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MACROECONOMIC & MARKET OUTLOOK
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Macroeconomic and Market Outlook 2016[1]

1st Quarter, 2016

Highlights:

- The global economy decelerated to 2.4 percent growth in 2015, weighed down by the slowdown in developing and emerging market economies which overshadowed firming growth in high income countries.
- Global growth could marginally pick up in 2016, lifted up by strong impetus from high income countries (US, Europe and Japan), but is subject to downside risks.
- Developing and emerging market economies are facing headwinds from declining commodity prices; weakening global trade amid the slowdown in China; the rise in US interest rates, which is inducing capital outflows in emerging markets; USD appreciation and volatility in global financial markets.
- African countries are largely buffeted by the slowdown in China, declining commodity prices and the effects of the hike in the US interest rate.
- The commodity price super-cycle ended, marked by a steep plunge in oil prices and other commodities, amid excess supply in the face of weak demand. The oil supply glut seems to be persisting as supply still outpaces demand, further depressing prices in the medium term. Recovery in oil prices is expected to be much slower and oil prices could average at or reach below the $50-60 per barrel range in 2016, and remain below $70 per barrel until 2018 in the absence of major geopolitical turmoil.
- The diverging monetary policy stances of major central banks, financial market sentiment and developments in China will largely influence financial conditions in developing and emerging economies.
- The hike in the US interest rates is appreciating the USD, raising the cost financing, inducing capital outflows from emerging market economies and heightening volatility in emerging market economies.
- The macroeconomic outlook is less robust than what it was a few months ago, with risks tilted to the downside. Key risks to monitor are: China's economic slowdown, commodity price weakness, renewed financial market volatility following the US tightening of monetary policy and the recent China equity volatility, possible escalating geopolitical risks in the Middle East, election-related political tensions in Africa, and El Nino related unfavorable weather conditions affecting parts of Africa (and other parts of the world).
- Despite attendant risks, there are ample investment opportunities in Africa, especially in infrastructure development.

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Global Macroeconomic Outlook

The global economy has slowed down to an estimated growth of 2.4 percent in 2015, from 2.6 percent in 2014, weighed down by continued deceleration of activity in emerging and developing countries which have been buffeted by the decline in commodity prices, the slowdown in China which has weakened global trade, and subdued capital flows[2]. This has largely overshadowed activity pick-up in high income countries. Growth in high income countries is led by firming activity in the United States, and return to positive growth in Japan as well as modest recovery in the Euro Area. However, lower growth in some commodity exporters (Canada and Norway), is tempering the high income growth impetus, amid depressed commodity prices.

The US economy is solidifying further, with recent data showing strengthening labour markets, muted inflation, and robust services sector and improving consumer spending including the housing market[3]. US growth could rise to 2.8 percent in 2016 from 2.5 percent in 2015, supported by lower energy prices, reduced fiscal drag and an improving housing market. The Federal Reserve Bank raised its policy interest rate – the Federal Funds Rate – by 0.25 percentage points on 16 December 2015, for the first time since 2006, as the new monetary policy cycle begins. Growth in the Euro Area is helped by lower oil prices, accommodative monetary policy and currency depreciation. Deflationary concerns are easing but wage growth remains subdued. The ECB has extended the quantitative easing (US$60 billion monthly bond purchase programme) to March 2017 and cut deposit rates to -0.3 percent from -0.2 percent, providing support to growth.

Global growth is projected by the World Bank to edge up to 2.9 percent in 2016 and 3.1 percent in 2017.[4] In our view this growth projection could be more optimistic given the inherent risks in developing and emerging markets. We believe growth could pick up marginally to a level somewhat below 2.9 percent, supported by stronger recovery in the US and Euro Area as well as firming Japan's positive growth, offsetting the weakening in commodity exporting economies somewhat. Global inflation is also expected to tick up as commodity prices stabilize later 2016.

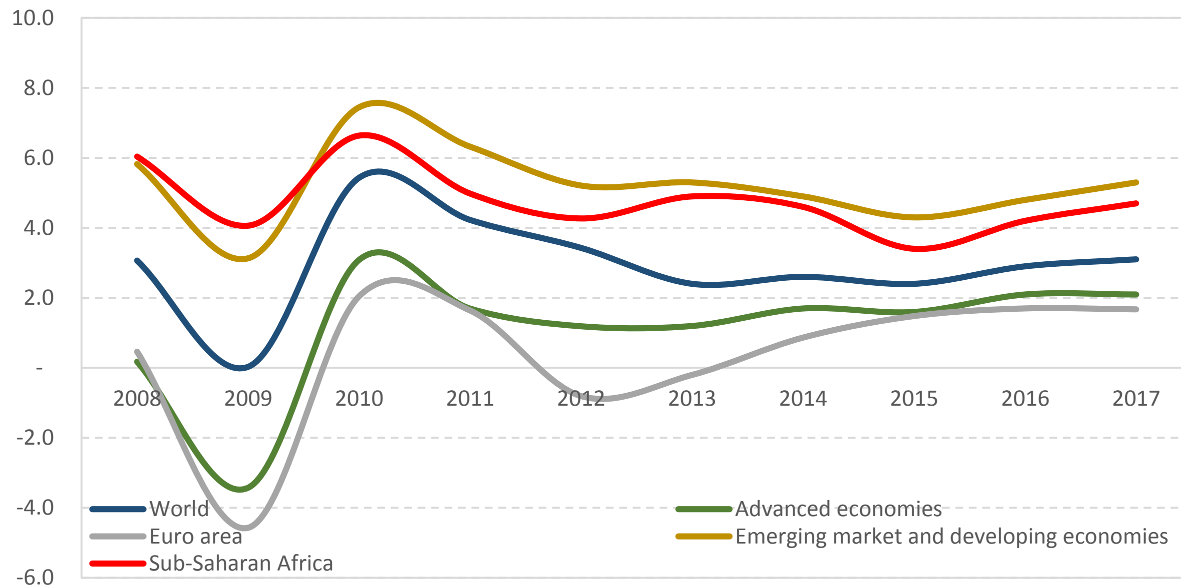
Developing and emerging market economies growth decelerated in 2015 to 4.3 percent from 4.6 percent in 2014, held back by subdued growth in major emerging market economies: China, Russia and Brazil, and South Africa. The key headwinds facing emerging and developing countries includes: the decline in oil and other commodity prices; weak global trade amid the slowdown in China; financial markets volatility in the run up to the increase in US interest rates in December, decrease in capital flows and rapid strengthening of the US dollar. Developing countries growth is projected to increase to 4.8 percent in 2016 and 5.3 percent in 2017, as some of the headwinds relent somewhat.

[2] World Bank, Global Economic Prospects, January 2016

[3] Federal Reserve Bank data, 2015.

[4] World Bank, Global Economic Prospects, January 2016

Figure 1: Global Growth and Projections



Source: IMF and World Bank

The structural shifts in the Chinese economy are causing concerns. China's growth has slowed down to 6.8 percent in 2015[5], its lowest growth rate in 25 years, as the economy transitions from an investment and export-led growth strategy to the new growth model led by domestic consumption and services. The rebalancing of the economy while sustaining aggregate demand, is proving to be painful and challenging. Amid the slowdown of the economy, the Shanghai stock market tumbled by more than 30 percent between June and December 2015. It further slid by 12 percent in the week of 4 -8 January 2016, triggering twice the so called "circuit breakers"- a mechanism that halts trading when shares falls steeply.[6] The yuan was devalued in August 2015, sparking a wave of depreciations of many emerging market currencies with trading links to China. It weakened further by 1 percent against the US dollar in the first week of January 2016, a development that could spark another global sell-off in risky assets.[7]These events have raised concerns about the health of the Chinese economy, signaling the beginning of a transition to a "new normal" growth rate for China, widely expected to be around 5 percent. However, the possibility of hard landing is unlikely, as Chinese authorities have policy levers to intervene and ensure a gradual rebalancing.

Brazil is battling with a recession on the back of declining commodity prices, continued weak investor confidence, and rising price inflation. Output is projected to contract by 3 percent in 2015 and further 1 percent in 2016. Russia is going through a severe adjustment in the face of external shocks, sanctions and geopolitical concerns. The economy contracted by 3.8 percent in 2015 and could contract by -0.7 percent in 2016. Economic activity in commodity exporting EMEs such as Mexico, Ukraine, Malaysia, Venezuela, Chile, South Africa and others is buffeted by the decline in commodity prices. However, net oil importers such as India, Turkey, Indonesia, Hungary, Kenya and others are benefiting from lower oil prices. India is outpacing

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[5] IMF, World Economic Outlook, October 2015

[6] http://www.nytimes.com/2016/01/08/business/international/a-new-economic-era-for-china-goes-off-the-rails.

[7] MRB Partners Report, January 2016

other EMEs, with robust growth of 7.3 percent in 2015 and projected 7.8 percent in 2016, propelled by strong investor confidence, low oil prices and credible policies from reform minded government.

With the lift-off of US interest rates in December, some emerging market economies are experiencing capital outflows, currency depreciations and increases in borrowing costs. Significant tensions in the financial markets were experienced in the run-up to the rate increase, especially in August, with the confluence of the crash in the Chinese stock market and devaluation of the Yuan and continued weak commodity prices. The broader weakness in commodity prices is expected to continue in 2016, maintaining pressure on commodity exporters. The diverging monetary policy stance of major central banks, financial markets sentiment and developments in China will continue to influence financial conditions in developing and emerging economies.

Macroeconomic Outlook for Africa

Growth in Sub-Saharan Africa (SSA) is expected to slow to 3.4 percent in 2015 from 4.6 percent in 2014, largely reflecting the growth slowdown in large economies (Nigeria, South Africa, and Angola). The key headwinds weighing down on growth are: the plunge in oil prices, the slump in other commodity prices, and the slowdown in China, decline in capital flows and power shortages. The decline in oil prices has considerably reduced growth in oil exporting countries (such as Angola, Nigeria, Cameroon, Congo Republic and Equatorial Guinea), and even slowed down economic activity in non-oil sectors in these countries due to backward and forward linkages. Prices of commodities such as metals and agricultural raw materials have also been declining since June in tandem with oil prices, weakening growth in most commodity exporting countries such as Burkina Faso, Sierra Leone, Zambia, Ghana, South Africa and others. The slowdown in China has also impacted on commodity exporters through reduced exports and a subsequent squeeze in fiscal revenues and widening fiscal deficits. Inflation remain moderate for many countries, except for some few countries (e.g. Ghana, Zambia and Angola), where it doubled digits.

On the outlook, SSA growth could firm up to 4.2 percent and 4.7 percent in 2016 and 2017 respectively, supported by the recovery in the global economy which could support a moderate increase in external demand, a modest recovery in oil prices later in 2016 which would benefit oil exporters. Improvement in domestic demand and continuing infrastructure investment will also support growth in some countries.

Table 1: Macroeconomic Indicators for Sub-Saharan Africa

	2008	2009	2010	2011	2012	2013	2014	2015E	2016F
Real GDP Growth (%)	6.3	4.1	6.9	5.1	4.1	4.1	4.6	3.4	4.2
Nominal GDP (USD Billion)	1077	1019.1	1275	1428	1526.3	1607	1670	1560	1639.8
Inflation (%, yoy ave)	13	9.8	8.2	9.5	9.4	6.6	6.4	6.9	7.3
Oil production (mbpd)	5.6	5.4	5.4	5.4	5.6	5.2	5.1	5	5.4
Net FDI (% of GDP)	2.1	2.8	2.7	2.1	2.0	1.3	1.3	2.1	2.5
Fiscal Balance	0.7	-4.6	-3.4	-1.1	-1.8	-3.1	-3.5	-4.3	-3.6
Total Public Debt (% of GDP)	24.1	29.7	27.7	28.3	28	29	29.9	30.7	31.2
CA Balance	-0.2	-2.8	-0.9	-0.7	-1.9	-2.4	-4.1	-5.7	-5.5

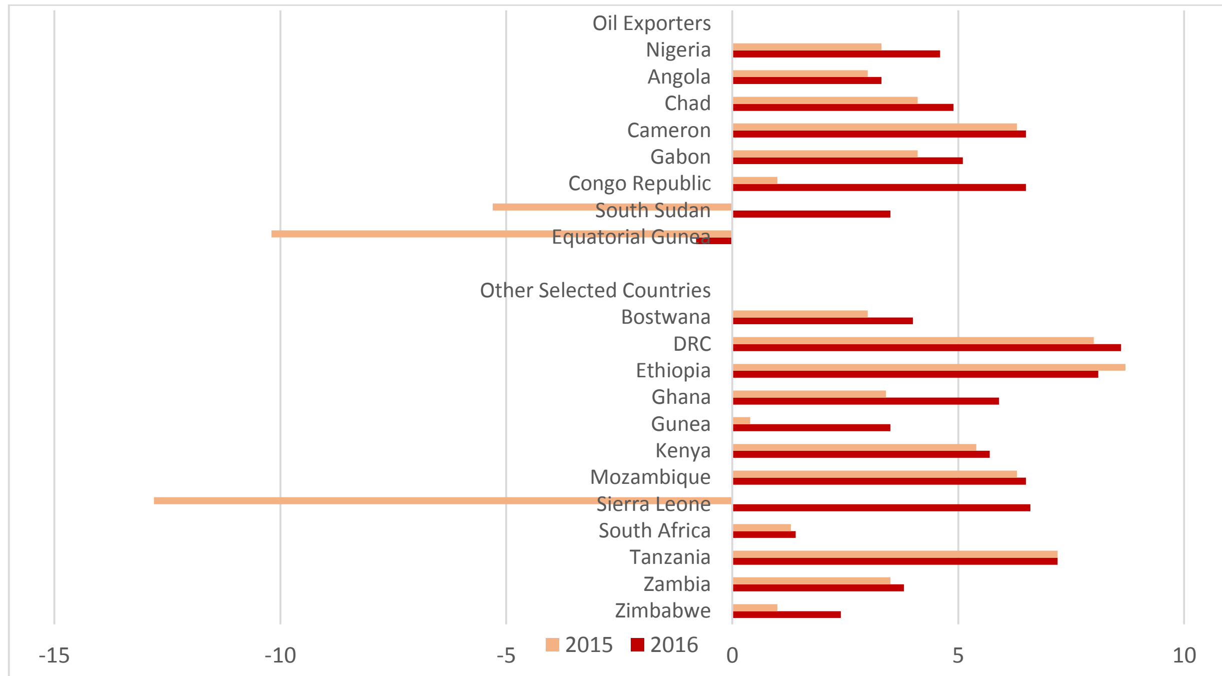
Sources: AFDB, IMF, World Bank

Nigeria's growth is edging down to 3.3 percent in 2015, largely dampened by the decline in oil prices and capital outflows. The fiscal position remained tight throughout 2015, as expenditures (especially capital expenditures) were cut to match the decline in revenues from the oil sector. The naira remains under pressure from the appreciation of the dollar, and the increase in US interest rates which triggered capital outflows from emerging market economies and raised the cost of borrowing. Foreign exchange reserves fell 20 percent to $34.25 billion (6.0 percent of GDP) as the Central Bank drew down the reserves in an attempt to defend the Naira under the managed floating exchange rate system. The Nigerian Central Bank implemented some administrative measure to stabilize the naira. Economic activity slowed markedly in the first half of 2015, as uncertainties surrounding the elections and subsequent political transition, fuel and power shortages, increases in import costs, and fiscal consolidation weighed on non-oil sectors. Nigeria's growth is projected to edge up to 4.3 percent in 2016 and 5.3 percent in 2017, as the fiscal drag moderates, activity in the non-oil sector improves, and the new government works on tackling corruption and implements structural reforms to enhance productivity.

Angola, the second biggest producer of oil in Africa, is seeing its growth slowing down to 3 percent in 2015, dampened by the decline in oil prices. Growth is forecast to improve to 3.3 percent in 2016 and 3.8 percent in 2017.[8] Oil accounts for 95 percent of total exports and 80 percent of fiscal revenues. The government presented a US$48 billion budget for 2016 based on the oil price of $45 per barrel and daily production of 1.8 million barrels. Facing external pressures, the budget deficit could widen to 5.5 percent in 2016 from 3.5 percent in 2015. The kwanza depreciated by 16 percent in January 2016, heightening inflationary pressures, which could rise above 12 percent in 2016. A lot of pressure is exerted on the foreign exchange reserves which have fallen to an estimated US$19 billion in 2015 from US$27.2 billion in 2014. Angola issued a US$1.5 billion sovereign bond in November 2015, which was oversubscribed. The rise in US interest rates could see the cost of servicing debt increasing.

[8] [8] IMF, World Economic Outlook, October 2015

Figure 2: Growth estimates and forecasts for selected African countries, 2015 and 2016



Source: IMF and World Bank

Following a 1.5 percent growth rate in South Africa in 2014, 2015 growth is estimated at 1.3 percent. Economic activity is held back by both external and domestic headwinds: lower commodity prices, energy shortages, supply bottlenecks, weak investor sentiment amid policy uncertainty, output contraction in agriculture following a severe drought in the summer, and tense labour relations. The South African rand depreciated by more than 45 percent since January 2015. Inflation is hovering around the upper target band of 6 percent. The outlook for 2016 is uncertain as economic activity is still subdued. Growth is projected at 1.4 percent in 2016. The country's credit rating was downgraded in December after the unexpected change of finance minister, while the balance of payment pressures continues amid capital outflows in the wake of the increase in US interest rates in December 2015.

Fiscal consolidation, power shortages, a slump in the cocoa harvest and the decline in oil prices continues to hamper Ghana's growth (3.4 percent) in 2015. Ghana cedi weakened more than 30 percent since June 2014, reflecting low commodity prices and loose fiscal and monetary policy. Ghana issued a US$ 1 billion sovereign bond, its fourth issue, which was oversubscribed by more than 100 percent, reflecting high appetite for its credit. In Zambia, economic activity is constrained by subdued copper prices, high interest rates, and severe electricity shortages. From 3.5 percent in 2015, growth could pick up to 3.8 percent in 2016 on the back of improvements in the regulatory environment enhancing the outlook for investment in the mining sector.[9] Other frontier-market economies such as Côte d'Ivoire, Kenya, and Senegal are anticipated to grow at robust paces, supported by strong infrastructure investment and credible policy fundamentals.

In the Franc Zone, the depreciation of the Euro against the dollar has further weakened the CFA Franc, helping to smooth the adjustment to the oil price shock. In some low income countries,

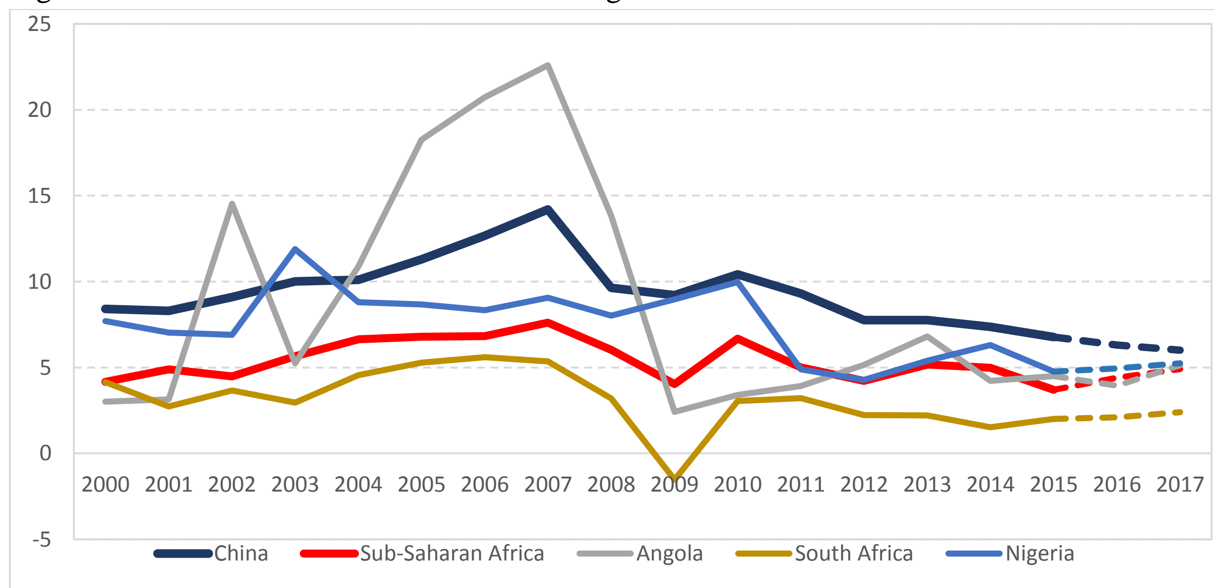
[9] African Economic Outlook, 2015

growth is holding up, supported by infrastructure (Rwanda, Ethiopia) and mining expansion (DRC, Mozambique and Tanzania), agricultural growth (Ethiopia) and consumer spending (Uganda). These countries are anticipated to register growth of 7 percent or more in 2015 and 2016[10]. Guinea, Liberia, and Sierra Leone are recovering as the effects of the Ebola crisis wane. Poor weather conditions, emanating from the expected persistence of the El Nino effect, will reduce agricultural output in Southern and Eastern Africa in 2016.

Impact of the slowdown of China

The slowdown in China is a source of growth concerns for developing countries, especially in Africa. China is Africa's largest bilateral trading partner which has propelled African growth in recent years. The impact of its slowdown on African countries will vary, depending on whether they are exporters or importers, the share of exports/imports and the types of goods being exported/imported. China accounts for more than half of total exports, largely commodities in Sierra Leone, Gambia, Mauritania, Congo Republic, Angola, Chad and South Sudan. As such, the continued slowdown could significantly reduce exports, widen current account and fiscal deficits and retard growth. Its slowdown will also see a decline in investment flows in African countries such as Nigeria, South Africa, Ethiopia, Kenya, Uganda and Zambia.[11] Some projects may be delayed while financing for infrastructure could be curtailed. Estimates suggest that a 1 percentage point decline in China's investment growth reduces SSA`s exports growth by 0.6 percentage points.[12] For many years, SSA growth has largely mirrored that of China as shown in Figure 3.

Figure 3: China and Sub-Saharan Africa GDP growth: 2000-2015



Source: IMF

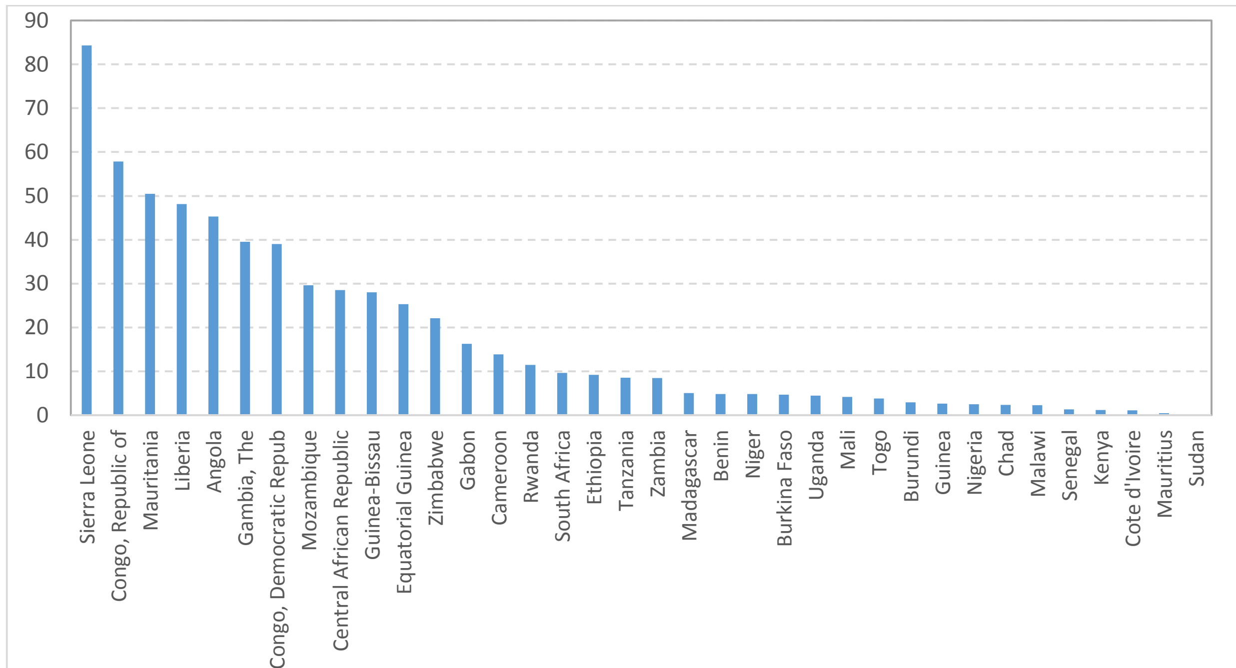
[10] World Bank, Global Economic Prospects, January 2016

[11] UNCTAD (2013 "World Investment Report: Global Value Chains: Investment and Trade for Development." UNCTAD/WIR/2013, Geneva

[12] Drummond and Liu (2013), Africa's Rising Exposure to China: How Large are Spillovers through Trade? , IMF Working Paper No 13/250

The effects of the slowdown in China will be transmitted directly through lower exports from Africa and indirectly through lower commodities prices. China's slower growth has pushed down prices of gold, crude oil, copper, platinum and iron ore, as it accounts for 12 percent of global oil demand, 70 percent of global demand for iron ore and 45 percent of global demand for copper.[13] For countries where exports to China account for a very significant share of total exports, such as Angola, the Democratic Republic of Congo, the Republic of Congo, Sierra Leone, Mauritania, and Gambia the effects of the slowdown are huge (Figure 4).

Figure 4: Sub-Saharan Exports to China, 2014 (percentage of total exports)



Source: IMF, Direction of Trade Statistics

The faltering Chinese economy has triggered a slump in the country's stock market by more than 30 percent from June 2015 up to the end of the year. The stock market slumped again by about 12 percent in the first week of January 2016. The yuan was devalued by about 4 percent in August 2015, the biggest fall in its value since 1994, sparking fears of stagnation of the economy and compounding the stock market decline. Such exchange rate readjustments have strong implications for African economies. The devaluation has unleashed volatility in the global financial markets and weakened currencies especially of African commodity exporters such as South African Rand, Angolan Kwanza, Nigeria Naira and Zambian Kwacha as concerns about China's outlook intensify. The dawn of 2016 saw another mild devaluation of about 1 percent in the first week of January, following the slump in the Chinese stock exchange.

Oil Markets

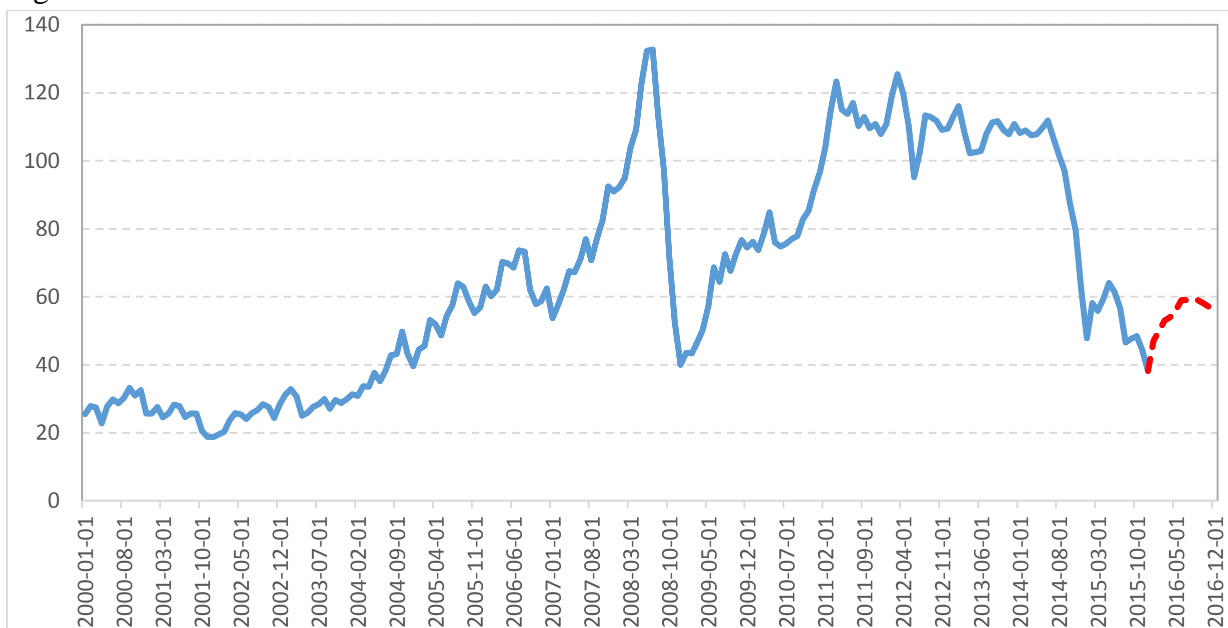
Oil prices have plunged by over 70 percent since June 2014, due to the surge in unconventional oil production in North America, especially the US, OPEC`s policy of moving from price targeting to market share, and improved production in some key producers in the Middle East (notably Iraq and Saud Arabia) and other major producers (Russia and Brazil). These factors

[13] International Energy Agency

were amplified by a sharp appreciation of the U.S. dollar (which reduces the dollar-denominated oil price) and abating geopolitical risks, especially in Iran. Iran recently announced plans to increase oil production by 500 000 b/d starting early in 2016, following the lifting of sanctions. Iraq and Russia also announced plans to increase production. In the wake of these announcements, coupled with the rise in US interest rates, oil prices have further slumped below $40 per barrel in December for the first time since 2009.

Oil prices averaged $52.3 per barrel in 2015 and are expected to recover marginally to $56/bbl in 2016, but remain below $70 per barrel until 2018, the absence of geopolitical turmoil (Figure 5).[14] The pace of the recovery in oil prices will largely depend on the speed at which supply will adjust to current market conditions. The following factors will shape the oil market outlook: geopolitical events in the Middle East (in particular increasing involvement of foreign powers in Syria, and conflict in Iraq), possible decline in US tight oil production, the timing and size of Iran's increase in oil exports, and demand growth in emerging market economies, especially China (China could continue to fill its strategic reserves in 2016, taking advantage of low prices).

Figure 5: Brent Oil Prices and Forecast



Source: EIA

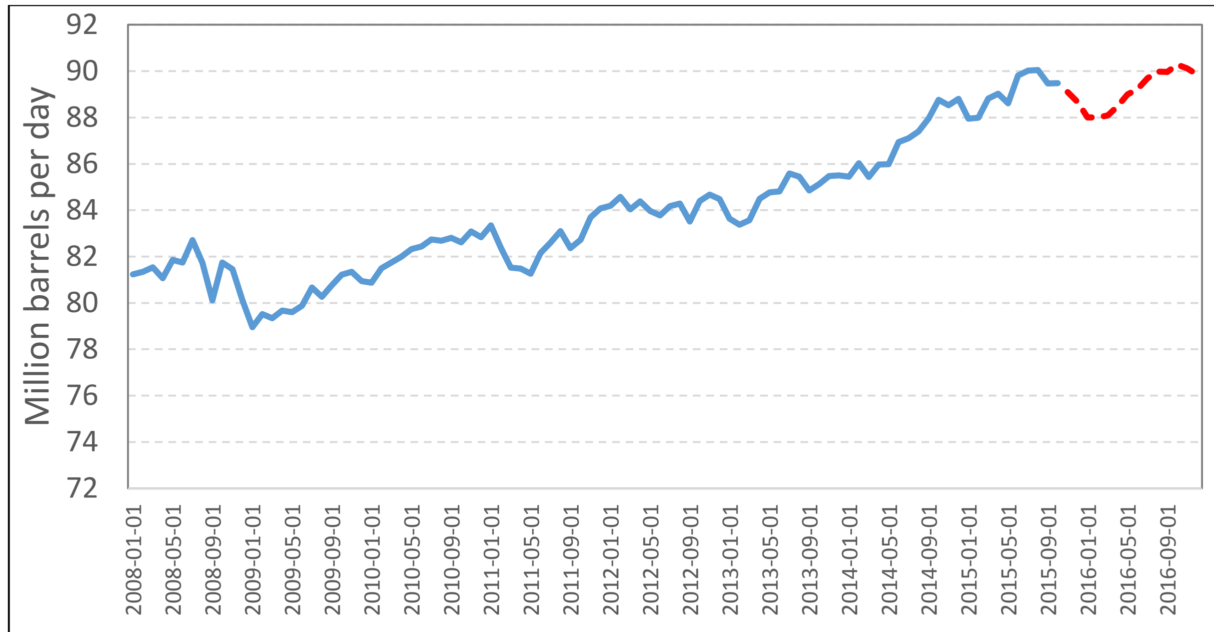
US oil production has already declined by about half a million barrels per day (mbpd) since peaking at 9.6 mbpd earlier in 2015, and the Energy Information Administration (EIA) expects further declines to about 8.8 mb/d in 2016, as drilling activity has fallen dramatically since 2015 (Figure 6). OPEC has been producing about 1.7 mb/d above its nominal 30 mb/d ceiling in recent months, contributing to the glut in supply.[15] Non-OPEC output could fall by 0.5 mb/d in 2016 due to lower oil prices and steep investment spending cuts. In general, global oil production is expected to decline slightly in the coming months before picking up in the second quarter of 2016. The supply glut of approximately 1.8-2 mb/d is anticipated to continue into

[14] Energy Information Administration (EIA); World Bank

[15] Energy Information Administration (EIA)

2016, and could put further downward pressure on prices. The EIA sees oil demand growing by 1.4 million barrel per day (mb/d) in 2015 and in 2016. The International Energy Agency (IEA) is more bullish and sees oil demand growing by 1.8 mb/d in 2015 and 1.2 mb/d in 2016.

Figure 4: Oil Production and Forecasts



Source: EIA

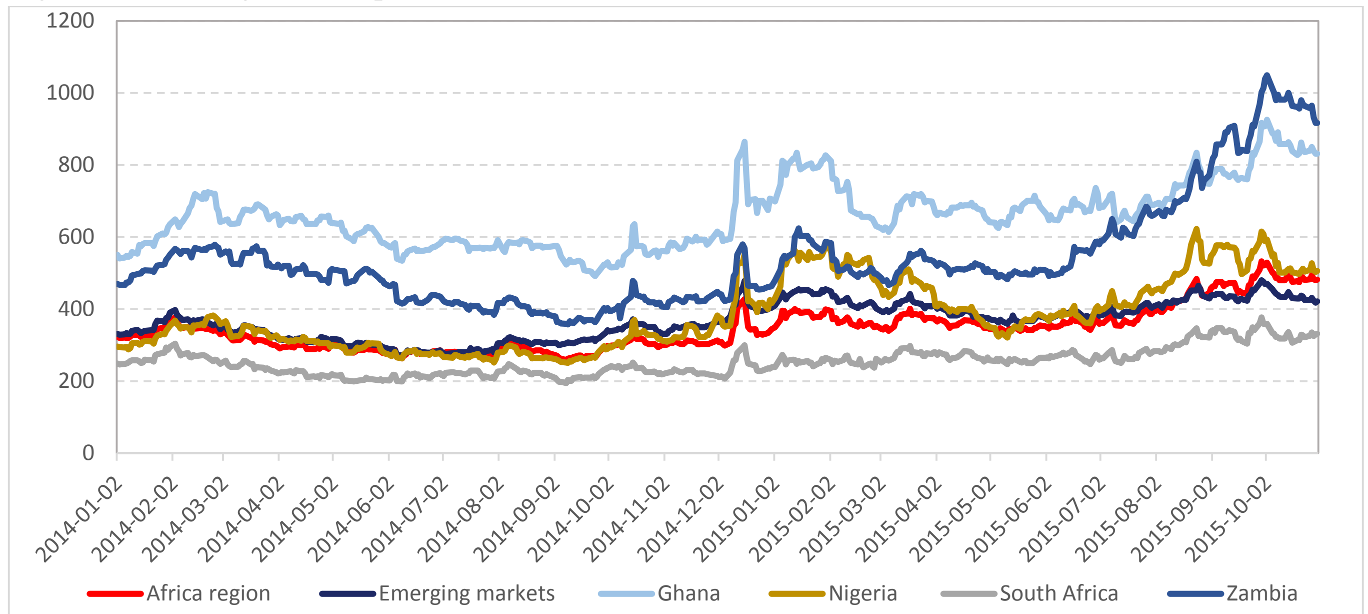
The decline in oil prices is significantly shaping the macroeconomic outlook of many African countries. In oil-exporting countries, lower prices are negatively affecting economic activity and putting pressure on current accounts, fiscal balances and exchange rates. The hardest hit are the less diversified oil exporters, such as Angola and the Republic of Congo. Many African governments are cutting spending to offset falling fiscal revenues, but are confronted with a policy dilemma for their monetary policy in the face of depreciation pressures and rising inflation. The oil price induced growth decelerations in oil-exporting countries are also exacerbating corporate balance sheet strains and raising nonperforming loans. In oil importing countries, low oil prices are boosting consumption and investment, and reducing inflationary pressures, while narrowing fiscal and external positions to some extent and helping to reduce vulnerabilities. This is creating policy space for central banks to cut interest rates to support economic activity. The disinflationary impact of lower oil prices however is expected to be transitory, possibly fading away in 2016.

Financial Markets

In the run-up to the US interest rate hike in December 2015, global financial markets experienced marked volatility, which intensified in August with the decline in the Chinese stock market, devaluation of the Yuan and appreciation of the US dollar. Equity and currency markets were particularly affected with significant depreciation especially in commodity exporting countries. Sovereign bond spreads widened markedly especially in African countries (Figure 7). Since 2007, a lot of SSA countries such as Zambia, Ethiopia, Rwanda, Kenya, Ghana, Senegal and Ivory Coast have issued sovereign bonds worth over US$24 billion. With the

expectation of the increase in US interest rates, the cost of borrowing increased sharply in 2015 for many sovereigns. For example, Ghana issued US$1 billion (15 year tenure) at 10.75 percent and Zambia issued US$1.25 billion at 9.375 percent (11 year tenure on average) and these rates are much higher than previous issues. The spreads on African countries' sovereign bonds have widened over uncertainty about government policies and slowdown in the economies. Spreads are higher in countries where market confidence is weakest.

Figure 7: Sovereign Bond Spreads



Source: Bloomberg.

Impact of US interest rate hike

After more than 12 months of anticipation, the US Federal Reserve Bank raised its benchmark short term interest rate, the Federal Funds rate by 0.25 percent on 16 December, 2015. Emerging and developing countries are affected, but the impact is limited and benign compared with the tapering of monetary policy (quantitative easing) in 2013 because of several factors: (i) The current rate hike was well communicated and widely anticipated for some time, smoothening adjustment (ii) the magnitude of the rise is widely in line with market expectations and the rate hike has been adjusted for, (iii) the tightening is taking place at a time when other major central banks such as ECB and Bank of Japan are easing their monetary policy stances, such that global liquidity conditions are less affected, and (iv) and the Fed highlighted that further rate adjustments will be gradual.

The rise in US interest rates is expected to dampen capital flows to emerging markets as US markets become more attractive for global investors looking for stable and safe returns. The most vulnerable countries are those with large external financing needs, large stocks of inward foreign portfolio investments (shares and bonds), high foreign currency debt levels, small foreign exchange buffers, and low monetary policy credibility. A number of emerging market economies such as Brazil, Indonesia, Malaysia, Colombia, South Africa and Turkey[16] are

[16] Atradius Economic Research, 2015

heavily relying on foreign capital inflows to fund fiscal or current account deficits. Between 2009 and 2013, emerging market economies received about US$4.5 trillion of gross capital inflows, representing about half of all global capital flows in that period.[17] The World Bank estimates that a 50 basis points jump in global long term interest rates could temporarily reduce aggregate capital flows to developing countries by 0.9 percentage points of their combined GDP.[18]

With the expectation of subsequent rate increases, as this is the beginning of the tightening cycle of the monetary policy, the US yield curve could steepen as the long term interest rates are expected to increase. This could result in a surge in borrowing costs in emerging markets and further straining corporate balance sheets. Also, as the rate hike induced further appreciation of the US dollar, contributing to rising cost of debt refinancing and upsetting growth. The impact could be more acute in countries that have large borrowings denominated in US dollars and countries with heightened domestic challenges such as Brazil, Mexico, Russia and Turkey. The Brazilian Real depreciated by 1.5 percent, while the Mexican Peso, Columbian Peso, the Russian Rubble and the South African Rand depreciated by 1.4 percent, 4.1 percent, 3.7 percent and 3.7 percent respectively following the hike in the US interest rate. However, in countries that trade more with the United States, such as Mexico and others in Central America, the negative impact will be partially offset by an increase in their exports emanating from the depreciation of their currencies. Also considering that market liquidity is still fragile, the impact of the initial shock may be amplified and propagated to other market segments, such as sovereign bonds markets.[19]

The appreciation of the dollar due to the interest rate hike also affects the oil market. The Brent crude oil price fell by 3.2 percent on the announcement of the rate hike, and further slid below $32 per barrel in January, the lowest price level in 12 years. The dollar is closely linked to the oil market in two ways. First, oil is priced in US dollars, such that appreciation of the US dollar would reduce the purchasing power of oil importing countries and, at the same time, impact revenues for exporters. Secondly, due to the interconnectedness of the currency and commodity markets, a stronger dollar prompts speculative traders to sell oil futures and other commodities and buy more of the U.S. currency, thus effectively dampening oil prices. Oil exporters such as Russia, Nigeria, and Venezuela will continue to feel the pain.

Although bond spreads widened on the hike, the equity markets actually rallied, reflecting confidence in the US economy and the global economy in general. The MSCI emerging markets index leaped up by 0.6 percent while the Shanghai composite index climbed 1.8 percent on the Fed's announcement.

For African countries, the impact of the US interest rate hike will largely impact countries that have borrowed in international capital markets through sovereign bonds. Many African countries such as Zambia, Ethiopia, Rwanda, Kenya, Ghana, Senegal and Ivory Coast, have borrowed in international capital markets in recent years through sovereign bonds. As such,

[17] IMF World Economic Outlook, October 2015
[18] World Bank, Global economic prospects, January 2016.
[19] World Bank, Global economic prospects, January 2015.

further tightening of financial conditions could make financing more expensive, depending on the extent of debt that is denominated in US dollars. Most African countries are already reeling under the effects of the decline in oil and other commodity prices. With further dampening of oil prices following the hike, oil exporters such as Nigeria, Angola, Cameroon, Equatorial Guinea, Congo Republic and others will feel the pinch as export revenues decrease and fiscal budgets are squeezed.

Further strengthening of the US dollar emanating from the rise in US interest rates could weaken African currencies. Countries with ballooning debt and high exposure to global markets, such as Ghana, South Africa and Angola, are most vulnerable, while other countries including Ethiopia and Kenya which have some buffers may cope with the shock somewhat.

Key risks to monitor

Risks to the outlook remain tilted to the downside. A protracted decline in oil prices could further weaken growth and revenue in oil-exporting countries, requiring them to undertake deeper fiscal adjustments with sharper expenditure cuts. Further declines in other commodity prices could continue to upset growth in commodity exporting countries, straining corporate balance sheets and further raising non-performing loans. Some oil companies may delay or even cancel planned investments in 2016. Investors should continue to monitor weak links in the world economy, especially commodity contagion and imbalances in major financial centers.

Further tightening of the US monetary policy in the medium term after the start of the monetary policy tightening cycle in December could continue to appreciate the US dollar, increase financing costs, heighten risk aversion and reduce capital flows in developing countries. The impact could be pronounced in the Africa region’s frontier markets (Zambia, Ethiopia, Rwanda, Kenya, Ghana, Senegal and Ivory Coast, Angola), which have recently issued Eurobonds to finance their large investment needs. Renewed tensions in the global financial markets is another risk to watch. The sharp decline of stock markets in China in the opening of trading in January 2016, resulting in halting of trading twice in one week could induce turbulence in the global financial markets.

The continued slowdown in China could be a chronic drag to growth in many African countries. A sharper-than-expected and protracted slowdown in China could lead to renewed weakening of oil and other commodity prices, fueling further contraction in economic activity in commodity exporting countries. The persistent slump of the Chinese stock market and further depreciation of the yuan could continue to induce volatility and dampen the outlook for African countries.

Geopolitical risks require careful monitoring. Tensions in the Middle East (especially in Syria and Iraq) and parts of Africa remain difficult, amid continued civil war in these countries and terror attacks in various parts of the world. These geopolitical tensions will take a heavy toll on economic activity, transactions costs, confidence, travel and tourism and heightened risk aversion. This is further complicating the migrant crisis in Europe, amid differences among members on how to deal with it. The EU is also facing uncertainty, with the United Kingdom

set to hold a referendum on whether to withdraw. Its withdrawal could weaken the union and affect trade flows and economic prospects.

Political factors associated with elections in a number of countries are key risks for Africa. Recent elections proceeded well in some countries such as Nigeria, Tanzania and Cote D'Ivoire, strengthening confidence over maturing democracies and improving political stability on the continent. However, elections in Burundi and Burkina Faso were mired by violence, while the situation in South Sudan remains volatile. In Libya, conflicting factions are disrupting oil installations and the Islamic State insurgency is growing. Boko Haram insurgencies remain a constant threat in Nigeria and its neighboring countries-Cameroon, Chad, and Niger. These acts of violence hamper economic activity, while diminishing the prospects for foreign direct investment. Planned elections to monitor in Africa in 2016 are in Uganda, Niger, Benin, Chad, DRC, Gabon, Equatorial Guinea, Ghana, and Gambia.[20]

Unfavorable weather conditions, driven by the El Nino phenomenon, are a threat to food security and agriculture growth in Southern and Eastern Africa in 2016. In Southern Africa, more than 30 million people could face food shortages in 2016.[21]

On the upside, the benefits from lower oil and non-oil commodity prices could boost demand. Cheaper fuel has helped to reduce inflation and improve current account deficits in some countries, while a weaker yuan could benefit importers of capital goods and intermediate goods (e.g. Kenya, Mozambique, and Ethiopia). Lower oil and other commodity prices could provide some upside to demand in commodity importers, but complicate the outlook for commodity exporters, some of which already face strained initial conditions.

Investment opportunities in Africa

Despite attendant risks, investment opportunities remain visible in Africa. The huge infrastructure gaps presents ample opportunities. Recent estimates shows that about US$93 billion is required annually to meet the infrastructure needs of the continent, but only half of that amount is currently being met.[22] Booming population growth and increasing life expectancy across the continent is pushing up demand for utilities such as water, power and roads, which few countries are providing in sufficient quantities. This presents huge investment opportunities.

As the African continent is also undergoing rapid urbanization, with a relatively young labour force and a growing middle class, it is proving to be a new emerging market and destination for investment. The number of middle-class households in the region has tripled in the last 30 years, and is still expected to grow further.[23] The middle class consumers have swelling disposable incomes, and represent expanding workforce, and a growing market for goods and services.

[20] National Democratic Institute: https://www.ndi.org/electionscalendar

[21] IRIN NEWS: http://www.irinnews.org/report/102317/an-unwanted-guest-el-niño-and-africa-in-2016

[22] Foster. V and Briceño-Garmendia, C. (2010) Africa's Infrastructure, A Time for Transformation, Africa Infrastructure Country Diagnostic, World Bank, Washington, DC.

[23] African Development Bank (2011). The middle of the Pyramid: Dynamics of the middle class in Africa, Market Brief

According to McKinsey (2010), the overall purchasing power of the populations of the 18 largest cities in Africa could amount to USD 1.3 trillion by 2030.[24] The effect is already manifesting in fast growing consumer sectors: telecommunications, banking, tourism and other service sectors are growing at rates 2-3 times faster than in the OECD countries. New technology adaptation is growing very fast and driving growth of consumer industries and altering the way Africans interconnect, shop and socialize.

With about half of the world's arable land, Africa's agriculture presents ample opportunities. Opportunities range from irrigation, development of advanced seeds, to fertilizers and other inputs. Recent discoveries of oil and gas in some African countries (e.g. Kenya, Uganda, Mozambique) is also opening opportunities in real estate, construction and hotels, accommodation and other services. With great need for industrialization and diversification, opportunities are also vast in creating industrial clusters to increase value addition in resource sectors and agro processing value chains.

Policy implications

The confluence of low oil prices and other commodities prices, the slowdown in China and developments in global financial conditions and other risk factors are raising multiple challenges and opportunities for African countries that lead to different policy responses. In oil importing countries, lower oil prices could ease constraints and pressures on prices, creating policy space for central banks to cut interest rates to support economic activity. The accommodative monetary policy need to be augmented with macro prudential policies to contain financial risks. However, for oil exporters, instituting prudent fiscal policies to keep budget deficits at sustainable levels will be necessary.

In countries with large fuel subsidies and low energy taxation, lower oil prices are presenting an opportunity for subsidy realignments, energy tax reform and efficient energy pricing. These could help build fiscal space to achieve a fiscal windfall that could be used to re-build buffers against future cyclical downturns, or to expand spending on infrastructure investment. Policy priorities could include broadening revenue base and adjusting nonessential expenditures while maintaining essential capital expenditure to address infrastructure gaps and social spending. Improvements in public investment management systems would need to be accompanied by efforts to ensure that resources are allocated to the most productive ends.

African countries need to speed up the adoption and implementation of policies that favor structural transformation and diversification of production beyond commodities to insulate the economies from external shocks. They also need to take advantage of globalization to promote greater integration into global trading networks. This could help in building strong and inclusive economic bases that create jobs for the rapidly growing young population as the region experiences a significant demographic transition in the next decades.

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[24] Mckinsey Global Institute (2010), Lions on the move: The progress and potential of African economies. Mckinsey Global Institute.

The slowdown of the Chinese economy and the recurring commodity price fluctuations underscores the need for African countries to look into the long term and pursue concerted industrial policies to shore up manufacturing value added by incentivizing domestic production and domestic demand for locally-produced products. In most African economies, the manufacturing value added and demand for domestic products is still very low. Most countries are de-industrializing in spite of comparative resource advantages, fueling dependence on an increasingly volatile global market. This calls for efforts to speed up the industrialization of economies.

For many Sub-Saharan African countries which have been experiencing robust growth, sustaining high GDP growth is a policy priority. Policies to remove impediments to private sector activity, and to improve the business environment would be critical. Addressing power shortages should also be a priority for many African countries.

Conclusions

Global economic growth has decelerated in 2015, weighed down by the slowdown in developing and emerging market economies, overshadowing an improved growth performance in high income countries. The end of the commodity price super-cycle, marked by a plunge in oil prices and other commodities, as well as the slowdown in China and the hike in US interest rate contributed to slower growth in emerging and developing countries. A marginal increase of world growth and developing and emerging market economies is anticipated in 2016, as recovery in high income countries solidify. The oil market will remain oversupplied in the medium term and oil prices will likely remain depressed. Diverging monetary policy stances of major central banks and financial markets sentiment continue to influence global financial conditions. The macroeconomic outlook is largely clouded by risks. The key risks include financial market volatility and China's economic slowdown, amid rebalancing and depressed commodity prices. While short-term policy responses to external shocks could be necessary for many African economies, the recurrence of these shocks and the ensuing volatility emphasize the need to accelerate diversification of economies and insulate economies from boom-bust cycles associated with commodity swings. Policies that instill confidence, promote investment and reduce constraints to business remain critical.