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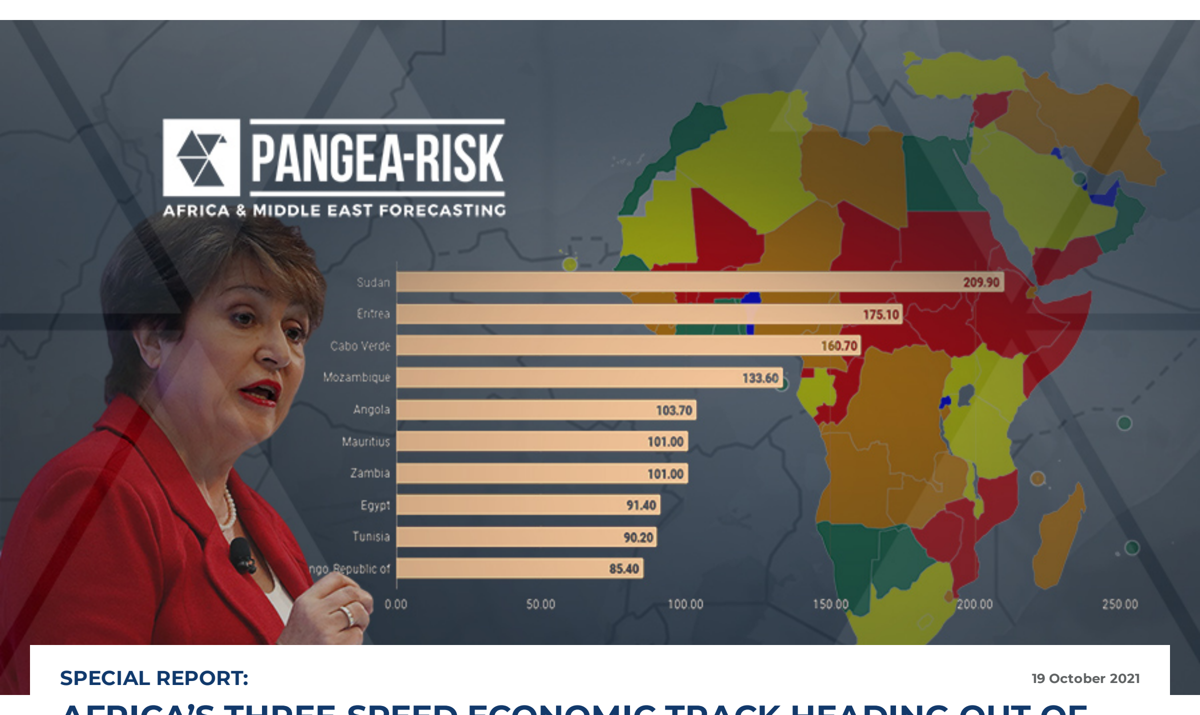


SPECIAL REPORT: 19 October 2021

AFRICA'S THREE-SPEED ECONOMIC TRACK HEADING OUT OF THE PANDEMIC

October's IMF and World Bank annual meetings may have been overshadowed by geopolitical rivalries, but the message for Africa is that the continent is now on a three-speed economic track heading out of the pandemic and that debt sustainability risks will rise from next year. Debt restructuring will again play into these same geopolitical rivalries, while western support on climate change adaptation may further increase debt burdens for African governments. PANGEA-RISK seeks to make sense of the Bretton Woods institutions' mixed messaging on Africa in this special report, which also ties economic and sovereign debt projections to our newly updated bespoke country risk ratings.

On 17 October, the International Monetary Fund (IMF) and the World Bank finished the annual meeting of the world's two foremost international financial institutions with a strong warning on African debt sustainability. According to a new World Bank report released at the meeting, the debt of low- and middle-income countries in sub-Saharan Africa increased to a record USD 702 billion in 2020, more than doubling from USD 305 billion in 2010. Most of this debt, i.e., USD 589 billion, consists of long-term external debt, mostly denominated in foreign currency. The World Bank report specifically issued warnings of debt distress for four countries: Angola, Mozambique, Zambia, and Cape Verde, based on a debt to Gross National Income (GNI) ratio of above 100 percent. Both Zambia and Mozambique's sovereign debt have fallen into default, while PANGEA-RISK has forecast debt sustainability warnings on Angola and Cape Verde in previous reports.

At the annual meeting, World Bank Group president David Malpass said, "we need a comprehensive approach to the debt problem, including debt reduction, swifter restructuring and improved transparency." He also warned that the debt situation for poor countries could worsen due to volatile commodity prices and higher interest rates, urging countries to begin a gradual fiscal consolidation to maintain investor confidence. However, the IMF and World Bank did not agree to extend the pandemic-era Debt Service Suspension Initiative (DSSI). This means that countries offered a suspension of their bilateral and concessional debt interest payments during 2020 and 2021 will have to resume interest payments from 2022, while also settling the arrears on two years of suspended interest payments. Countries that are unable to meet such terms will have to apply to the Common Framework for debt treatment beyond the DSSI to manage a restructuring of their debt. So far, three African countries have applied to the Common Framework: Zambia, Chad, and Ethiopia, with creditor committees already formed for the latter two countries.

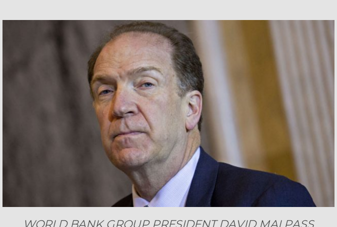
PANGEA-RISK delves deeper into the main takeaway messages from the annual meeting of the world's most prominent international financial institutions and the impact on the country risk outlook for Africa.

Scandal at the World Bank

The October 2021 annual meeting was overshadowed by allegations that former World Bank acting president Kristalina Georgieva, who is now the IMF's managing director, and current World Bank president Malpass presided over the manipulation of data for the Bank's 'Doing Business' index. The index is an important input for many investment rankings used by companies investing in Africa. Many African countries have hired lobbying and consulting firms to boost their ranking on the World Bank index. Togo, Morocco, and Rwanda, for example, have seen noticeable improvements in their rankings by addressing key benchmarks in the 'Doing Business' index over past years. PANGEA-RISK has previously been critical of the 'Doing Business' methodology believing it has been open to manipulation and misinterpretation, and the index does not feed into PANGEA-RISK's own country risk scoring methodology.

IMF MANAGING DIRECTOR KRISTALINA GEORGIEVA

Most African countries backed the current IMF and World Bank leadership, which also maintained the support of the European Union and China in the dispute. Ahead of the annual meeting, 17 African finance ministers backed Georgieva in a public statement. In the 'Doing Business' rankings, these same 17 countries gained an average of 11 positions from the 2017 report, which was published in 2016, the year before Georgieva joined the World Bank, to the 2020 report, which was published in 2019, the year she left.

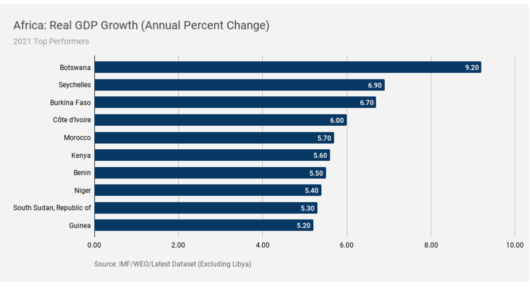


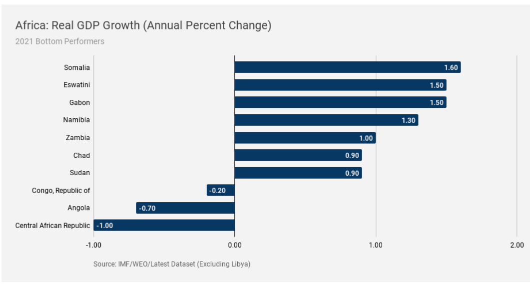
WORLD BANK GROUP PRESIDENT DAVID MALPASS

The US and Japan unsuccessfully tried to remove the institutions' leadership and both Georgieva and Malpass have been retained in their roles. This means that the current IMF policy of rapid financial support for emerging markets during the pandemic will be continued. In 2020, the IMF disbursed USD 30 billion in financial support to African countries. Notable amounts disbursed include USD 8 billion to Egypt, USD 3.4 billion to Nigeria, and USD 2.47 billion to Sudan as financial assistance. Additionally, since the start of the pandemic in March 2020, the World Bank has made available nearly USD 24.7 billion to respond to the COVID-19 crisis in sub-Saharan Africa. Together the two institutions also lobbied for the creation of the DSSI debt relief scheme.

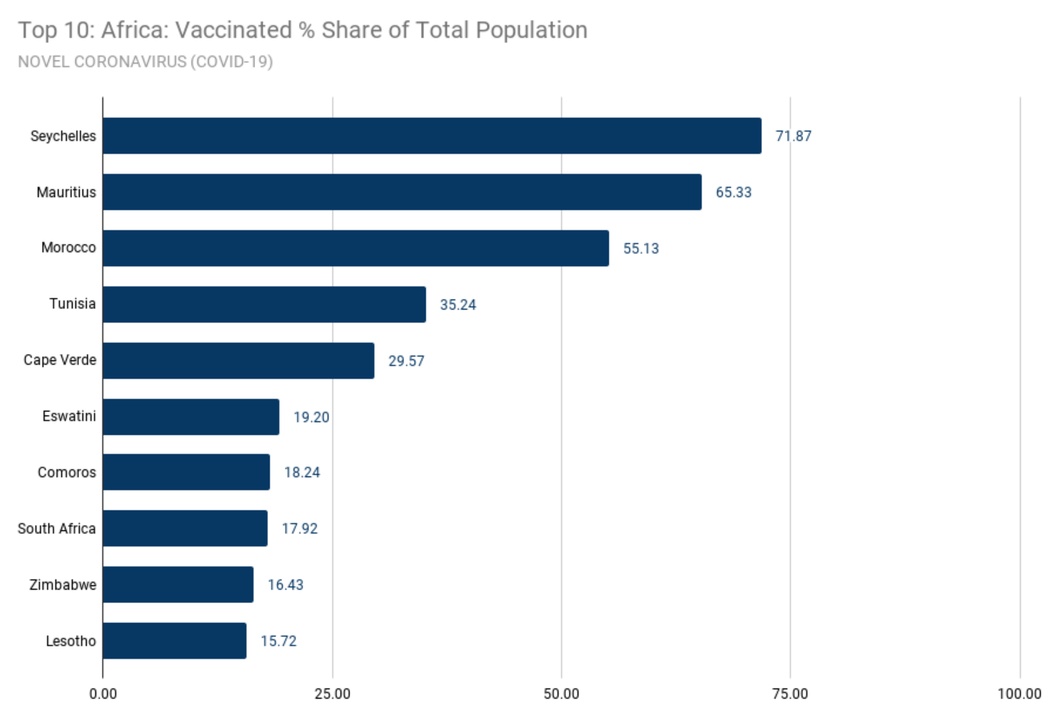
Africa's three-speed economic recovery

According to Africa's Pulse, which is the World Bank's twice-yearly economic update for the region, Sub-Saharan Africa is set to emerge from the 2020 recession sparked by the COVID-19 pandemic with growth expected to expand by 3.3 percent in 2021. According to Africa's Pulse, this rebound is fuelled by elevated commodity prices, a relaxation of stringent pandemic measures, and recovery in global trade. However, the Bank warned that the region remains vulnerable given the low rates of COVID-19 vaccination on the continent, protracted economic damage, and a slow pace of recovery. Moreover, fiscal constraints that pre-dated the pandemic have left African countries unable to provide adequate stimulus measures to engineer a sustained recovery. Africa's Pulse estimates the funding gap at USD 290 billion in 2020. Sub-Saharan Africa needs significant additional funding to counter damage wrought by the coronavirus pandemic, bolster its economic recovery prospects, and mitigate threats posed by climate change, according to the World Bank.





Meanwhile, the IMF has revised its 2021 global economic growth forecast down slightly, highlighting the uneven pace of the vaccination roll-out between advanced and low-income economies. The Fund projects that sub-Saharan Africa will achieve 3.7 percent GDP growth in 2021 and 3.8 percent growth next year, up from a 1.7 percent economic contraction in 2020. This projection for sub-Saharan Africa is well below the Fund's global economic forecast of 5.9 percent growth, and a reversal of the trend of the past few years where African economies outpaced the rest of the world.



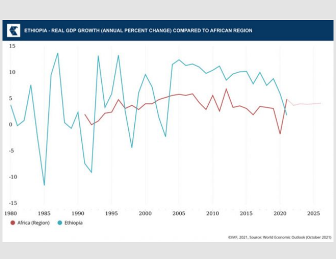
The main driver of economic recovery is the COVID-19 vaccination rate, with the outlook for the low-income developing country group darkening considerably due to worsening pandemic dynamics, according to the IMF. "While almost 60 percent of the population in advanced economies are fully vaccinated and some are now receiving booster shots, about 96 percent of the population in low-income countries remain unvaccinated," the Fund has said. The Africa Centres for Disease Control and Prevention data show that Africa is the world's least-inoculated region with only 4.3 percent of its 1.2 billion people fully immunised against the disease. Meanwhile, commodity prices, and the mismatch in supply and demand stemming from global bottlenecks, have in turn set off inflationary alarm bells. The IMF therefore sees interest rates rising faster than previously expected, which will have important consequences for Africa's economies.

These factors have created a three-speed economic trajectory for Africa, categorised by economies boosted by higher commodity prices, such as Burkina Faso, South Sudan, and Guinea, whose GDPs are all set to grow by 5 percent or more. This category also includes countries who led the pre-pandemic economic growth rate charts thanks to relatively superior fiscal and monetary governance, such as Côte d'Ivoire, Kenya, Benin, Niger, and Rwanda. Moreover, the fast-track also includes countries whose economies dipped by the most in 2020, notably Botswana, Seychelles, and South Africa. The region's most industrialised economy, South Africa, saw its growth forecast by the IMF for this year lifted by a full percentage point from 4 percent to 5 percent previously, indicating a recovery from a deep contraction of 5.7 percent last year. However, the South African economy is the only one among the G20 group of countries that will not achieve pre-pandemic levels of growth before 2022.

Meanwhile, the majority of African countries will fail to match the global economic recovery rate of above 5 percent growth this year as they suffer from low vaccination rates. This category includes major regional economies such as Nigeria, Ghana, Egypt, Algeria, and Sudan. In North Africa, Morocco leads the pack with a projected GDP growth rate of 5.7 percent, but all other countries in the region lag despite deep economic contractions in 2020. Most countries in Africa are on this medium-speed laggard-track, indicating that most of the continent will not reach pre-pandemic economic output levels for several more years. This trend is a major setback for Africa's growth narrative and puts the continent behind other emerging market regions.

The slowest-speed track includes countries with structural economic weaknesses such as Angola and Republic of Congo, as well as war zones and failing states such as Central African Republic, whose economies will continue to shrink this year. Matching PANGEA-RISK forecasts at the start of 2021, Angola will suffer from a sixth consecutive year of economic contraction, while Congo marks a seventh year of negative GDP growth (see ANGOLA: ECONOMIC CHALLENGES AND CONSTITUTIONAL CONTROVERSY DRIVE ELECTIONS OUTLOOK). Other African countries that will barely register economic growth in 2021 include Common Framework applicants Chad and Zambia, debt distressed Namibia, and states with deep inherent imbalances such as Sudan and Eswatini (formerly known as Swaziland).

No economic projections for Ethiopia

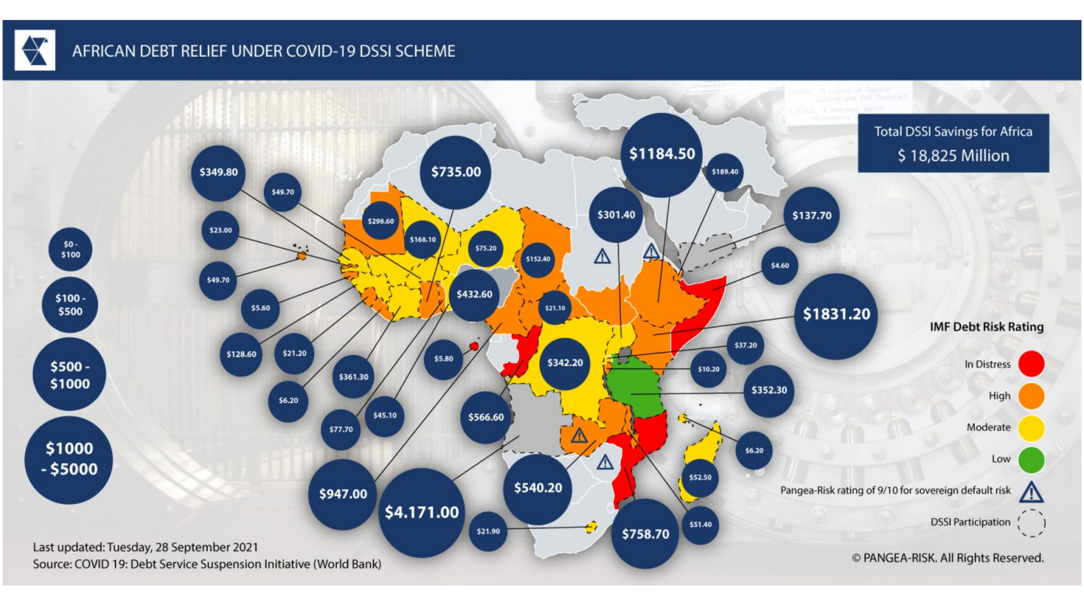


The IMF has not released a GDP growth forecast for Ethiopia in its latest World Economic Outlook for the next four years. Africa's fastest growing economy for many consecutive years is now categorised with other war zones such as Afghanistan, Libya, and Syria. The ongoing civil war in Ethiopia's northern regions is the most likely reason why the multilateral lender has withheld its predictions for the country's economic recovery in 2022, although the Fund still forecasts a 2 percent GDP growth rate for this year. As a former champion of foreign investment, Ethiopia now also faces western sanctions, a threatened suspension of US preferential trade terms, and a potential debt default scenario (see SPECIAL REPORT: CLOUDS GATHER AS ETHIOPIA'S PRIME MINISTER STARTS FIRST FULL TERM).

The lack of economic projections will certainly frustrate Ethiopia's efforts to attract new foreign direct investment for the government's flagship privatisation spree in telecoms and other key sectors, while also potentially disrupting the country's debt restructuring process led by China and France and its application for disbursements from the IMF's Extended Credit Facility and Extended Fund Facility (see ETHIOPIA: STABILISING THE DEBT POSITION EVEN WHILE SECURITY COSTS DRAIN STATE REVENUES).

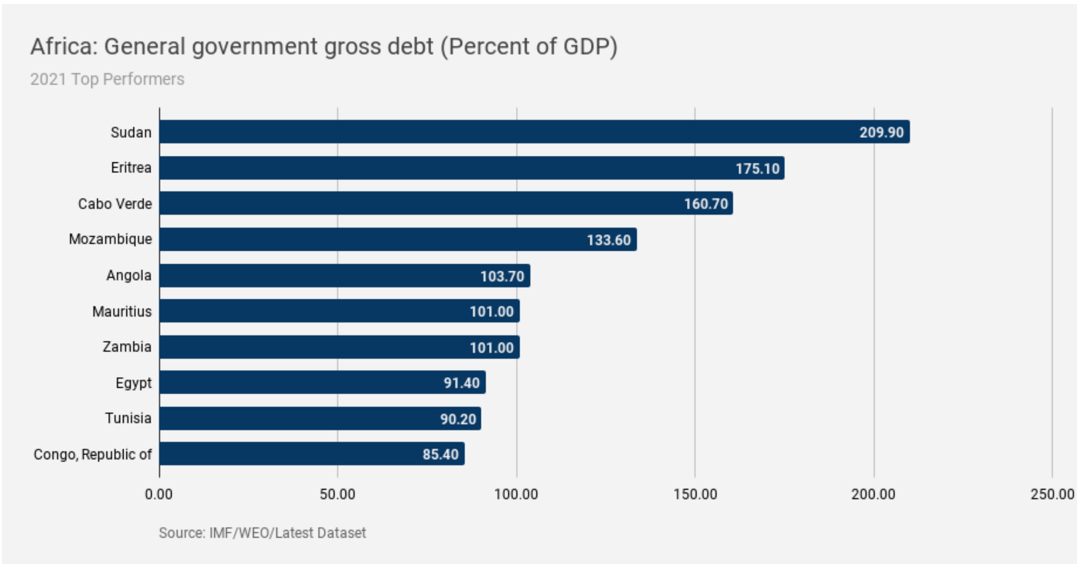
Debt sustainability outlook

Last year, the World Bank and the IMF urged G20 countries to establish the DSSI, which has delivered more than USD 5 billion in relief to more than 40 eligible countries since May 2020. Beyond offering temporary debt interest relief, the DSSI commits participating countries to disclose all public sector financial commitments and to limit non-concessional borrowing. The initiative has had a major impact in some African countries, such as Angola where total DSSI savings have accounted for 4.7 percent of GDP, or 5 percent in Mozambique and 5.7 percent in Djibouti. Even initially reluctant markets such as Kenya have eventually joined the initiative. Although the G20 has also called on private creditors to participate in the initiative on comparable terms, there has been little take-up by commercial lenders. The initiative has also failed to achieve its goal of reducing debt-service costs thus far, with potential savings estimated at only 1 percent of GDP from January.



The DSSI will officially end at the end of this year and from 2022 debt-service payments owed to official bilateral creditors will resume. For many African countries, the end of the DSSI will renew debt servicing risks, especially for countries suffering from slow economic growth and low revenues. In many instances, external debt has outpaced gross national income (GNI) and export growth. To offer continued relief to such countries, the G20 and Paris Club of official creditors late last year launched a Common Framework for Debt Treatments to restructure unsustainable debt situations and protracted financing gaps in DSSI-eligible countries. Ethiopia, Chad, and Zambia have already applied to the Common Framework, and the World Bank has urged low- and middle-income countries to consider restructuring their debts when the DSSI expires. Other African countries that are not DSSI-eligible, such as Sudan, have also begun debt restructuring talks with significant support from international financial institutions and partner countries like France.

According to the World Bank, the debt of low- and middle-income countries in sub-Saharan Africa increased to a record USD 702 billion in 2020, more than double the amount of ten years ago. The debt burden in the region rose 5.5 percent from 2019-2020 alone. In 2020, the debt to GNI ratio was above 100 percent in four sub-Saharan countries, including Mozambique, Zambia, Cabo Verde, and Angola. Meanwhile, the average debt-to-export ratio increased three times over a decade to 205.1 percent in 2020. Such data is hampered by a lack of transparency of debt in some countries, such as Zambia, Republic of Congo, and Angola, particularly in relation to loans issued by Chinese state banks and related companies. World Bank president David Malpass has often been critical of opaque Chinese lending terms in Africa and other emerging markets.



Debt and geopolitics

The Common Framework is likely to become a theatre of geopolitical rivalry between the US and China in coming months, as heavily indebted African countries such as Ethiopia, Zambia, and Chad apply for debt relief. Western bilateral, concessional, and commercial creditors will seek greater transparency into these countries' borrowing terms with China. These creditors will also seek to avoid a scenario where any debt relief offered under the Common Framework does not facilitate continued debt servicing and repayments to Chinese creditors, which has been a major stumbling block for the DSSI and other debt restructuring processes.

ZAMBIA PRESIDENT HAKAINDE HICHILEMA AND IMF MANAGING DIRECTOR KRISTALINA GEORGIEVA

The case of Zambia's opaque debt burden has been a discussion point for the US and the World Bank in trying to enhance transparency in emerging markets and to avoid the so-termed Chinese "debt trap." In October, Zambia's new government revealed that its external public debt had grown uncontrollably over the past decade to almost USD 15 billion by June this year, including money owed by state companies (see ZAMBIA: STEADY PROGRESS ON ECONOMIC RECOVERY AND DEBT SUSTAINABILITY). PANGEA-RISK has long assessed that Zambia's debts, in terms of Chinese project finance, were considerably higher than reported by its previous government. Similar unreported debts have tarnished relations between the IMF and countries such as Republic of Congo, Mozambique, Sierra Leone, and others.

Common Framework debt restructuring negotiations are a key indicator for other African countries and emerging markets elsewhere seeking debt relief. Unlike the DSSI, the framework is not solely focused on temporary relief from repayments associated with bilateral debt. Instead, there is a stronger focus on restructuring loans and allowances for cancellations in "the most difficult cases", although this is strongly discouraged. Creditor states such as China, Saudi Arabia, India, and Turkey are participants in the new framework. Applying countries need to undergo a debt sustainability audit and are required to sign up to an unspecified IMF programme. With these prerequisites in place – and the support of bilateral and multilateral institutions – debtor countries can then negotiate with bilateral, multilateral, and private creditors on restructuring terms.

Debt and climate change

KUSILE POWER STATION IN SOUTH AFRICA

In addition to funding to counter damage wrought by the coronavirus pandemic and to bolster its economic recovery prospects, Africa will need new funding to mitigate threats posed by climate change. The sub-Saharan region will also need as much as USD 50 billion each year over the next decade to adapt to climate change, according to the World Bank. While the continent is a relatively low producer of carbon emissions, it is the most vulnerable to environmental shifts due to its high reliance on rain-fed agriculture. Rising temperatures, sea levels and rainfall anomalies heighten the frequency and intensity of natural disasters.

The World Bank says that financing climate change adaptation is more cost-effective than frequent disaster relief and the region should "seize the climate opportunity to adapt and transform its economy", while adopting policies that foster sustainable and inclusive growth. Linking climate-related finance to governance reforms could help mobilise resources. The IMF has suggested that redirecting special drawing rights (SDRs) by wealthy countries to poorer ones should boost climate change adaptation. Yet, sub-Saharan Africa received only about 3.6 percent of the USD 650 billion in SDRs distributed by the IMF in August this year. Some countries like France have already committed to reallocating part of its SDRs to Africa, but few other wealthy nations seem keen to reallocate their SDRs.

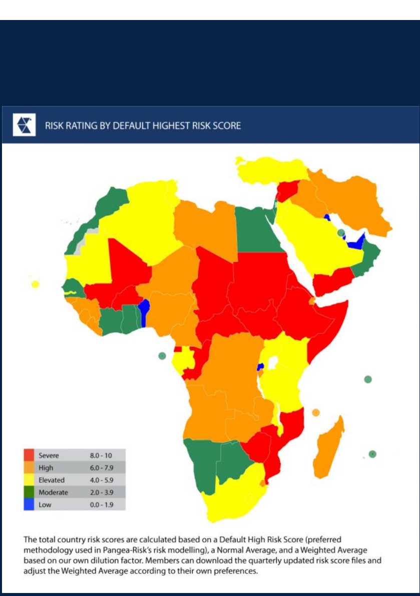
African countries are also pushing for a fairer share of the USD 100 billion a year that rich countries promised by 2020 to allocate to developing economies for adjustment to the effects of climate change. Until now Africa has had just 3 percent of that fund, with the bulk going to India and China. Many wealthy countries are falling behind on their payments to the fund and the issue will be a key theme at the upcoming COP26 summit. Climate change financing is more likely to come from further foreign direct investment, as well as additional borrowing through development finance. The European Union has promised to make Africa part of its 'Global Gateway', a new planned initiative programme, which the European Commission has heralded as its answer to China's 'Belt and Road' agenda. It is hoped that the European Investment Bank and other development finance institutions will generate the bulk of the lending in partnership with the private sector.

The world's most polluting power company, South Africa's Eskom is at the forefront of a new loan-financed strategy to boost climate change adaptation in Africa. The World Bank, the African Development Bank, and wealthy countries such as France, Germany, the UK, and EU are discussing a USD 5 billion financing package to fund Eskom's green power transition from a dependence on coal. Eskom relies on coal for around 90 percent of its electricity generation. The company has said its green transition will create 300,000 new jobs but cost USD 10 billion. Eskom already has debts of USD 24 billion, which are the greatest threat to South Africa's sovereign debt position. The company's investment status is also tarnished by corruption allegations with reports suggesting it awarded over USD 11.5 billion in corruption-tainted contracts over the past decade. Discussions on financing Eskom's green transition may therefore be hampered by a legacy of corruption and debt vulnerabilities with contagion risks to the sovereign.

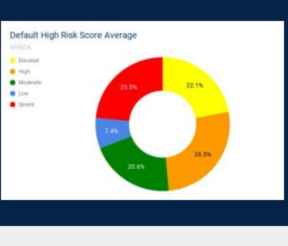
MEDUPI COAL POWER STATION IN SOUTH AFRICA

INSIGHT

Based on the outcome of the IMF and World Bank's annual meeting and their revised economic projections for African countries, PANGEA-RISK has updated its country risk scores. PANGEA-RISK has developed a unique risk scoring system for 68 African and Middle East countries that allows our members to compare ten individual risk perils for each country representing the macro political, economic, and security environment over a forecasted one-year outlook. These individual perils form the basis of our overall country risk ratings. Our risk methodology combines both a qualitative and a quantitative approach to assessing risk and is influenced by international best practice, such as the United Nations Security Risk Management Process, European Interagency Security Forum, and the World Economic Forum.



One of the biggest losers in the quarterly rankings is Ethiopia, which PANGEA-RISK now rates at a "Severe" risk rating for the first time since the start of the risk scoring in 2015. This risk rating downgrade is mostly due to economic volatility, fiscal imbalances, threat of sovereign default, prospect of sanctions, and mounting insecurity and civil unrest risks.



On the winning side, Zambia's rating has improved from "Severe" to "High" due to the new government's pro-business reforms, sensible mining sector policy, improved outlook for metals exports, and the prospect of debt restructuring, and an IMF programme being concluded by early 2022. Further improvements in Zambia's rating, though anticipated in coming quarters, will depend on progress in the Common Framework and implementation of promised structural reforms.