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Considerations on the economic impact of the coronavirus pandemic on Africa

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The coronavirus crisis poses major challenges for Africa. Not only are export markets collapsing in the wake of the demand shock. The supply of necessary imported goods is also under threat from temporary production shutdowns and rising protectionism (supply shock). The measures introduced to contain the pandemic, such as border and business closures, stay-at-home orders and social distancing are a special challenge for Africa as some 90% of retail transactions are local and informal. The measures that were adopted in many places have derailed the continent's economic dynamism. This has hit Africa hard because it requires high growth rates to manage the dynamic demographic trend. The current developments could therefore massively exacerbate the social challenges and poverty in Africa.

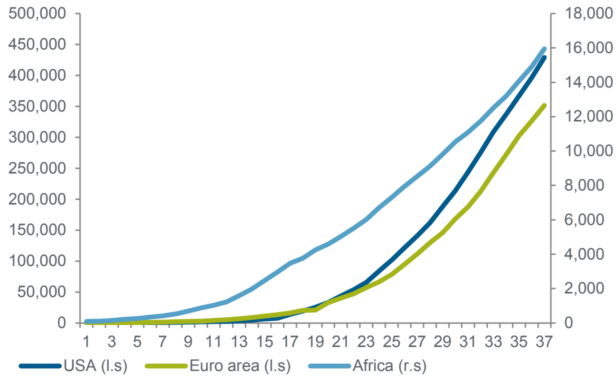
The current situation in Africa

The number of infections in Africa is rising (Figure 1). Last week the number of people who have fallen ill with Covid-19 increased by 50%, while deaths from the disease rose by 60%. Despite this growth rate it has to be said that the pandemic is generally evolving on a lower level than in Europe and the US. Many African countries have adopted strict measures for fear that the situation could take a similar path as in China, Europe or the US. These measures include border closures, entry bans for certain at-risk groups, restrictions of gatherings, school closures and even stay-at-home orders. These proactive measures are also aimed at preventing further strain on the already scarce capacities of the health system. According to the World Health Organization, they are already beginning to have an effect[1].

According to the Africa Centers for Desease Control and Prevention (CDC), it is still unclear how the virus outbreak will evolve in Africa. But experience from other countries shows that the virus primarily affects the working-age population, as the average age of confirmed cases is 44.9 years. The elderly and people with pre-existing medical conditions are most at risk. Africa's population is young, averaging 19.7 years of age but many people have underlying health conditions, including malnutrition and other diseases such as HIV/AIDS and tuberculosis. Algeria, Egypt, Morocco and South Africa are currently reporting the highest case numbers. Infections are currently rising at the fastest rates in Côte d'Ivoire and Ghana. The low case numbers in other countries are sure to reflect inadequate testing capacity, although 44 countries now have the necessary equipment.

Figure 1: Case numbers in Africa, Europe and the US

Case numbers by days since the 100th case



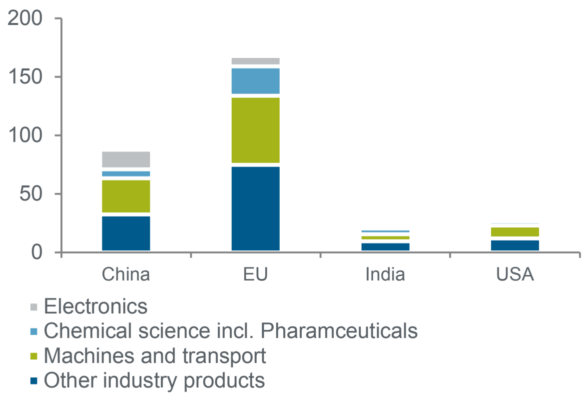
Sources: Johns Hopkins, Africa CDC, own rendition, as at 16 April 2020

The consequences of the supply shock: shortages of critical goods and medical equipment

At the beginning of the year, as production came to a halt in China and goods were no longer loaded onto ships in Chinese seaports, countries experienced the first shortages of consumer goods imports, especially electronics, machines and textiles. The port of Mombasa, a trading hub between (East) Africa and China, reported a drop of ship traffic of around one fourth in March.

Figure 2: Total African imports by trading partner and group of goods

In USD billion, 2018



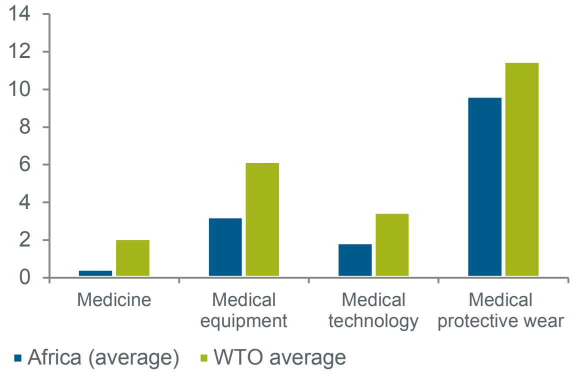
Source: UNCTAD, own rendition

While China's production and exports are slowly recovering, Europe, the US and India are now experiencing disruptions to their production and export logistics. Most imported machines, vehicles and pharmaceutical products originate in the countries currently affected (Figure 2). The shortage of goods could therefore worsen in the months ahead and affect other groups of goods as well. With the outbreak of the coronavirus pandemic, India restricted exports of medicines and pharmaceutical ingredients, for example. But the crisis may also lead to food shortages. Only 15 African economies are net food exporters.[2] Inflation will probably rise as a result of diminishing availability of goods and products. Nigeria has already reported that the price of rice has risen by 30% in the world market as a result of shortages.

The price increases caused by the supply shock mainly affect the poor population. In order to reduce inflationary pressure, African states could reduce import tariffs on the most important goods and products such as food, medical equipment and technology, although average import tariffs for medical equipment are already below the WTO average (Figure 3). Because tax revenue is generally low in Africa, import tariffs constitute an important source of public revenue – on average around 20% of tax revenue. In general, the weaker a country's economic basis is, the higher the share of import tariffs in total state revenue. A reduction in import tariffs would then go at the expense of the already strained public budgets.

Figure 3: Average import tariffs on medicines and medical equipment

In per cent



Source: WTO, own calculations

While industrialised countries are attempting to fill shortages in the world market by retooling production lines, many African countries do not have the industrial basis to do this. On average, manufacturing accounts for only 11% of total value added. Accordingly, only few African countries possess a major pharmaceutical industry, among them Kenya, Nigeria, Tunisia and South Africa. It is doubtful that the companies located there have the necessary capabilities and inputs required to bridge the gaps in the supply of pharmaceutical products or medical technology. Another question is which manufacturing firms would be able to support the supply of the economy, and the health sector in particular, with critical equipment such as facemasks or gowns.

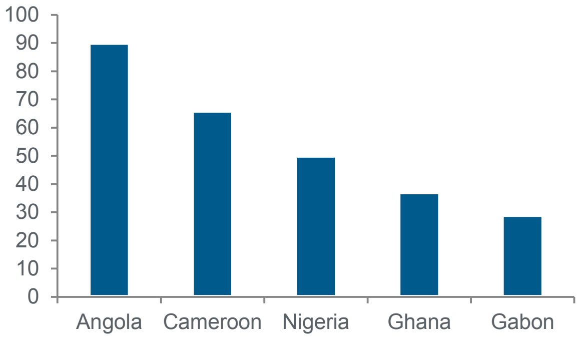
The demand shock: oil producers and commodities exports at the centre of a global economic crisis

The global economic downturn is reducing demand for inputs from Africa, especially crude oil and copper. The tourism sector is suffering as well. Oil producers are also affected by falling oil prices in the wake of the trade dispute within OPEC+ (Figure 4). Angola is particularly affected because of its low diversification. In the combination of falling demand and excess supply, the average price of Brent crude oil is predicted to settle at USD 29 per barrel this year.[3] That puts the average oil price well below production cost and the price assumed for budgetary planning and it will increase oil producers' need for public finance. Whether the cuts in oil output announced over the Easter holidays will change the general situation in any way remains doubtful. Demand for oil continues to fall as a result of the deepening global recession, while global oil storage facilities are filled as a result of weeks of overproduction. The oversupply situation in the oil market could thus continue for several more months and dampen the development of the oil price.

At the same time, the rising price of gold is easing pressure on African economies, particularly Ghana (share of gold in total exports approximately 35%) and South Africa (around 4%).

Figure 4: Crude oil exports as a share of total exports

In per cent, 2018



Sources: WTO, Trade Map, own calculations

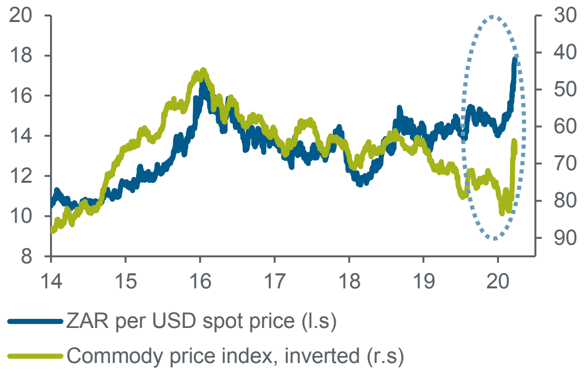
South Africa in particular is in the spotlight because of its very close integration into international commodities and capital markets. This is reflected in the exchange rate variations of the South African rand. The currency has devalued by around 26% since the start of the year (Figure 5). In addition to the many problems which the country was facing even before the outbreak of the coronavirus crisis, the economic and financial situation is now worsening substantially. The major rating agencies' recent downgrading of the country is an expression of this very difficult situation and of the doubts about a rapid economic recovery.

Social distancing is weakening the economic basis even more

As a result of the upcoming global recession and the effects of the crisis described above, Africa's economic growth will slow this year. The UN Economic Commission for Africa (UNECA) has downgraded its growth forecast for 2020. It predicts that Africa, too, will slip into recession.[4] The main reason for the downward revision is the deepening global crisis and the resulting loss of export markets, particularly for commodities. However, exporters of industrial goods such as textiles and automobile parts are also suffering from the coronavirus-induced demand shock. The World Bank also expects a recession in Africa this year.[5] The intra-African containment measures could act as a further dampener to growth (Figure 6). The measures introduced in Algeria, Angola, Egypt, Kenya and South Africa are particularly drastic. These countries are the continent's economic heavyweights, together generating some 50% of Africa's GDP.

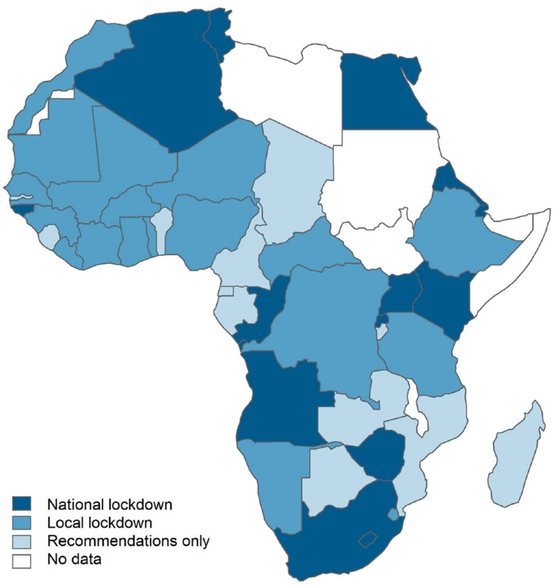
Figure 5: US dollar / South African rand and price index of South Africa's commodities exports

Index value, in USD billion



Source: Eikon, own calculations

Figure 6: Overview of lockdown measures in Africa



Source: BBC 2020 'Coronavirus: The world in lockdown in maps and charts', own rendition

Social distancing measures, such as business and border closures as well as stay-at-home orders, are making it impossible for many companies to do business. The service sector, which makes up some 60% of African GDP, has been hit hardest by these measures. Although many African countries are already substantially more advanced in the use of mobile or app-based payments than Latin America, for example, online trading is still not very widespread. In 2018 it accounted for just 1.9% of all retail turnover in South Africa. According to estimates, more than 90% of all retail turnover in Africa is generated by local and informal businesses.[6] Many entrepreneurs, both male and female (some 30% of businesses are owned by women)[7] have had to stop trading because of the containment measures. This has further weakened the economic basis of many African countries and slowed their economic growth.

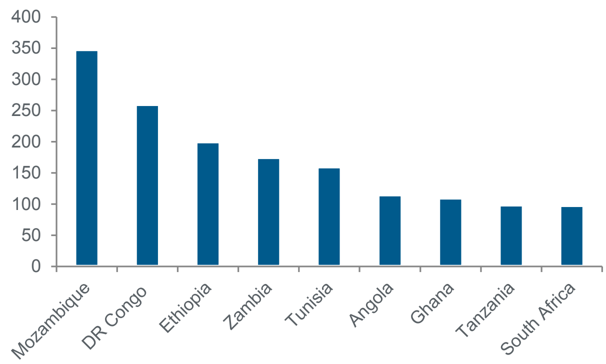
At the same time, Africa's population is growing by approximately 2.8% each year. It requires an adequate rate of growth in order to meet the needs of a growing and young population.

Fiscal scope is limited

Most African countries do not have the financial resources to mitigate the economic impact of the crisis and finance the rising costs of the healthcare system. Africa's average debt is currently approximately 59% of GDP. According to the IMF, however, African countries currently service their debt with around 30% of their export revenue, which they will lose for the time being in the ongoing crisis. Since many African states have taken advantage of the global low-interest environment to borrow in euros or US dollars, the financing situation is exacerbated when the local currency loses value. In the course of the 'Super Commodity Cycle' which ended in 2014, currency reserves have also declined as a result of falling export earnings. This downward trend is now continuing. Gross external financing requirements now exceed many countries' foreign exchange reserves (Figure 7).

Figure 7: Gross external financing requirements

In percentage of foreign exchange reserves. 2019



Source: Capital Economics, own rendition

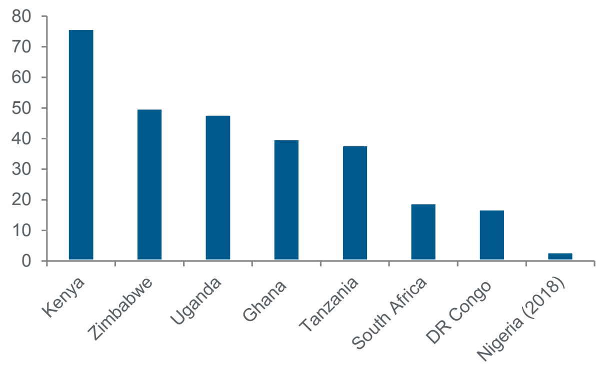
Many African states are in contact with the International Monetary Fund and the World Bank in a bid to meet increased financing requirements caused by the coronavirus crisis. The IMF had already responded and cancelled debt to the sum of around USD 210 million for 19 African states. Among them are the two states with the highest gross borrowing requirements: Mozambique and the Democratic Republic of the Congo. Further measures in the framework of the G7 and G20 are currently being discussed. Debt relief or deferment of payments would give many African countries necessary financial scope for investing in health care and mitigating economic impacts.

Despite the tense financial situation, a few African states, including Egypt, Nigeria and South Africa, have already adopted fiscal packages to cushion the economic impact. With the exception of Egypt, however, where the fiscal package is around 3% of GDP, the volume of the Africa-wide measures is relatively small. According to IMF information, the packages have an average volume of 0.3% of GDP.

Another major challenge consists in designing the fiscal packages in such a way that they actually reach the people and businesses that need them. Given the high share of the informal economy, that is not an easy task. Estimates show that approximately 60% of businesses[8] and 80% of workers[9] belong to the informal sector. In addition, disbursing support payments will be difficult because 66% of families do not have a bank account. That is why the announced fiscal packages are primarily directed at the formal segment of the economy, so that their effects are likely to be rather limited. In order to make the measures more effective for the general public, Kenya is currently working to organise the disbursement of cash transfers through mobile money accounts. Many mobile money customers work in the informal sector, which increases the chances of these transfers reaching more families but these accounts are spread very unevenly across individual countries (Figure 8). The use of mobile money for a broader distribution of cash transfers is thus not suitable for all African economies.

Figure 8: Mobile money users

In percentage shares of the working-age population, 2019



Sources: Center for Global Development, EFInA, own rendition

Preliminary assessment of the situation in Africa

It is difficult to predict how the situation in Africa will evolve. Case numbers are rising, although currently more slowly than in Asia, Europe and the US. On the positive side, African states were much quicker to adopt measures aimed at containing the pandemic than European countries. Although these measures are correct and important to slow the spread, they are an additional burden on the already weak economies.

Most of the transactions in the service sector, which is key to Africa's economies, are informal and local. The service economy has been hit the hardest by the containment measures. Unlike in America and Europe, buying goods online is not an alternative. As a result, many families will see their income dry up in the near future. Many African states do not have the funds and distribution channels that are necessary to mitigate the economic impact.

Moreover, the global slump in demand is closing export markets for many African products and inflationary pressures are rising as many imported goods, especially medicines and food, are becoming increasingly scarce because of production shutdowns and logistical bottlenecks. This parallel development will additionally take away purchasing power in many countries, slow down growth further and make it harder to supply the population. At the same time, populations continue to grow at a fast rate. The current crisis therefore has the potential to massively slow Africa's economic and social development in the years ahead and reverse progress previously achieved.

[1] WHO Covid-19 Situation Update for the African Region, 15 April 2020

[2] UNECA 2020 'Economic Impact of the COVID-19 on Africa'

[3] Standard Chartered 2019 'Oil Notes – OPEC+ collapse sparks oil price war'

[4] UNECA 2020 'Economic Impact of the COVID-19 on Africa'

[5] World Bank 2020 'Assessing the economic impact of COVID-19 and policy responses in Sub-Saharan Africa'

[6] UNECA 2014 'Dynamic Industrial Policy in Africa'

[7] Mastercard's Annual Index of Women in Entrepreneurs 2019

[8] IMF 2016 'The Informal Economy in Sub-Saharan Africa: Size and Determinants'

[9] ILO 2018 'More than 60 per cent of the world's employed population are in the informal economy'