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Quarterly Report

NKC AFRICAN ECONOMICS
AN OXFORD ECONOMICS COMPANY

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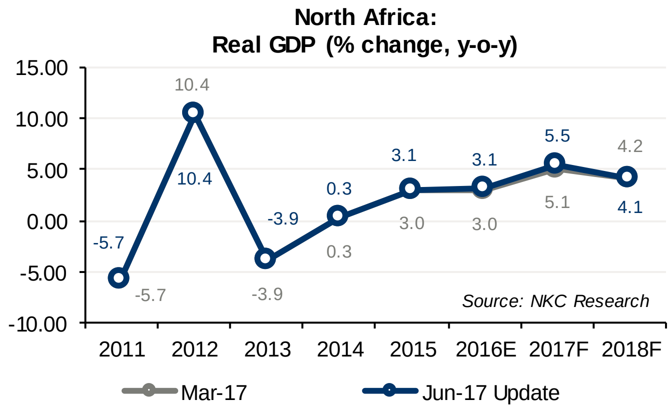
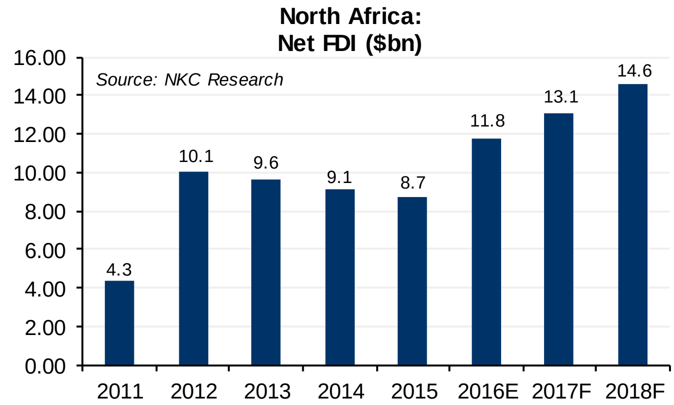
NKC Coverage

CONTENTS

NORTH AFRICA



Countries included: Algeria, Egypt, Libya, Morocco, Tunisia



Countries included: Algeria, Egypt, Libya, Morocco, Tunisia

OVERVIEW

Political risk in North Africa remains elevated and is likely to stay so as **Libya** appears little closer to establishing a centralised authority with broad legitimacy to govern. The other country which makes North Africa the riskiest region on the continent is **Sudan**, where a new government was formed after a dubious 'national dialogue' came into effect over the past quarter. Relative calm in the country due to the ceasefire with rebels has given the government hope that the US will finally lift economic sanctions, but tensions persist. Meanwhile, regional heavyweight **Egypt** has seen a number of terrorist attacks targeting its Coptic Christian minority and the government has put in place a state of emergency. The government is ever more repressive, with the media, opposition politicians and civil society coming under attack over the past quarter. The region's calmer countries – **Tunisia, Algeria and Morocco** – have not been without their own ructions over the quarter, but present markedly lower political risk.

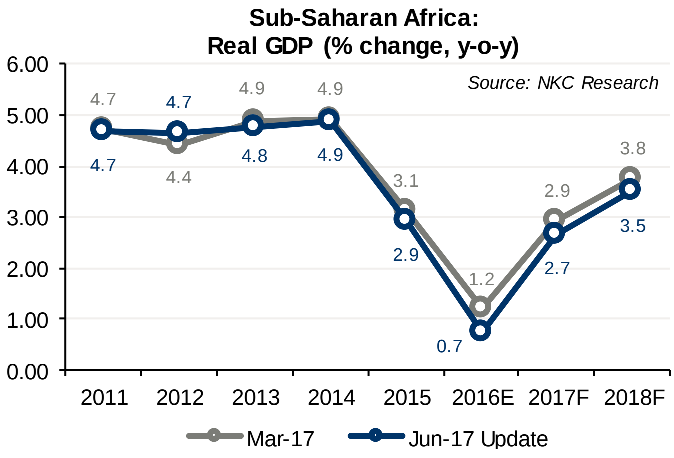
KEY ISSUES AT PRESENT

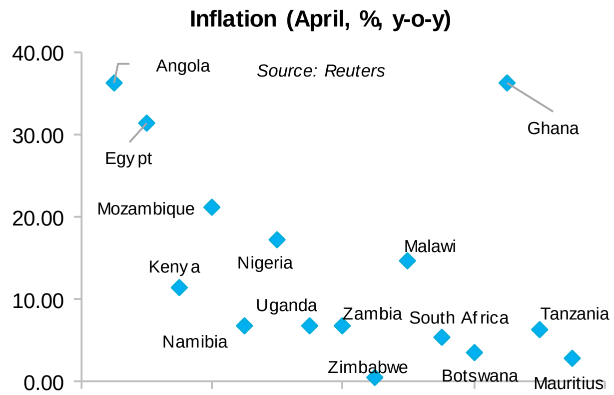
- **Egypt** – In May, the International Monetary Fund (IMF) released the second disbursal of the $12bn loan following a positive review of the reform progress. The approval of the investment and licensing laws will aid the country's economic recovery through increasing investment, exports and industrial production. However, Egypt is expected to be constrained by inefficient bureaucratic hurdles, stringent regulatory requirements and high unemployment. Furthermore, despite the easing of core inflation over the past two months, the annual rate is still significantly high at 32.1% y-o-y in April, resulting in a 200 bps interest rate increase in May. High inflation and rising borrowing costs are expected to dampen private sector investment and activity further, but will attract portfolio investments and satisfy multilateral organisations.
- **Morocco** – The current account deficit widened significantly further than expected in 2016 due to a surge in capital and food imports, which offset a lower energy import bill and an increase in tourism revenues, remittances and exports. A similar trend is expected this year, while rising international oil prices are expected to push up the import bill further. The insurance provided by the IMF's Precautionary Liquidity Line will however support the country's external and fiscal position and presents a lower risk associated with financing difficulties.
- **Tunisia** – The IMF approved the second loan disbursal in April 2017 of the Extended Fund Facility programme, following a three-month delay. The Fund indicated that it continues to support Tunisia's reform programme, but that urgent action is needed to address the health of public finances and to speed up the reform process. Unlike Egypt, Tunisia struggled to contain wage spending and raise tax revenues, resulting in fiscal slippages over the past year.

FORECAST

Economic growth in the North Africa region is forecast to pick up from 3.1% in 2016 to 5.5% in 2017. Regional growth prospects are partially supported by an expected recovery in Morocco and Tunisia on the back of a rebound in agricultural production. Morocco's manufacturing sector is forecast to pick up pace this year as the country is favoured by international investors due to positive reforms and relatively stable macroeconomic and political dynamics. In contrast, Tunisia's economic growth prospects are constrained by slow reform progress, labour union opposition and rising inflation. In Egypt, double digit inflation and high interest rates remain a burden on the private sector over the short term, but the positive impact of reforms is anticipated to boost medium-term economic growth prospects, supporting the region's economic outlook. The expected rise in international oil prices from 2017 onwards will have an asymmetric impact on the North African region, benefiting oil exporters (Libya and Algeria), while weighing on oil importers (Egypt, Tunisia and Morocco). Nevertheless, despite the expected rise, oil prices are predicted to remain low over the forecast horizon, which will heighten the need for further diversification and reform implementation of oil-based economies.

SUB-SAHARAN AFRICA (SSA)





OVERVIEW

Generalising about political risk trends in the region remains as difficult as ever, but the past quarter has seen more negative news than positive. Over the long term, we remain optimistic about the prospects for democratisation and the building of effective institutions of governance. These institutions will be vital in allowing the region to benefit off of its expected demographic dividend. However, a booming population obviously presents as many dangers as opportunities, countries will struggle with the common challenges of high youth unemployment, growing inequality and strains put on urban areas as people migrate to cities in search of improved livelihoods.

KEY ISSUES AT PRESENT

Over the past quarter risks to macroeconomic stability have largely been clustered around **domestic** factors, **political** developments and **weather** shocks. The Famine Early Warning Systems Network (FEWS NET) estimates that, due to the prolonged drought, the regional maize deficit reached just over five million tonnes. While the cumulative moisture deficit in the southern part of the continent has reduced considerably in the wake of favourable late rains, harvest prospects in the eastern region remain poor as pest infestation amplify the negative impact of a below-average rainfall season. Specifically, FEWS NET warned that the southern parts of South Sudan, Uganda, Kenya, Ethiopia, Somalia and northern Tanzania continue to suffer from drought-like conditions. Late season rains have been poorly distributed in time and space in Kenya, which led to localised flooding damage – the destruction of infrastructure and recent plantings, displacement of households, and loss of livestock – while other counties in pastoral areas continue to suffer from a moisture deficit. As a result, while food price pressures are forecast to ease in southern Africa in H2 on the back of bumper harvests in South Africa and Zambia, poor harvest prospects in parts of East Africa will limit any seasonal declines in staple foodstuff prices, weighing on headline consumer price growth as well as the fiscal and current account positions. With regard to the latter, Kenya introduced a subsidy on maize flour in May, although quantities of subsidised goods have been restricted. The cost of a two-kilogramme pack of maize flour decreased to KSh90, from KSh150 previously. The maize flour subsidy is expected to stay in place until the end of July – elections are scheduled for August 8. Across the region, staple food prices may remain well-above the five-year average, although countries with surplus stock will see prices decline below previous season levels.

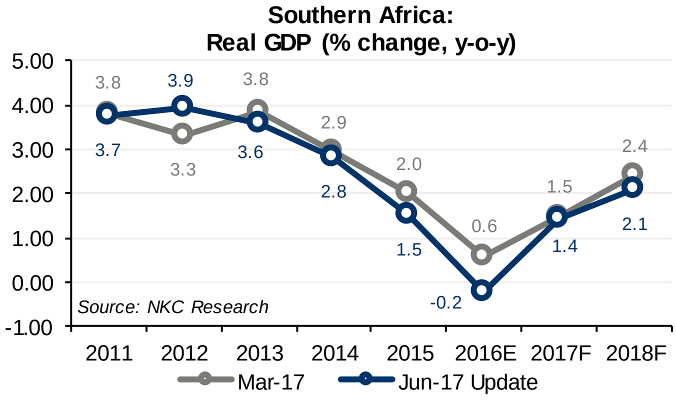
Political developments continue to dominate the risk profile in South Africa – a cabinet reshuffle at the end of March, which triggered downgrades of South Africa's ratings to sub-investment grade by S&P Global Ratings and Fitch Ratings, is likely to undermine governance of state-owned enterprises (SOEs), weaken fiscal consolidation and reduce private sector investment as a result of weaker business confidence. Factionalism within the ruling African National Congress (ANC) has become starker, and the narrative around 'State capture' louder; while this is a good sign, it also presents the risk that the corrupt will, in desperation, speed up their efforts to loot what they can. Any clear indication of this, or evidence in recent leaks that past corruption is more serious than had been realised, will tend to serve as justification for further negative ratings actions. Also, severe tensions within the ANC undermine policy predictability as it is unclear which factions will prevail on individual policy issues. Namibia, which has suffered from a cyclical downturn due to commodity price weakness rather than a perceived deterioration in institutions and governance such as its southern neighbour, nonetheless remains highly vulnerable to negative developments in South Africa due to the Common Monetary Area (CMA) agreement. In turn, Lesotho turned to the polls for the third time in five years on June 3, in a fresh attempt to bring some political stability to the troubled mountain kingdom.

Notable legislative elections in Q3 include Senegal (July 2), Gabon (July 29), Congo Republic and Kenya. Rwanda (4th), Kenya (8th) and Angola (23rd) all host presidential elections in August; while no serious unrest is expected in Angola and Rwanda, some violence is possible in Kenya if the process is not perceived to be credible. While it remains too early to be confident of the result, our forecasts suggest that the incumbent, Mr Uhuru Kenyatta, will be able to win the election with a comfortable margin – which would decrease the risk of post-election conflict due to a challenge to results.

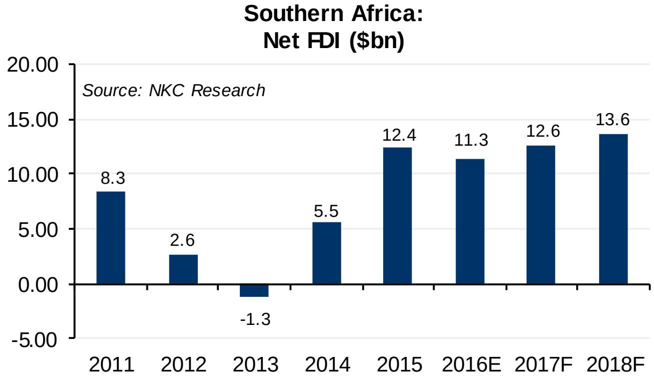
FORECAST

The SSA economy is forecast to expand by 2.7% this year, emerging from an estimated trough of 0.7% in 2016, as regional agricultural sector performance improves and the unwinding of tight monetary policy supports modest growth in private sector consumption and services. However, downward revisions in the growth trajectories of regional giants **South Africa** and **Nigeria** from our March forecast round have contributed to the shaving off of 0.2 percentage points from the regional growth forecast for 2017.

SOUTHERN AFRICA



Countries included: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Zambia, Zimbabwe



Countries included: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Zambia, Zimbabwe

OVERVIEW

Southern Africa remains the continent's safest bet from a regional political risk perspective, with two of the most stable countries on the continent – Mauritius and Botswana – located there. **Namibia**, too, presents relatively low risk on the political front despite recent populist rhetoric related to land reform. The region, however, also has its riskier members, and political dynamics in **Zimbabwe** – with elections around the corner – **Zambia** – with an opposition leader on trial for treason – and **Lesotho** – where a new coalition government is likely to be as shaky as the last – need to be watched closely for deterioration. **Angola** shows low overall risk but is going through an uncertain time, with an upcoming election and the prospect of the end of President Jose Eduardo dos Santos's almost 40-year reign. **South Africa**, having long discarded its reputation as a model of good governance in the region, continues to lurch from one political crisis to another, and tensions may yet rise as its ruling party heads towards its elective conference at the end of the year. Those looking for good news will have to settle for **Mozambique**, where the rebel-cum-opposition movement Mozambican National Resistance (Renamo) announced over the past quarter that it is extending its truce with the ruling party indefinitely.

KEY ISSUES AT PRESENT

- **South Africa –** The regional powerhouse had some reprieve as Fitch Ratings affirmed the country's long-term foreign- and local currency at "BB+" with a stable outlook on June 1. This after the ratings agency downgraded the country from "BBB-" to "BB+" (with a stable outlook) on April 7. The move by Fitch came after S&P Global Ratings decided to cut South Africa's long-term foreign currency rating from "BBB-" to "BB+" (with a negative outlook) on April 3. Most recently, on June 2, S&P affirmed its long-term foreign and local currency sovereign ratings on South Africa, retaining its negative outlooks. The agency remains concerned about the country's low growth expectations – which pose a risk for fiscal consolidation – and rising contingent liabilities, as well as elevated political risk. On a separate note, the local unemployment rate has risen to 27.7% in Q1, which is the highest since January 2008.
- **Angola –** The Instituto Nacional de Estatistica (INE) estimates that real GDP contracted by 4.7% y-o-y over the 2016 Q1 - Q3 period. This suggests that the economy fared much worse than we originally anticipated last year. We have downgraded our real GDP growth estimate following the release of the INE's figures.

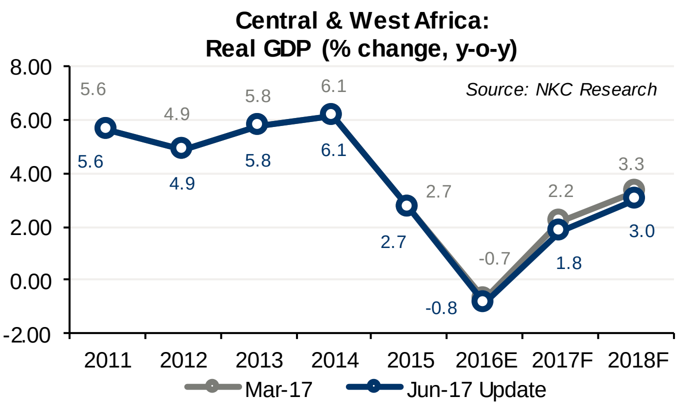
However, we see a high likelihood that the INE's figures may be revised as its assessment may very well be overly pessimistic. We estimate real GDP contracted by 3.8% in 2016.

- **Mozambique –** The Mozambican Attorney General's office finally received the independent audit report from forensic audit firm Kroll on May 12. The Mozambican government will likely present a debt resolution proposal once the findings of the audit is published. The IMF demanded the independent audit as a condition for resuming normal relations with Mozambique.
- **Bumper harvesting season –** On a positive note, in our previous publication we reported that the outbreak of the fall armyworm would cause serious damage in the region. However, crop estimates for the season suggest that a bumper harvesting season is expected in most parts of the region after widespread rains. In fact, some areas expect double and others more than double the crop it had last year.

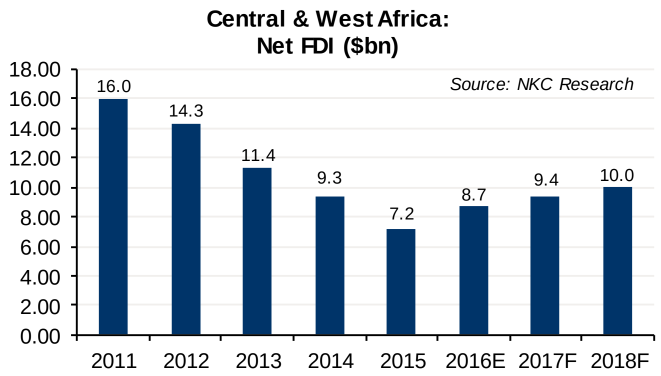
FORECAST

Due to the downward adjustment to Angola's GDP growth for 2016, it is now estimated that regional growth has contracted by 0.2% in 2016, from a previous estimation of 0.6% growth in March. Major role players South Africa and Angola are still struggling to gain any traction as a result of the slump in commodity prices. Angola is expected to bounce back slightly this year and grow by 1.6%. Unlike previously thought, oil production now looks set to decline slightly this year as Angola adheres to production cuts agreed upon by OPEC members and certain non-member countries. South Africa's GDP growth is forecast at 0.9% (1.2% in March) in 2017. Growth in South Africa will be driven by a better performance in the agricultural sector and a recovery in the mining sector. However, we also adjusted South Africa's GDP growth rates for 2018 and 2019 downwards. Countries such as Botswana (4.1% growth forecast for 2017), Namibia (3.1%), Lesotho (2.3%), and Zambia (3.3%) are set to receive a welcoming boost from mining production. Although facing a host of economic headwinds, Mozambique's growth is forecast at 4% for 2017 due to an increase in aluminium and coal prices. Zimbabwe's economy is forecast to contract by 0.3% this year as economic issues intensify. Regional growth is forecast at 1.4% for this year.

CENTRAL AND WEST AFRICA



Countries included: Cape Verde, DRC, Ghana, Guinea, Liberia, Mauritania, Nigeria, SaoTome & Principe, Sierra Leone, The Gambia



Countries included: Cape Verde, DRC, Ghana, Guinea, Liberia, Mauritania, Nigeria, Sao Tome & Principe, Sierra Leone, The Gambia

OVERVIEW

Ghana remains the region's least risky country given its recent record of peaceful changes in government through fair elections. Politics in the country appears to be normalising, despite reports of protests in some areas against the new government, and President Nana Akufo-Addo has been attempting to deliver on his considerable campaign promises. **Nigeria** has largely been without a president over the past quarter as President Muhammadu Buhari has been sick. His capable vice president, Yemi Osinbajo, has taken the reins and managed to keep the government functioning, but tensions within the ruling party are rising as ambitious members begin jockeying for position believing Mr Buhari will not complete his term, let alone run for re-election. The region's political risk average is dragged up by the **DRC** and it does not appear that matters will improve any time soon. Horror stories of large casualties in conflicts in Kasai province and simmering conflicts in the east speak of a country on the brink.

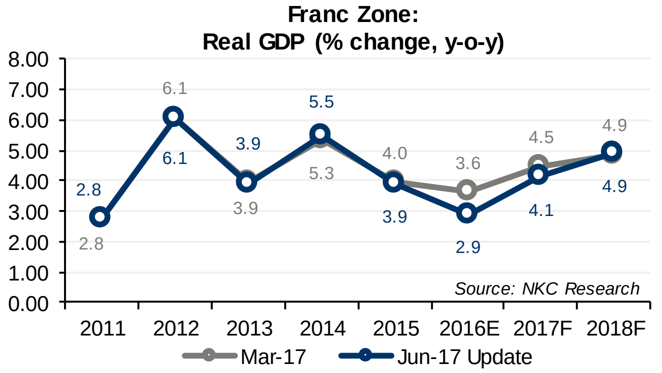
FORECAST

We estimate the regional economy would have contracted by 0.8% in 2016. This is mainly due to the poor performance of the Nigerian economy, ascribed to severe forex shortages, a delay in the ramp up in fiscal spending and Delta security threats curtailing oil production – it is worth noting that Nigeria's nominal GDP accounts for more than 80% of the regional total. Looking ahead, we have lowered our forecast for regional economic growth to 1.8% in 2017, mainly ascribed to the Nigerian economy's weaker-than-anticipated performance in 2017 Q1. Regardless, growth prospects in general continue to look encouraging, with all but two countries in the region expected to record higher real GDP growth in 2017. Ghana is expected to be the stand-out performer, with an increase in oil production and strengthening consumer demand seen lifting real GDP growth to 6.2% in 2017. Nigeria meanwhile looks set to remain a drag on regional economic growth over the next two years as the country struggles to come to grips with structurally lower crude oil prices.

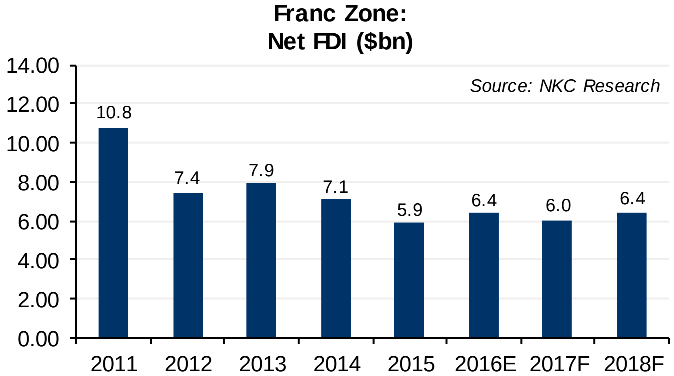
KEY ISSUES AT PRESENT

- **DRC –** The slump in commodity prices prompted certain mining companies to scale back operations and delay investment projects, which dragged real GDP growth down to an estimated 2.8% in 2016. Looking ahead, a rebound in commodity prices should incentivise a ramp up in mining output this year. An anticipated increase in fiscal spending also bodes well for the economy in general. We forecast real GDP growth will increase to 4.1% in 2017.
- **Ghana –** The economy looks set for a sharp rebound this year. While oil proved to be the main culprit last year, the commodity will likely be a key growth driver in 2017 as output from the new Tweneboa-Enyenra-Ntomme (TEN) project is ramped up – production at ENI's Sankofa development starting ahead of schedule provides further upside potential in this regard. Besides higher oil output, improved government technical assistance bodes well for agriculture. Furthermore, the demand side of the economy will benefit from lower inflation and interest rates. We project real GDP growth will increase to 6.2% in 2017.
- **Nigeria –** The Nigerian economy was slow out of the blocks this year, with real GDP contracting by 0.5% y-o-y in 2017 Q1. However, we expect the economy to gain more traction as the year progresses. While oil output remained depressed at the start of the year due to ongoing repair work, production should ramp up gradually moving forward. Furthermore, forex liquidity conditions were very tight at the start of the year, but have since eased in line with the central bank stepping up its foreign exchange interventions. Furthermore, increased fiscal expenditure should start to boost economic activity from H2 onwards. Nonetheless, we have lowered our real GDP growth forecast to 1.1% in 2017 due to the sluggish start to the year.

FRANC ZONE



Countries included: Benin, Burkina Faso, Cameroon, CAR, Chad, Congo, Ivory Coast, Equatorial Guinea, Gabon, Guinea-Bissau, Mali, Niger, Senegal, Togo



Countries included: Benin, Burkina Faso, Cameroon, Central African Republic, Chad, Equatorial Guinea, Gabon, Guinea-Bissau, Ivory Coast, Mali, Niger, Senegal, Togo

OVERVIEW

Ivory Coast saw further unrest over the past quarter as mutinying soldiers once again took to the streets in a number of towns demanding bonuses they were promised. While they got their way and stability has been restored, we interpret the events as a signal of broader discontent and have increased our political risk rating for the country to 'Moderate' from 'Low tending moderate'. Political tensions in Cameroon have eased somewhat after protests and government repression in Anglophone regions rocked those parts of the country earlier in the year. However, with no clear resolution to the protestors' demands, the potential remains for a resurgence in unrest over the short to medium term. Gabon, too, has seen a normalising in its political environment over the past quarter, but here, as in Ivory Coast and Cameroon, the potential for renewed unrest remains. Senegal once again represents the least risky alternative in the region, and while the country is not without its political difficulties and intrigues, they tend to highlight its inherent strengths and the healthy contestations of a consolidating democracy.

The low energy price environment continues to resonate negatively on the macroeconomic situation in the franc zone. The most affected countries are those belonging to the Central African Economic and Monetary Community (Cemac) – as five out of the six countries are net oil exporters. As such, both **Cameroon** and **Gabon** have initiated negotiations with the International Monetary Fund (IMF) to implement collaborative economic programmes which would allow these countries to attain higher and sustained levels of long-term economic growth. Not only will an IMF-supported economic programme provide some short-term fiscal and external relief, it will also help to anchor much needed structural reforms. Turning to Francophone West Africa, macroeconomic prospects are somewhat brighter in the West African Economic and Monetary Union (WAEMU). That said, economic prospects in high-flying **Ivory Coast** have come under pressure of late, as a result of a slump in the price of cocoa, the country's primary export and fiscal revenue generating commodity. Challenges in Ivory Cost have been further compounded by the government agreeing to pay bonuses to mutinous soldiers. **Senegal**, on the other hand, is set to record robust growth on the back of increased agricultural production, infrastructure investment and the implementation of economic reforms backing the Emerging Senegal Plan (PSE).

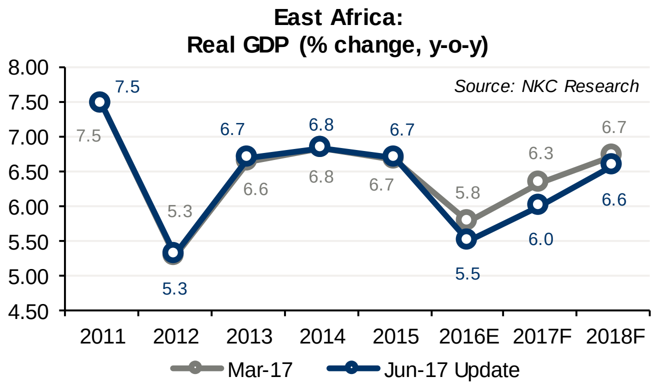
KEY ISSUES AT PRESENT

- **Senegal** – Senegal's government recently launched a 16-year $1.1bn Eurobond, intended primarily to finance infrastructure projects.
- **Ivory Coast** – Government recently revised its 2017 fiscal budget lower due to new budget constraints imposed by lower fiscal revenues generated from cocoa, as well as agreeing to pay bonuses to mutinous soldiers.
- **Gabon** – The near-term priority for government will be to clear the large amount of arrears it has accumulated. The government is currently pursuing fiscal consolidation measures, with the budgeted fiscal expenditure for 2017 being lower than last year.
- **Cameroon** – The past quarter has been unusually volatile in Cameroon because of unrest in the English-speaking region, and the reaction of President Paul Biya's government to the unrest.

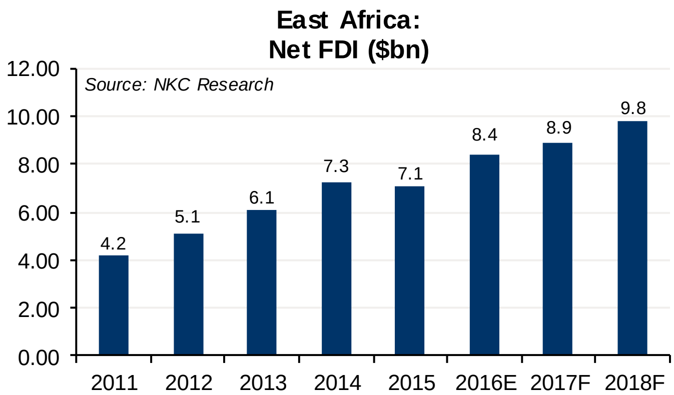
FORECAST

We estimate that the regional economy grew at a rate of 2.9% last year. Overall regional economic growth was negatively impacted by economic contractions in oil producing nations, including: Equatorial Guinea (-10%), Chad (-6.4%) and the Republic of the Congo (-2.7%). The scenario was particularly dire for Equatorial Guinea, which is the most oil-dependent economy in the franc zone – around 60% of GDP stems from hydrocarbons. Ivory Coast and Senegal recorded the strongest economic growth rates in 2016, with respective estimates of 7.5% and 6.5%. Looking ahead, we expect regional economic growth to increase to 4.1% this year on the back of strong infrastructure investment-driven economic expansions in Ivory Coast and Senegal, and a recovery in international oil prices increasing growth rates in the oil producing countries. Turning to foreign direct investment (FDI), we expect foreign interest in the region to dip slightly this year, due primarily to a reduction in foreign oil investments. Overall, we expect that net FDI inflows will fall to $6bn this year from an estimated $6.4bn in 2016.

EAST AFRICA



Countries included: Burundi, Comoros, Djibouti, Eritrea, Ethiopia, Kenya, Madagascar, Rwanda, Seychelles, Somalia, Tanzania, Uganda



Countries included: Burundi, Comoros, Djibouti, Ethiopia, Kenya, Madagascar, Rwanda, Seychelles, Tanzania, Uganda

OVERVIEW

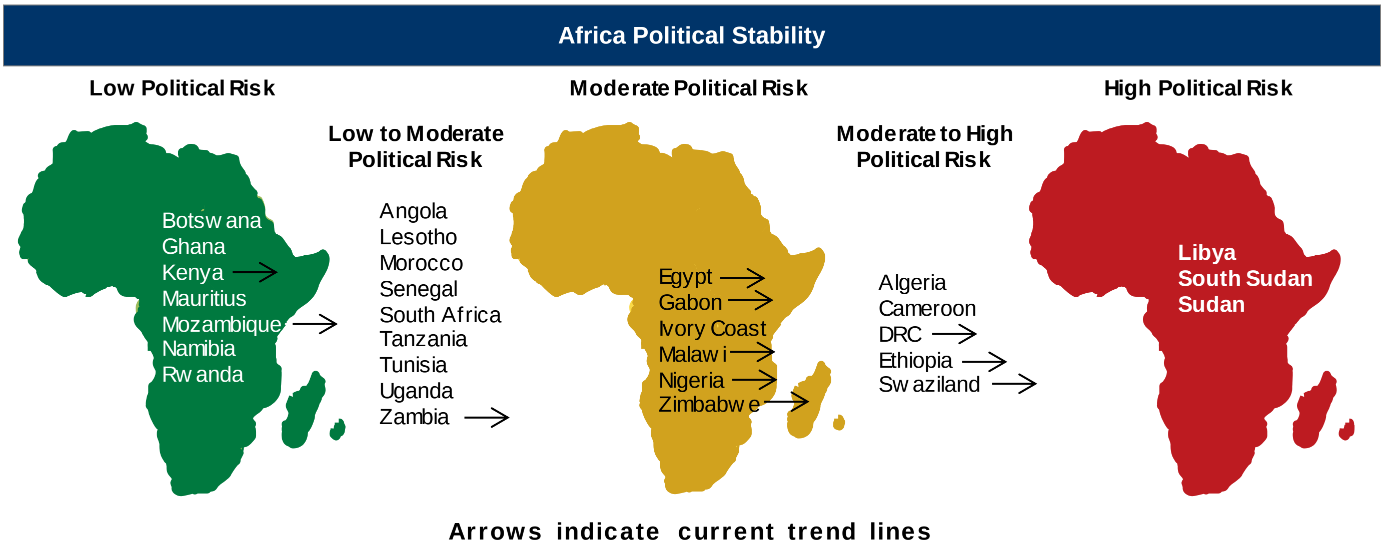
If it were not for the inclusion of **South Sudan** and **Ethiopia** in our categorisation for East Africa, the region would be our least risky on the continent politically. Indeed, it is difficult to imagine a riskier political environment than that of South Sudan at present, which is effectively a failed State on the brink of famine and all-out ethnic cleansing. Ethiopia, meanwhile, has seen order return thanks to its state of emergency which was renewed in March for an extra four months. Political stability over the medium to long term, however, will require real reforms that the current regime looks unlikely to implement. The other countries in the region represent markedly lower political risk. **Kenya's** elections in August are likely to see an uptick in violence, but we do not believe it will be much worse than that experienced in 2013 and far lower than the post-election violence of 2007/08. **Rwanda** is gearing up for elections in the same month, but President Paul Kagame will no doubt use his usual repressive measures to keep a lid on any real challenge, and violence and instability will be kept to a minimum. **Tanzania**, meanwhile, continues to see its president's mission to reform and clean up the country's public sphere playout. While fighting corruption and minimising government wastage are laudable ends, his means of achieving them are far from ideal and do not bode well for the consolidation of democracy. Lastly, **Uganda** represents just where centralising decision-making and repressing the opposition can get you. While relatively stable, little progress has been made at improving institutions of governance. Furthermore, the East Africa region is emerging from the adverse economic effects of a severe drought that plagued the east of the continent in 2016 and earlier this year. All the large economies in the region (except Kenya) saw a marked slowdown in growth last year, driven by poor performances in agriculture which then spilled over into other spheres of the economy. Most countries in the region also saw a notable slowdown in private sector credit extension during the latter part of the year, which has encouraged authorities in Rwanda, Tanzania and Uganda to step up monetary stimulus this year.

KEY ISSUES AT PRESENT

- **Ethiopia** – The government has extended the six-month state of emergency, in place since October 2016, by an additional four months, with authorities stating that there are still *"some people who occasionally strive to disrupt peace and security*".
- **Kenya** – Rocketing food prices have encouraged to government to subsidise maize flour and remove import duties on other foodstuffs, thus halting opposition momentum on the issue of the rising cost of living.
- **Rwanda** – Diane Rwigara, a 35-year-old accountant and outspoken critic of President Paul Kagame's authoritarian rule has announced that she would run as an independent candidate in the August elections.
- **South Sudan** – President Salva Kiir has declared a unilateral ceasefire and vowed to release political prisoners as the initial steps in facilitating an inclusive peace process or 'National Dialogue'.

FORECAST

While East Africa is expected to see an improvement in regional growth this year, we have still adjusted our forecasts to reflect the more-severe effects of the drought in 2016, and the impact that this has had on overall growth momentum this year. In addition, the available data suggests that Kenya's regulatory caps on interest rates are having a pronounced effect on private sector credit extension, which has necessitated a downward revision in the growth forecast for the region's largest economy. Still, regional growth is expected to increase from 5.5% in 2016 to 6.0% this year, driven by stronger growth in most of the region's large economies. The improvement in growth prospects will be reflected in upward trending FDI, with most of the larger economies in the region seeing an uptick in foreign interest over the medium term.



The democratic status of a country is an insufficient indicator of that country's political risk profile. Subject to the value-belief system of the local populace (do they recognise the claims of kings and sultans to govern); a functioning democratic system is a necessary condition for political stability, but not a sufficient one. Democracy and stability do not necessarily equate nor can we assess business opportunities based on a country's democratic status. It is possible to do business with any country, irrespective of the political risk profile subject to other variables and the understanding that in a high-risk country any political action is possible while in lower risk environments the actions of the political system are predictable.