Sub-Saharan Africa's Economic **Outlook 2019**

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Sub-Saharan Africa

Differentiated growth outlook

Global backdrop still supports a moderate improvement in growth

The next two to three years will emphasise the **structural reforms** that many African economies need to undertake. After all, the FX supply problems in some of these economies are now behind us.

Admittedly, Angola still has the remnants of the FX challenges that hamstrung economic growth, ensuring that the economy would endure three years of recession. But, even here there is light at the end of the tunnel. Recall that the central bank devalued the kwanza, taking USD/AOA to 166 in mid-2016 from about 103 at the end of 2014. Having kept the pair around 166, the Banco Nacional de Angola then devalued the kwanza more forcefully during 2018.

But, before then, oil prices had recovered, with Brent crude rising back above USD60/bbl in late-2017. The current account balance, which registered a deficit of nearly 9.0% of GDP in 2015, gradually improved and turned to a surplus that we estimate was just over 7.0% of GDP in 2018. This is despite the decline in oil production from nearly 1.8m bpd in 2015 to less than 1.5m bpd in 2018. The fiscal balance also improved, turning to surplus last year. All these developments suggest that the backlog of FX demand is likely to be fully satisfied quite soon.

To top it all, the Angolan government has obtained financial assistance from the IMF via a SDR2.67bn (roughly USD3.7bn) Extended Fund Facility program. Fiscal consolidation, diversifying tax revenue by mobilising non-tax revenues and structural reforms to diversify the economy are key elements of the program.

In Nigeria, another economy that is enjoying a recovery after suffering from FX supply shortages, structural reforms are likely to be on the agenda. There will be elections in February and March for national and state elective offices respectively. Challenging President Buhari is Atiku Abubakar of the Peoples Democratic Party, who served as the Vice President between 1999 and 2007. He has made forceful arguments for floating the NGN, reforming the national oil company (perhaps even partly privatising it), and allowing domestic fuel prices to be cost-reflective.

Even if he were not to win, President Buhari is likely to press ahead with the reform agenda that he proposed when he got elected the first time around.

These reform efforts, and many others across the continent, are likely to be bolstered by a **global backdrop that still supports a continuation of the moderate acceleration in economic growth across the continent**.

The experience of 2018, where an emerging market sell-off occurred against a backdrop of strong global economic growth and elevated commodity prices, is comparable to 1998. Just as in 2018, global economic growth was strong in 1998. The US economy was enjoying a productivity-fuelled surge in economic growth.

But unlike 1998, commodity prices were still elevated in 2018. Sure, some of these dropped meaningfully in H2:18. Copper prices fell from over USD7,000/MT in mid-Jun to just below USD6,000/MT in mid-Aug, where they remained for the remainder of the

year. Brent crude oil price fell from just over USD85.0/bbl in early-Oct to nearly USD50.0/bbl in late-Dec.

Commodity prices: murky near-term outlook

The decline in commodity prices in the latter part of 2018 has put many of them in no-man's land. They are neither low enough to suggest that they are oversold nor high enough to suggest further upside.

Figure 1: Commodity prices have dropped

Source: Bloomberg

The decline in oil prices was very curious. It came just days after OPEC members and some other major non-OPEC countries decided to cut production further. The recovery since the beginning of the year has put the Brent crude oil price at a level that is consistent with the budget assumptions for Nigeria and Angola.

Although consensus forecasts for copper were pulled lower in Q3:18, following the decline in copper prices, expectations are still that they will rise above USD6,500/MT by the end of this year. It seems like the prognosis to the effect that the supply-demand balance for copper points to supply tightness in coming years has led to expectations of elevated copper prices in coming years.

As is the case with oil prices, there is nothing to suggest that copper prices might not initially decline from current levels before rising later in the year. There are already indications that perhaps the Chinese economy is slowing more quickly than consensus expectations, with the PMI indicating that the manufacturing sector may have contracted towards the end of 2018. Of course, there are plenty of other risk events that may dampen confidence somewhat, not least of which is the trade negotiation between the US and Chinese governments.

Political risks: heavy electoral calendar

The market is likely to keep an eye on a number of key elections in the countries in our coverage. However, for the most part these elections carry little security or policy risks. This might be because the chances of a change in government are low or there isn't that much divergence in policy preferences among the leading parties in those countries.

Mauritius epitomises this. That country's politicians are adept at realigning alliances. Admittedly, political leadership tends to revolve around a small core of what might be regarded as political dynasties. Who becomes Prime Minister at any given point in time depends on the alliances of the day. But a political alliance led by either a Ramgoolam or a Jugnauth has always won.

From 1967 to 2014 the country had 11 elections, but only 5 prime ministers. Sir Seewoosagur Ramgoolam was the first prime minister, replaced by Sir Anerood Jugnauth in 1983, who in turn was replaced by Dr Navin Ramgoolam (Seewoosagur's son) in 1995. Although Sir Anerood Jugnauth became prime minister after the 2000 elections, he resigned 3-y later to allow Paul Berenger to take over. In 2005 Dr Navin Ramgoolam returned as prime minister. In 2014 Sir Anerood Jugnauth became prime minister again, but resigned in 2017 to allow his son, Pravind Jugnauth, to become prime minister.

It is also hard to regard the upcoming general elections in Namibia as risk events. Sure, the ruling South West African People's Organisation (still referring to the country's old name), is presiding over an economy that is in recession. The deterioration in fiscal metrics, characterised by a rising debt/GDP ratio that contributed to the downgrade in credit ratings, also leaves the government with little room for manoeuvre.

The elections are likely to be peaceful. Despite contentious land reform proposals, we doubt that business and investor sentiment towards the country will deteriorate in the period leading up to the elections.

At face value, the Nigerian elections could usher meaningful change in macroeconomic policy management, if Abubakar were to win and follow through on his promises with respect to the currency. But it is hard to believe that policymakers would actually float the NGN. The exchange rate would probably end up being extremely volatile relative to the past. After all, oil exports account for close to 90% of total goods exports. The volatility of oil prices would probably be a primary driver of USD/NGN volatility. Furthermore, portfolio flows would very likely exaggerate any oil price induced volatility in USD/NGN.

The DRC had its first ever peaceful transfer of power via the ballot box since independence. However, this is probably easy to overlook, and instead focus on the uneasy calm that has descended upon the DRC following the announcement by that country's electoral commission that Felix Tshisekedi won the presidential elections held in late-December. The presidential election was essentially a 3-horse race between Emmanuel Shadary of the ruling People's Party for Reconstruction and Democracy (PPRD), Felix Tshisekedi of the Union for Democracy and Social Progress (UPDS) and Martin Fayulu of Lamuka, a coalition of 7 parties.

There was something of a controversy on the eve of the elections. Opposition parties decided to club together and present a single presidential candidate. At the summit to nominate the candidate, Martin Fayulu emerged as that nominated candidate. But immediately after the summit, Felix Tshisekedi had a change of heart and opted to go it alone.

In the end, Tshisekedi pipped Fayulu to the post. Fayulu challenged the validity of the results, alleging that they were a fabrication following a deal between outgoing President Kabila and Tshisekedi for the latter to be declared as the winner. The Constitutional Court ruled against Fayulu. It remains to be seen whether his call for demonstrations will lead instability.

Ian Khama stepped down as Botswana's President in April 2018, appointing Mokgweetsi Masisi in his place. But the two fell out almost instantly, apparently over Khama's retirement entitlements and pension. 4 opposition parties could form a coalition in an effort to unseat the ruling Botswana Democratic Party in the October elections.

Anxiety could mount in the lead-up to the Mozambican general elections in October. If the local government election in September 2018 are any guide, the outcome could be close. The opposition RENAMO party's fighters are supposed to be integrated into the

army as part of a peace agreement between the party and the government. But the party complained last year that in some regions its agents were not being allowed to freely operate, raising the risk that the party might boycott the elections.

A peaceful election, and progress in implementing the peace agreement will be crucial for the country. Key investments in the fledgling gas sector may well be dependent on this. These investments have the potential to transform the country's economy in the next 10 to 15 years.

Debates between presidential candidates will headline the Malawian presidential elections due in May. President Mutharika dismissed his former deputy, Saulos Chilima in early November 18. Chilima may well challenge him. There are allegations of corruption against the president, with news reports indicating that he may have received a bribe. Former president Joyce Banda, implicated in a 2013 corruption scandal, may also be a candidate.

Although Ghana's general elections are not until next year, they are likely to affect market sentiment this year too. It is not so much the elections that might matter, but perceptions that political calculations might enter fiscal policy conduct. Already there has been a delay in the completion of the 7th review of the IMF's Extended Credit Facility.

Although IMF staff visited the country in September 2018, there has been no indication that the review was completed. We believe that the 7th and 8th reviews might be combined in April, when the program is due to expire. We also believe that it is fiscal performance that is preventing a successful completion of the 7th review. Revenues were consistently below budget in 2018, prompting the government to revise the budget and cut spending, mostly capital expenditure.

This experience might cause many market players to doubt that the government will stick with the fiscal consolidation effort going into next year. To be sure, the government has been trying to assure the market that it will stick with the aim of keeping the fiscal deficit between 3% and 5% of GDP, meant to be enshrined in a fiscal responsibility law, even if there are delays in enacting such a law.

Elections in Côte d'Ivoire will also only be next year. But following the fracture between the Democratic Party of Côte d'Ivoire (PDCI) and the Rally for Republicans, the market will probably watch developments there very closely. Additionally, the International Criminal Court dropped charges against Laurent Gbagbo, potentially allowing him to make a return to active politics We still think that a process that will lead to a realignment of coalitions could be underway there. It is well worth noting that nearly 30% of MPs are independents. But reports of fatalities last year as a result of post-election violence in parts of the country might be a source of lingering concern for the market.

FX outlook: stability likely to return

Most **African currencies are likely to rebemain stable this year**. The terror attack in Nairobi in mid-January hardly caused a flutter in the FX market, even though it could have caused some trepidation. Even as we admit that there is a risk that the attack may undermine tourism, which has enjoyed a long period of revival, we are not convinced that it could cause the shilling to depreciate that much.

It is worth recalling that a similar attack in 2013, exacerbated by other security incidents along the coast immediately afterwards, precipitated an average 12.0% y/y drop in visitor arrivals in the four years to 2015. In response to this attack, many governments of countries from which most tourists originate issued travel advisories urging their citizens not to travel to Kenya.

Yet, despite this drop in tourist arrivals, the USD/KES exchange rate rose by just 3.1% in the 12-m following the 2013 attack. But in the 12-m to September 2015 it rose by a further 18%. Foreign investors' holdings were close to 10% of total domestic debt in September 2013. Arguably, the pressure on the shilling in 2015 was mainly due to these outflows. Foreign investors' holdings are currently less than 5% of total debt, potentially reducing the upward pressure on the exchange rate.

As already argued above, there are reasons to believe that the naira peg will remain in place even if the opposition were to win the elections. This is all the more so if oil prices were to remain in a USD60/bbl to USD65/bbl range.

The Angolan kwanza was the worst performing currency in 2018, with the central bank devaluing it by about 45%. But it essentially stopped devaluing it since about mid-October 2018. It is highly unlikely that it will be devalued significantly this year.

The IMF does not require the kwanza to be devalued further as part of the economic program that it has financed. In fact, the IMF's assessment is that the devaluation of the kwanza in 2018 took it from being about 26% overvalued to being less than 4% undervalued. Furthermore, the IMF seems happy with the narrowing of the gap between the official and parallel exchange rates. Even then we expect the exchange rate to rise by just over 11% this year.

The Malawian and the Zambian kwacha are 2 currencies that continue to defy our expectations. We are still concerned about the Zambian kwacha. Foreign exchange reserves fell to USD1.6bn in October from USD2.4bn in June 2017 and USD2.1bn in December 2017. Clearly, if copper prices were to decline to below USD4,500/MT then some copper mines might be forced to cut production.

If portfolio investors holding local currency bonds do not liquidate those, then the Zambian kwacha will likely not depreciate as much as we expect. Additionally, the government has budgeted for a reduction in domestically-financed capital expenditure, something that should lower the government's FX requirements. But it will need to obtain all the external financing that it budgeted for. Otherwise it would face challenges meeting its external debt service obligations.

Similarly, something will perhaps need to trigger the depreciation of the Malawian shilling. The sharp depreciation of the MWK ended in early 2016, having depreciated at a 23.5% annualised pace in the prior five years. Financial support from the IMF has helped not only in bolstering FX reserves, but also encouraging aid inflows.

There is an election later this year. Former President Banda, who was implicated in the bribery scandal in 2013, intends to run. The current president, who is running for re-election, is suspected of taking bribes. Perhaps, only if the risk of fiscal slippage materialises or there are threats to aid inflows would the MWK depreciate sharply.

Even though there is likely to be disruption to oil production this year due to repairs to the offshore platform on the Jubilee field, portfolio flows probably matter more for the Ghanaian cedi. The amount of coupon payments that will likely accrue to foreign investors is quite large. With the Bank of Ghana likely to be biased towards easing the policy stance, there might be some portfolio outflows that might weaken the cedi. As pointed out above, the market is apprehensive about fiscal policy conduct, something that will likely skew portfolio flows towards outflows.

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