Nigeria, the top-two recipients of remittances to Africa are among the top-10 recipients world-wide. Last year, Egypt received US\$32 billion and Nigeria US\$21 billion. For more details, see [https://www.knomad.org/sites/default/files/publication-doc/migration\\_and\\_development\\_brief\\_37\\_nov\\_2022.pdf](https://www.knomad.org/sites/default/files/publication-doc/migration_and_development_brief_37_nov_2022.pdf)

Exhibit 15: Remittances as a share of GDP in 2022



Sources: IMF and Afrexibank Research

Decentralising these supply chains offers Africa an opportunity to transcend the colonial development model of resource extraction and become better integrated into the world economy through greater backward participation in global value chains. The latter involves using

imported inputs to produce manufactured goods that are then shipped abroad—generating higher absolute levels of gross exports, domestic value added and employment—rather than chiefly (or often only) as a provider of raw materials that other economies then capitalise on.

▼ Favoring the friend-shoring of supply chains to a large number of trusted countries, so we can continue to securely extend market access, will lower the risks to our economy as well as to our trusted trade partners.

Janet Yellen, U.S. Treasury Secretary



Image: commons.wikimedia



The geopolitically-led decentralisation of global supply chains, therefore, will support the development of more robust regional value chains in Africa. This, in turn, could hasten the shift away from the highly carbon-intensive ‘round-tripping’ trade model, under which African countries export crude oil to other nations and then import refined petroleum. In addition to the costliness of this model, which sees not only oil but potential employment opportunities exported, round-tripping contributes a major portion of the shipping industry’s sizable carbon footprint (Faber and Lee, 2017).<sup>58</sup>

The AfCFTA will act as a pull factor that increases the region’s competitiveness as global supply chains are realigned (Fofack, 2018).<sup>59</sup> By allowing corporations to spread the risk of investing in smaller markets, economies of scale associated with the continental trade integration reform will boost African countries’ productivity and competitiveness. Completing the virtuous circle, these productivity gains will help to accelerate the development of regional value chains and facilitate Africa’s integration into global value chains through backward activities.



Decentralising these supply chains offers Africa an opportunity to transcend the colonial development model of resource extraction and become better integrated into the world economy through greater backward participation in global value chains.

<sup>58</sup> The shipping industry, which accounts for more than 3% of annual greenhouse gas emissions, is projected to become one of the major drivers of climate change in the coming decades, with its emissions set to increase by 20%-120% between 2012-50. For more details, see [https://cedelft.eu/wp-content/uploads/sites/2/2021/03/IMO\\_7169\\_Reduction\\_GHG\\_Emissions\\_ships\\_FULLREPORT.pdf](https://cedelft.eu/wp-content/uploads/sites/2/2021/03/IMO_7169_Reduction_GHG_Emissions_ships_FULLREPORT.pdf) and <https://www.transportenvironment.org/challenges/ships/greenhouse-gases/>

<sup>59</sup> The AfCFTA will significantly boost competitiveness across Africa by addressing inefficiencies that have constrained economic growth. For more details, see <https://www.imf.org/en/Publications/fandd/issues/2018/12/afcfta-economic-integration-in-africa-fofack>

## VII. Risk to the outlook

**Even as China's strong economic rebound is expected to lift global demand and boost African trade, the balance of risks to Africa's baseline growth forecasts remains tilted to the downside.**

We are in a challenging global environment in which achieving the right balance between combating inflation and supporting growth has been made even more difficult following the collapses of SVB and Signature Bank in the US, which have aggravated tensions between price stability and financial stability. In the immediate term, restraining inflation in the most affected leading economies without provoking a hard landing or a full-blown financial crisis remains the most urgent challenge and risk to both global and African growth.

Africa's projected growth resilience is therefore tied firmly to developments in the global economy, in addition to other critical factors that will shape its near-term path. These include: how systemically important central banks tackle persistent inflation; geopolitical risks and attendant supply-chain disruption; trade wars and fragmentation risks; conflict and growing insecurity; and climate change. The latter two are especially worthy of consideration. The quest for peace in conflict-stricken parts of Africa has been made even more punishing in the aftermath of the Covid-19 crisis, given the degree to which responding to the pandemic constrained countries' already-limited fiscal space. And climate change, of course, has grown into a perennial risk with wide-ranging consequences for growth and food security in a region that remains highly dependent on rain-fed agriculture.

 In the immediate term, restraining inflation in the most affected leading economies without provoking a hard landing or a full-blown financial crisis remains the most urgent challenge and risk to both global and African growth.



## Security is a key regional risk to Africa’s growth prospects, though in this age of new great power rivalries it possesses a global geopolitical twist.

Recent developments suggest the Fed is preparing to slow the pace and quantum of interest rate rises. However, if inflation remains stubbornly high in a still-tight labour market—or if there is an acceleration thereof, generated either by reflationary impulses connected to China’s economic rebound or geopolitically-driven supply-chain disruption—policymakers may advocate for yet more aggressive monetary tightening. This would have significant adverse implications for Africa, which is highly exposed to external debt denominated largely in foreign currencies—the “original sin” (Eichengreen and Hausmann, 1999).<sup>60</sup>

Last year, tightening global financial conditions resulted in disproportionate increases in risk spreads and large-scale capital flow reversals. This caused most African countries to be shut out of capital markets and, for those that defended their currency, drained hard-earned foreign exchange reserves. In addition to shutting even more countries out of international capital markets, any additional monetary tightening risks further eroding global investor sentiment, which would trigger yet another wave of damaging capital outflows. The attendant currency depreciation would raise the cost of servicing external debt, undermining fiscal and debt sustainability objectives. Moreover, it could enflame inflationary pressures, especially in a region where a greater exchange rate pass-through has been an important transmission channel.

At the same time, inflation dynamics are shaped by geopolitical uncertainty. Following the outbreak of the Ukraine crisis, these tensions compounded supply-chain disruptions and supply-demand imbalances, driving up food and energy prices. The social and macroeconomic consequences were significant for African countries, which saw current account deficits widen and, among the most vulnerable nations, had to contend with the higher risk of food crisis.

Heightened geopolitical risk remains the paramount threat to global and African growth. Reviving and strengthening international co-operation has never been more critical and should be prioritised in the search for shared solutions to global crises. Bringing the Sino-US trade war to an end would not only give a much-needed boost to growth, it would also reduce the impact of tariffs on trade costs and alleviate inflationary pressures.

Security is a key regional risk to Africa’s growth prospects, though in this age of new great power rivalries it possesses a global geopolitical twist. Across conflict-afflicted countries, especially in the Sahel, military expenditures have become one of the largest items in national budgets as countries strive to curb the growth of transnational terrorist networks (Fofack, 2022). In addition to undermining cross-border trade and public investment—in a region where infrastructure deficits have long constrained growth—rising military outlays have aggravated


<sup>60</sup> The “original sin” emphasises an incompleteness in financial markets that prevents the domestic currency from being used to borrow abroad or to borrow long term, even domestically. For more details, see <https://www.nber.org/papers/w7418>

fiscal deficits and weakened governments' ability to respond to various crises. Apart from conflict-related emergencies, these can range from climate-related risks, including extreme weather events, poverty and food insecurity, and the rising costs of external debt servicing. Any further deterioration of the security environment will weigh heavily on Africa's growth outlook in the short term and undercut the expansion of intra-African trade, which has great potential for mitigating the region's exposure to global volatility but remains dismally low at present.

A worsening security environment would also deter long-term investment and undermine structural transformation. Both are key to reducing the unhealthy correlation in Africa between growth and commodity price cycles, which are responsible for recurrent balance of payments crises that drive external liabilities (Fofack, 20219). While the AfCFTA is a necessary condition for accelerating the diversification of sources of growth and boosting both extra- and intra-African trade, it is not sufficient in and of itself. Successfully implementing the AfCFTA also hinges on addressing non-tariff barriers and injecting long-term and patient capital.

Steps taken recently to boost power generation capacity and progress made on the rules of origin are key milestones on the path towards the AfCFTA's implementation. Besides growing the tax base and expanding employment opportunities, the benefits of structural transformation brought about by the continental trade integration reform will be especially significant for fiscal and debt sustainability. For the average African economy, an additional percentage point of annual GDP growth over a decade could reduce its debt ratio by almost 15 percentage points (IMF, 2022b).<sup>61</sup>

But in the immediate term, reining in inflation must be the priority. At this critical juncture of heightened global volatility and geopolitical uncertainty, striking the correct balance between curbing inflationary pressures and buttressing growth is crucial. This is especially true for African countries, which depend heavily on external financing for growth and trade, but which have been the most affected by aggressive monetary tightening on the global stage. Even though the sovereign debt of African countries is extremely low, they are overburdened by default-driven borrowing rates, which in a rising interest rate environment has pushed several into debt distress.



At this critical juncture of heightened global volatility and geopolitical uncertainty, striking the correct balance between curbing inflationary pressures and buttressing growth is crucial.

61 For more details, see <https://www.imf.org/en/Publications/REO/SSA/Issues/2022/10/14/regional-economic-outlook-for-sub-saharan-africa-october-2022#:~:text=Living%20on%20the%20Edge&text=But%20growth%20in%202022%20is,an%20ongoing%20series%20of%20shocks>



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This assessment of Africa's growth prospects has been prepared by Hippolyte Fofack, Chief at the African Export-Import Bank (Afreximbank).

The document provides analyses of the Research Department and does not purport to reflect the views of Afreximbank.

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ISBN: 978-92-95097-31-5