OECD *Multilingual Summaries*

African Economic Outlook 2010

Summary in English

- *The African Economic Outlook 2010* investigates how public resource mobilisation can help Africa reduce its dependence on aid and other external financial flows to finance its own development agenda; it reviews best practices in tax administration and multilateral agreements as well as policy options for meeting future challenges.
- Africa was propelled by seven years of strong growth from 2002 to 2008, only to be stopped in its tracks by the world's deepest and most widespread recession in half a century. This edition finds the continent struggling to get back on its feet and identify new, more crisis-resilient practices for moving forward.
- This year's Outlook reviews recent economic, social and political developments and the short-term likely evolution of 50 African countries.
- Its overview chapter provides a comparative synthesis of African country prospects which places the evolution of African economies in the world economic context.

Macroeconomic and Structural Developments

Macroeconomic Prospects

The world economic crisis brought a period of relatively high economic growth in Africa to a sudden end. Average economic growth was slashed from about 6% in 2006-2008 to 2.5% in 2009 with per capita Gross Domestic Product (GDP) growth coming to a near standstill. The global crisis of 2009 had its strongest effect on southern Africa, where growth dropped drastically (from the average over the preceding three years) by almost 8 percentage points to negative growth of around 1%. East Africa and North Africa proved to be the most resilient regions.

In Africa, the global crisis was mainly felt through the collapse of commodity prices and the fall of export volumes. In 2009, Africa's export volumes declined by 2.5% and import volumes by about 8%. Due to the fall in commodity prices, Africa's terms of trade deteriorated. Export values declined sharply, and more than import values, leading to a deterioration of trade and current account balances. The global crisis also hit through the decline of worker remittances and of foreign direct investment.

On the positive side, donor countries have generally maintained their aid flows to Africa, despite substantial fiscal pressures at home. Furthermore, debt relief under the Heavily Indebted Poor Countries initiative by the International Monetary Fund (IMF) and the World Bank has reduced debt service costs. This together with additional loans by the IMF, the World Bank and the African Development Bank has helped African countries to better cope with the crisis.

Thanks to past fiscal prudence and to disinflation, many African countries could pursue expansionary fiscal and monetary policies, which mitigated the downturn. Major public spending programmes were mostly continued and key policy interest rates were reduced. However, in a few countries, where economic fundamentals were less favourable, governments were forced to pursue tight macro policies to counter deteriorating current balances, falling exchange rates and losses of international reserves.

A gradual recovery of African economies is expected with average growth reaching 4.5% in 2010 and 5.2% in 2011. All African regions will achieve higher growth although the recession will leave its mark. Southern Africa, which was hardest hit in 2009, will recover more slowly than other regions. East Africa, which best weathered the global crisis, is likely to again achieve the highest average growth in 2010/2011.

External Financial Flows to Africa

Many African governments have implemented frameworks to attract more foreign investment. Nonetheless, most foreign investment in Africa goes to extractive industries in a relatively limited group of countries. Attracting investment into diversified and higher value-added sectors remains a challenge for Africa. Constraints on investment such as weak infrastructure and fragmented markets also adversely affect foreign direct investment (FDI) flows to Africa.

Prior to the financial crisis, however, FDI to Africa had been rising strongly, driven by a surge in prices for raw materials, particularly oil, which triggered a boom in commodity-related investment. The global crisis led to a considerable slowdown and preliminary estimates for 2009 indicate foreign investment fell by more than one third.

African countries are developing Special Economic Zones to attract FDI. Foreign investors, notably China, are promoting the creation of such zones, which provide employment, spill over to domestic economies and allow firms to benefit from better infrastructure and easier regulations. By investing in Africa, emerging countries also benefit from the preferential trade agreements of African countries with Europe and the United States.

Official Development Aid to Africa appears to have been broadly sustained during the global crisis. Prospects for meeting the Group of Eight (G8) target of increasing aid to poor countries by USD 50 billion from 2004 to 2010 will depend on sharply accelerating growth in core development aid.

Donors outside the OECD's Development Assistance Committee are becoming more important for Africa. China gives aid to almost every country in sub-Saharan Africa. Some argue that Chinese aid is only motivated by access to Africa's natural resources. However, there is little evidence that China gives more aid to countries with more natural resources, or specifically targets countries with a poor governance record.

Trade Policies and Regional Integration in Africa

A rising number of protectionist measures were adopted by advanced countries in 2009 to curb the effect of the financial crisis. Often stimulus packages were geared to favour domestic sectors, such as through export support or preferences for buying, lending, hiring or investing in local goods and services. Such measures clearly discriminate against developing countries, including those in Africa.

A critical reason for Africa's relatively poor trade performance is the weak diversification of African trade in terms of structure and destination. Most African economies depend on few primary agricultural and mining commodities for their exports and mainly import manufactured goods from advanced countries. As traditional markets in advanced countries are expected to grow less than those in emerging Asian and Middle East countries as well as markets in Africa, trade relations with these more dynamic markets must be enhanced.

Despite some progress, intra-African trade is still low, representing on average only about 10% of total African exports. Many factors contribute to the low trade performance, including the economic structure of African countries, which constrains the supply of diversified products, poor institutional policies, poor infrastructure, weak financial and capital markets, political instability, insecurity in several regions and intra-African trade barriers.

African countries, with the assistance of the regional communities and development partners, are working to strengthen infrastructure development. In addition, the regional communities are developing and implementing harmonised laws, standards, regulations and procedures to ensure the smooth flow of goods and services and to reduce transport costs.

Millennium Development Goals

With five years left to the target date to reach the UN Millennium Development Goals, progress on most has been sluggish and it is unlikely that they will be attained.

Eradicating Extreme Poverty and Hunger. It is probable that the trend of poverty reduction has been reversed in many African countries, knocking them far off track to achieving the goal. The African Development Bank estimates that the continent would need about USD 50 billion per year of additional financing to reach the GDP growth rates needed to halve poverty by 2015.

Achieving Universal Primary School Completion. Despite absolute improvements in primary school enrollment and completion rates, the continent is likely to miss the goal. Countries reporting the most progress in primary enrolment and completion rates are those with significant private primary education sectors.

Promoting Gender Equality and Empowering Women. There has been much progress in achieving gender parity at primary school level. Progress has been slower and more uneven for gender parity in secondary and tertiary education, gender equality in employment, and increased political representation for women.

Reducing Mortality of Children Under Five. This goal is unlikely to be met by the target date. In particular, poverty and malnutrition, HIV/AIDS, low immunization coverage, high neo-natal deaths, and malaria still factor into the stagnation and reversal of previous gains made in reducing children mortality rates in some countries.

Improving Maternal Health. Despite some improvement, the risk of dying from maternal causes remains high in many African countries.

Combating HIV/AIDS, Malaria and Other Diseases. In 2008 sub-Saharan Africa accounted for about two thirds of new HIV infections among adults worldwide and about 90% of new HIV infections among children. Over time, there have been encouraging gains, but progress must be accelerated if the millennium targets are to be met.

Ensuring Environmental Sustainability. African countries face a significant challenge achieving their set goals by 2015 while also sustaining development and preserving the environment in the longer term.

Political and Economic Governance

Stability was broadly maintained in 2009. Lower food and energy prices relieved the burden on households, including the vocal urban middle class that had instigated protests in 2008. Several governments put measures in place to sustain internal demand, thus limiting social tensions. Nonetheless, rising unemployment exacerbated social discontent in several countries. Concerns remain for the future, as fiscal stimulus measures have to be phased out to restore fiscal sustainability while at the same time unemployment may remain high or increase.

Overall in 2009, tensions and hardening indicators decreased. Several countries successfully undertook fair democratic elections, and government accountability increased. While setbacks are still common, improvements in checks and balance mechanisms bode well for future institutional consolidation in Africa. High-intensity conflicts and rebellions generally calmed down, with some important exceptions. When confronted with tensions, many governments struck a better balance between hardening their military stance and launching/strengthening dialogue with rebellion movements.

By and large, governments reacted more strongly and more responsively than in the past, which may contribute to reducing long-term tensions.

To further strengthen political governance, however, and step up social progress, civil society must continue to develop and increase its capacity to become more involved in the political process. On the government side, institutional capacity needs to be strengthened and reforms pushed forward, in particular in the judiciary and security realms.

Despite the efforts recorded in some countries and rising domestic and international attention, corruption remains a serious problem in Africa. With respect to economic governance, Africa registered marked improvement in its regulatory environment in 2009. Several countries have introduced new laws or reformed existing laws, making it easier to do business.

Public Resource Mobilisation and Aid

The global economic crisis has given a new impetus to dialogue on domestic resource mobilisation in Africa. Lower export revenues, uncertain future foreign investment and aid inflows amidst generally high levels of indebtedness have raised the importance of increasing domestic resources. Africa faces three types of challenges with respect to mobilising additional public resources: structural bottlenecks; an unbalanced tax mix; and the erosion of existing tax bases by excessive granting of tax preferences, inefficient taxation of extractive activities and an inability to fight transfer pricing by multinational enterprises.

The solution is not to simply raise existing taxes. Strategies towards more effective, efficient and fairer taxation in Africa typically lie with deepening the tax base in administratively feasible ways. Policy options include removing tax preferences, dealing with abuses of transfer pricing techniques by multinationals and taxing extractive industries more fairly and transparently.

In the longer term, the capacity constraints of African tax administrations must be eliminated to open up policy options and enable tax revenue generation through a more balanced tax mix. Indeed, taxing new potential payers is crucial. The report identifies in particular urban property taxation as an instrument that can be more easily implemented with the aid of development partners. This type of taxation is progressive and can be scaled up with Africa's rapid pace of urbanisation and the corresponding need for financing urban infrastructure.

Ideally, taxes should be levied at low and relatively flat rates on bases broadened through the elimination of exemptions and other loopholes. Lower, simpler taxes are easier to collect and administer, and are an effective approach to stimulating private sector development.

The average African tax revenue as a share of GDP has been increasing since the early 1990s, mostly because of taxes on the extraction of natural resources. Income taxes (mainly personal and non-resource corporate) have stagnated over this period. At the same time, trade liberalisation in Africa has led to a reduction of revenue from trade taxes. Indirect taxes, corporate taxes and resource-related tax revenues have increased since the late 1990s.

There are very large differences in the tax raising performance across individual countries. Annual taxes per capita range from as low as USD 11 to USD 3 600. In fact, tax effort estimates confirm that some countries collect as little as half of what they would be expected, given their living standards and economic structures, while others collect two to three times what would be expected.

Many African countries are still heavily dependent on aid. In the past, donors have devoted little attention to public resource mobilisation. But targeting a larger share of aid to this goal, would enable countries to become less dependent on aid in the long run, to the benefit of recipients and donors.