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MACROECONOMIC & MARKET OUTLOOK
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Macroeconomic and Market Outlook[1]

Second Quarter, 2016

Highlights

- *The global markets have calmed down after a tumultuous start to 2016.*
- *The global economic recovery remains slow and fragile. Visible risks will keep global growth below the projected 2.9 percent in 2016.*
- *High income economies are gaining strength, but the slowdown in emerging and developing countries will continue to hold back overall global growth momentum.*
- *Developing and emerging countries are facing headwinds from persistent low oil and other commodity prices; weak global trade amid the slowdown and rebalancing in China; prospects of financial tightening and subdued capital flows.*
- *Growth in Sub-Saharan Africa is more moderate than initially anticipated, under the weight of external and domestic constraints.*
- *After a dip in oil prices at the beginning of 2016 ($31/bbl in January), oil prices have picked up in recent months. They are forecast to average $34/bbl in 2016 and $40/bbl in 2017, a marked revision from the previous forecasts.*
- *The macroeconomic outlook is largely subject to downside risks emanating from the slowdown in large emerging market economies, notably in China amid that economy's rebalancing, lower commodity prices and prospects of financial tightening. African countries are also subject to risks related to political uncertainties and security threats, and El Nino-induced drought.*

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Global Macroeconomic Outlook

The year began with turbulence in the global markets, marked by a further decline in oil prices, financial markets turmoil and volatile capital flows. However, the conditions have calmed down towards the end of the first quarter and economic sentiment has improved somewhat. The World Bank projects 2016 global growth at 2.9 percent. High-income economies are providing some lift up, but the slowdown in emerging and developing countries continues to hold back this momentum. Given the risks in emerging and developing countries, we believe that global growth would remain subdued and well below 2.9 percent in 2016.

High-income countries are projected to expand by 2.1 percent in 2016, led by the US economy, Euro Area and Japan[2]. Despite the headwinds in recent months, the U.S. recovery is gaining strength, with growth projected at 2.6 percent in 2016, supported by lower oil prices, a strengthening housing market and improving consumer spending, manifesting in improving labour data and low inflation[3]. The U.S. dollar has recently moderated after strengthening for some time in 2015, helping to improve manufacturing sector competitiveness. Monetary policy is expected to remain largely accommodative in 2016 as the Fed kept interest rates unchanged in March. In the Eurozone, the underlying economic conditions are improving, helped by lower oil prices, continued monetary policy easing and Euro depreciation. However, the tide of terrorist attacks, marked by recent attacks in Brussels in March, continues to threaten the budding signs of improving economic activity in Europe. Growth in Japan is expected to firm up in 2016, supported by continued accommodative monetary policy, which has seen interest rates remaining in negative territory as well as fiscal support and lower oil prices.

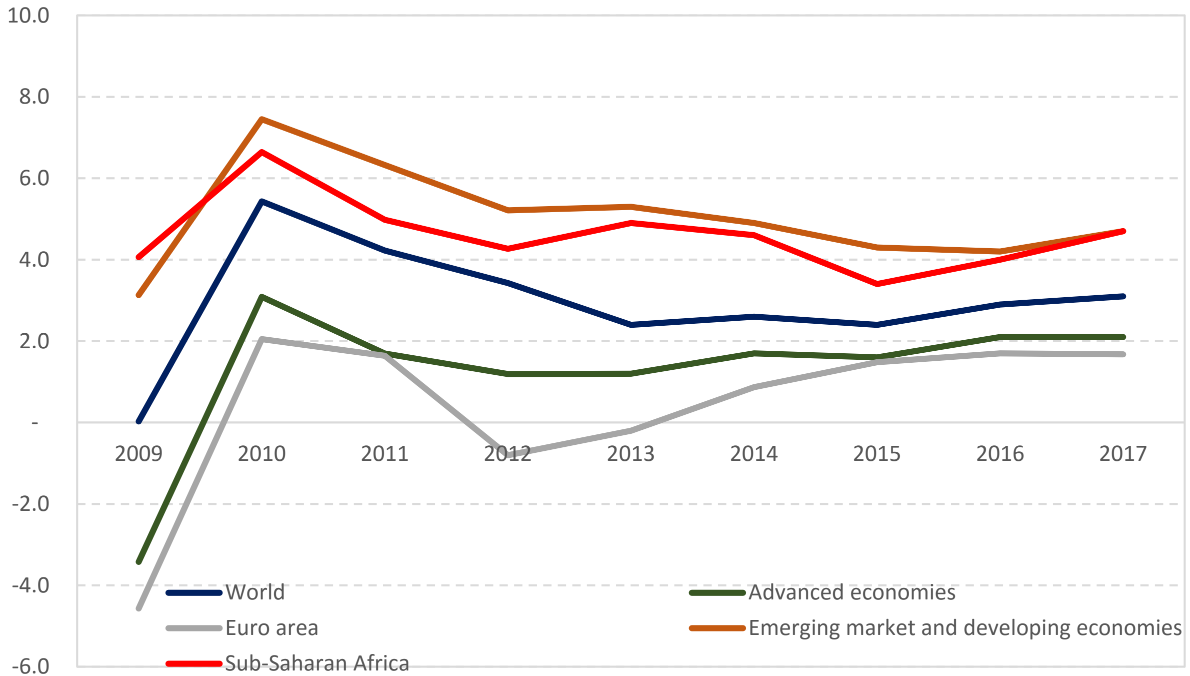
Global inflation is expected to tick up as commodity prices possibly stabilize later in 2016. Prospects of a gradual increase in policy interest rates in the United States after the December 2015 hike are contributing to tighter global financial conditions which is further reducing capital flows in emerging markets and putting depreciation pressures on emerging market currencies. Global trade and manufacturing activity remain weak amid China's slowdown and subdued global demand, especially in extractive industries. Going into 2017, global trade is expected to post a modest recovery to its pre-crisis rate of expansion, as the global economy improves.

The picture for emerging market and developing economies is still challenging amid visible downside risks in 2016. As emerging market and developing economies account for over 70 percent of global growth, their slowdown will weigh on 2016-17 growth prospects and offset a modest recovery in advanced economies. The simultaneous slowdown of major emerging market economies—Brazil, Russia, China and South Africa is a major source of concern. These countries are still facing headwinds including low oil and/or other commodity prices (affecting net commodity exporters); weak global trade amid the slowdown and rebalancing in China; heightened volatility in financial markets and subdued capital flows. Many emerging and developing economies are also grappling with the impact of weaker currencies on inflation and private sector balance sheets stemming from increase in debt service.

[2] IMF, World Economic Outlook update, January 2016

[3] Federal Reserve Bank data, 2015.

Figure 1: Global Growth and Projections



Source: IMF and World Bank

China's growth is projected to slow further to 6 percent in 2016, following a 6.8 percent growth rate in 2015, as the rebalancing progresses further toward growth driven by consumption and the services sector.[4] However, the rebalancing of the economy, while sustaining aggregate demand, is proving to be painful and challenging. The Shanghai stock market slumped by more than 12 percent while the Yuan devalued by 1.5 percent in January, sparking a global sell-off in risky assets.[5] These developments continue to cement the belief that China is drifting to a "new normal" growth rate, widely expected to be around 5 percent. Inflation is expected to remain low in 2016 and 2017, while the current account surplus will stay broadly stable. The market sentiments towards China remain bearish. However, the prospects of a hard landing are unlikely, as Chinese authorities have policy levers and fiscal space to smooth the rebalancing.

Brazil is battling with a recession on the back of declining commodity prices, continued weak investor confidence, and rising inflation. Output is projected to contract by 3.5 percent in 2016. The political situation is becoming fluid, raising uncertainty about the future of president Dilma Rousseff. If the most likely scenario materializes, President Dilma could be impeached and power transferred to her vice president, Michel Temer, who promises drastic changes to generate a primary fiscal surplus as early as 2017. This would be a significant change for a country that presented nominal deficits of 6 percent of GDP in 2014 and 9 percent in 2015.

Russia is facing a continued downturn, with -1 percent growth in 2016, as it continues to adjust to low oil prices and sanctions[6]. Economic activity in other commodity-exporting EMEs such as Mexico, Malaysia, Venezuela, Chile and South Africa continue to be saddled by the persistent low commodity prices. However, net oil importers such as India, Turkey, Indonesia,

[4] Asian Development Outlook, 2016
[5] MRB Partners Report, January 2016
[6] IMF WEO update, January 2016.

Hungary, Kenya and others are benefiting from lower oil prices. India is expected to grow at a robust pace of 7.5 percent in 2016, boosted by strong investor confidence, low oil prices and policy reforms. In the Middle East, positive growth prospects are weighed down by lower oil prices, and in some cases geopolitical tensions.

Macroeconomic Outlook for Africa

Growth in Sub-Saharan Africa is expected to be less robust than initially anticipated, under the weight of external and domestic constraints. Low commodity prices, the slowdown in China and other major emerging markets, and the tightening of financial conditions continue to weigh down on economic activities. On the domestic front, political instability and security threats in some countries, electricity shortages, and adverse weather conditions are further dampening growth. In light of these headwinds, 2016 growth could be well below the initially projected rate of 4.2 percent. Although oil prices have stabilized somewhat in in the first quarter, we believe that they will remain at lower levels and not enough to lift up growth prospects for oil exporting countries. However, stabilizing commodities and activity rebound in non-oil sectors could provide some hope for a modest improvement in growth in 2017.

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. Mineral exporters, including Mauritania, South Africa, and Zambia, are also hard hit by low commodity prices thus far in 2016.

Fiscal vulnerabilities, reflected in widening fiscal deficits, are visible in a number of oil exporting countries (e.g. Republic of Congo, Gabon, Angola) due to falling revenues. Low commodity prices are also depressing exports revenues, and widening current account balances in commodity exporting countries. But the fall in commodity prices has also meant that investments in exploration and extraction are being curtailed or delayed. As prices of agricultural commodities experienced only a moderate decline, exporters of agricultural commodities are experiencing a less pronounced slowdown in economic activity. In oil importing countries, current account deficits have remained large because of rising non-oil imports and capital goods for infrastructure projects in some cases (e.g. Kenya and Namibia). As a result, government debt ratios have continued to rise, driven by non-concessional borrowing, especially in frontier economies.

Although low fuel prices have helped to moderate inflationary pressures, currency depreciations and higher imports have contributed to higher inflation in some countries, such as Ghana, Angola and Zambia, where it is in the double digits. Food deficits due to El Nino- induced drought will affect the Southern and Eastern African countries and fuel inflationary pressures, compounded by electricity shortages and depreciating currencies. A number of central banks have responded by tightening monetary policy through raising interest rates (Angola, Ghana, Kenya, Mozambique, South Africa, Uganda, Zambia). Political uncertainty and security threats (Nigeria, South Sudan, Cote d'Ivoire) and electricity shortages (South Africa, Zambia, Ghana) continue to drag growth below potential in several countries.

Capital flows to the region slowed in 2015, as cross-border bank lending declined. Bond spreads have continued to widen, reflecting a re-assessment of risk among sovereign-debt investors to account for growing vulnerabilities, amid the global economic slowdown and expectations of further increases in US interest rates in 2016. US monetary tightening in December 2015 has raised debt servicing costs for many countries at the beginning of 2016.

Table 1: Macroeconomic Indicators for Sub-Saharan Africa

	2009	2010	2011	2012	2013	2014	2015E	2016F
Real GDP Growth (percent)	4.1	6.9	5.1	4.1	4.1	4.6	3.4	4.2
Nominal GDP (USD Billion)	1019.1	1275	1428	1526.3	1607	1670	1560	1639.8
Inflation (percent, yoy ave)	9.8	8.2	9.5	9.4	6.6	6.4	6.9	7.3
Oil production (mbpd)	5.4	5.4	5.4	5.6	5.2	5.1	5	5.4
Net FDI (percent of GDP)	2.8	2.7	2.1	2.0	1.3	1.3	2.1	2.5
Fiscal Balance	-4.6	-37.4	-1.1	-1.8	-3.1	-3.5	-4.3	-3.6
Total Public Debt (percent of GDP)	29.7	27.7	28.3	28	29	29.9	30.7	31.2
CA Balance	-2.8	-0.9	-0.7	-1.9	-2.4	-4.1	-5.7	-5.5

Sources: AFDB, IMF, World Bank

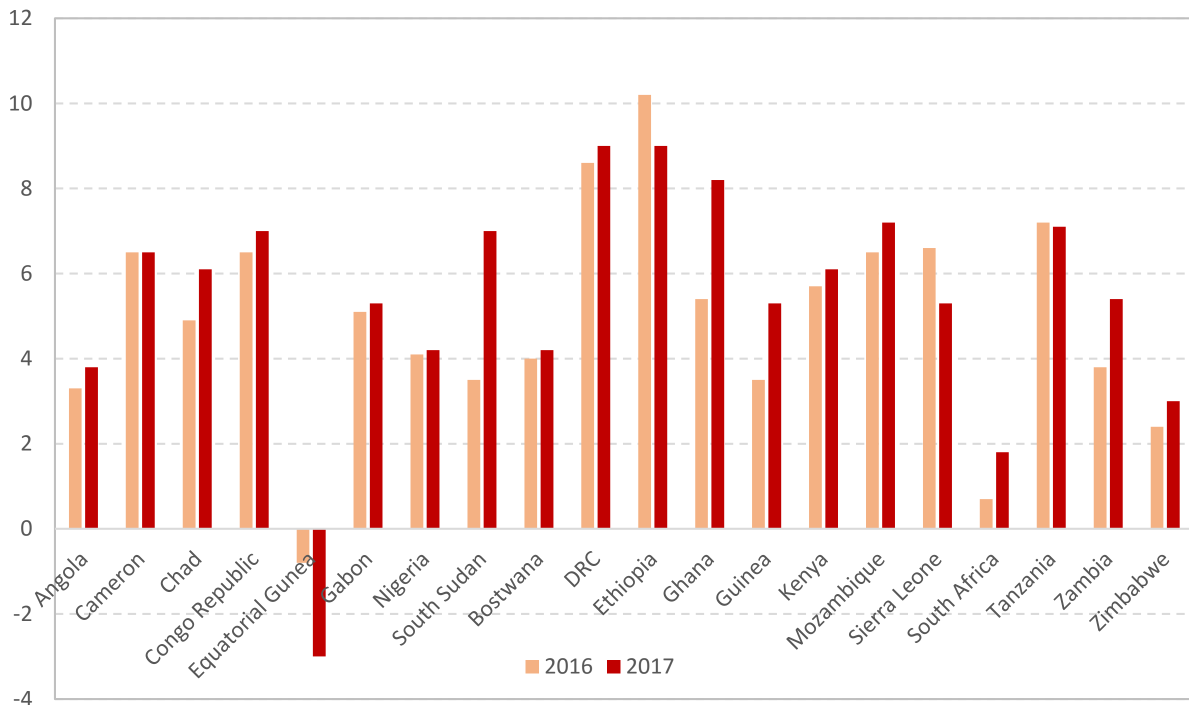
Most currencies remain under pressure from high fiscal and current account deficits, amid depressed commodity prices, combined with strong demand for the U.S. dollars. This is especially the case for currencies in commodity exporting countries and frontier-market economies. The South African rand depreciated by over 7 percent in January 2016, before strengthening in the last few weeks. The Angolan kwanza weakened by 18.7 percent in the first quarter of 2016, while the Zambian kwacha lost 2 percent in the first quarter. The Nigerian naira has, however, remained relatively stable, amid interventions by the Central Bank.

In our view, Sub-Saharan African growth will remain below potential in 2016, but could pick up modestly in 2017 as conditions improve somewhat, with stabilizing commodity prices and a strengthening global recovery supporting moderate external demand. Improvement in domestic demand and continuing infrastructure investment will also support growth in some countries. Consumption dynamics are expected to remain different for oil exporters and importers. Private consumption growth will remain weak in oil exporters as revenues decline and as subsidies are removed in some countries, while depreciation-induced inflation will weigh on consumers' purchasing power. Fiscal adjustments in oil-exporting countries is expected to result in further capital expenditure cuts. The fiscal policy stance in commodity exporters could ease gradually in 2017 if commodity prices stabilize. FDI will remain low due to the slowdown in major emerging market economies and lower commodity prices.

Nigeria, SSA's largest economy, is projected to grow by 4.1 percent in 2016 and 4.2 percent in 2017 (following a 3 percent growth rate in 2015), as oil prices stabilize, activity in non-oil

sectors improves, and the new government works on tackling corruption and implements structural reforms to enhance productivity. The economy experienced some turbulence at the beginning of 2016, amid heightened tensions in global financial markets which triggered some capital outflows. The economy continues to experience imbalances in the foreign exchange markets as authorities try to artificially maintain a strong naira. Foreign exchange reserves fell 20 percent to $34.25 billion (6.0 percent of GDP) in 2015 as the Central Bank drew down the reserves in order to defend the naira. The Central Bank of Nigeria cut the benchmark policy interest rate to 11 percent in November 2015, in an attempt to stimulate growth. The fiscal position remains tight in 2016, as expenditures (especially capital expenditures) were cut to match the decline in revenues from the oil sector. However, Nigeria's sovereign debt has remained low (less than 15 percent of GDP). Security concerns from Boko Haram militants and infrastructure and electricity deficits continue to hamper economic activity.

Figure 2: Growth estimates and forecasts for selected African countries, 2016 and 2017



Source: IMF and World Bank

In Angola, growth prospects remain low as low oil prices pose challenges. Growth is forecast at 3.3 percent in 2016 and could inch up marginally to 3.8 percent in 2017.[7] The government presented a US$48 billion budget for 2016 based on an assumed oil price of $45 per barrel and daily production of 1.8 million barrels/day which could grow to 1.9 million barrels/day in 2016. As global oil prices remain low, fiscal revenues remain curbed, while the budget deficit is expected to widen to 5.5 percent in 2016 from 3.5 percent in 2015. The government is implementing expenditure measures, including removing fuel subsidies and freezing public sector hiring, as it adjusts to a new normal of lower oil prices. The kwanza depreciated by 18.7 percent in the first quarter of 2016, exerting inflationary pressures. Foreign exchange shortages remain a challenge and the Central Bank has continued to limit the supply of foreign exchange

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

only to strategic sectors of the economy. The gap between the official exchange rate and the parallel exchange rate has continued to widen. Inflation reached 13.2 percent as of November 2015, weakening consumer spending. The credit rating agency Standard & Poor's (S&P) has downgraded Angola's credit rating from B+ to B in February, on concerns of slowing economic performance amid lower than expected oil prices.

In South Africa, lower commodity prices, the slowdown in China, power supply bottlenecks, tense labour relations, compounded by severe drought, and weak investor sentiment continue to dampen economic activity. Growth is projected slow down to 0.7 percent in 2016[8]. The South African rand depreciated by more than 8.3 percent in January, partly offsetting the decline in commodity prices. Inflation has surged to 7 percent, overshooting the upper target of 6 percent, largely fueled by surging food prices. The SARB raised its policy interest rates by 25 basis points from 6.75 to 7 percent in March to contain inflationary pressures. The country's credit rating was downgraded in December after the unexpected change of finance minister, while the balance of payment pressures continues to mount amid capital outflows in the wake of the increase in US interest rates in December 2015. In an effort to avert another credit rating downgrade, the government implemented stricter fiscal measures announced in the 2016 budget in February. Against the backdrop of a high unemployment rate, further budget cuts could potentially trigger social unrest. The outlook for 2017 points to a slight recovery, with real GDP growth forecast at 1.8 percent, as electricity supply improves and commodity prices stabilize. President Zuma's future is uncertain amid increasing pressure for him to step down in the wake of deteriorating economic conditions, corruption allegations and a recent Constitutional Court ruling that the President failed to uphold the Constitution in matters related to state-sponsored upgrades to his private residence.

In Ghana, economic activity is undermined by power shortages, a slump in the cocoa harvest and low oil prices, which could prevent growth from exceeding the projected 5.4 percent in 2016. The fiscal balance is projected at -5.3 percent of GDP, while the current account deficit is expected to narrow to -7.4 percent of GDP in 2016 from 8.2 percent in 2015[9]. Ghana experienced net capital outflows in 2015, partly driven by a deterioration in perceived risk amid global market volatility, putting pressure on the Ghanaian cedi to depreciate significantly in 2015. However, the cedi has been relatively stable since January 2016. Inflation has remained high and in the double-digit range (17.3 percent in February), amid currency depreciations, prompting monetary tightening. In Zambia, economic activity is weighed down by depressed copper prices, rising borrowing costs and severe electricity shortages caused by a prolonged drought. 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. Facing drought in 2016, in February Zambian authorities imposed restrictions on maize exports, a major source of agricultural revenue for Zambia.

Some 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. Cote d'Ivoire is benefiting from reforms of the progressive government,

[8] IMF WEO Update, January 2016
[9] IMF Country Report No. 16, January 16

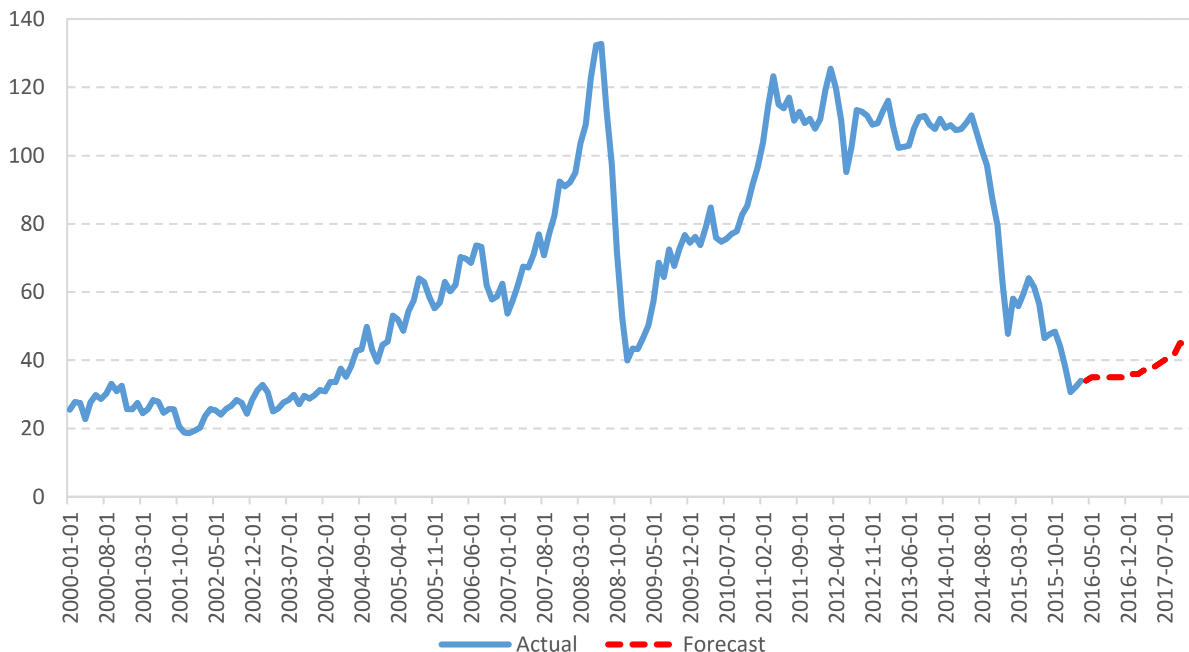
following the re-election of Ouattara in 2015. Fiscal discipline is helping to sustain the country's external debt and fiscal deficit, helping to improve perceptions of Cote d'Ivoire's as one of the most business-friendly countries in Africa.

Growth is holding up in some low-income countries, supported by infrastructure (Rwanda, Ethiopia) and mining expansion (DRC, Mozambique and Tanzania), agricultural growth (Ethiopia) and consumer spending (Uganda). These countries are anticipated to grow at 7 percent or more in 2016 and 2017.[10] Ethiopia experienced strong growth in recent years, but will battle a serious drought in 2016, which threatens food supplies and overwhelming government resources. About 10.2 million people will be in food deficit in Ethiopia, requiring about US$1.4 billion in food aid.[11] Guinea, Liberia, and Sierra Leone are recovering as the effects of the Ebola crisis wane. Poor weather conditions in 2016, emanating from the expected El Nino effects, will reduce agricultural output in Southern and Eastern Africa.

Oil Markets

Oil prices have dipped to very low levels in recent months, with the Brent benchmark averaging $31/bbl in January 2016 and $32/bbl in February – prices not seen since early 2004. This is a result of continued high levels of production, by both non-OPEC and OPEC countries, amid tepid global demand. Prices recovered slightly to around $40/bbl in mid-March. The main factors behind this uptick include the discussions about a possible output freeze by OPEC and Russia; supply disruptions in Iraq, Nigeria and the United Arab Emirates whose combined output fell by 350 kb/d in February), indications that non-OPEC production is falling (led by reduced output in the US and the North Sea) and recent weakness of the US dollar.

Figure 3: Brent Oil Prices and Forecast



Source: EIA, USA

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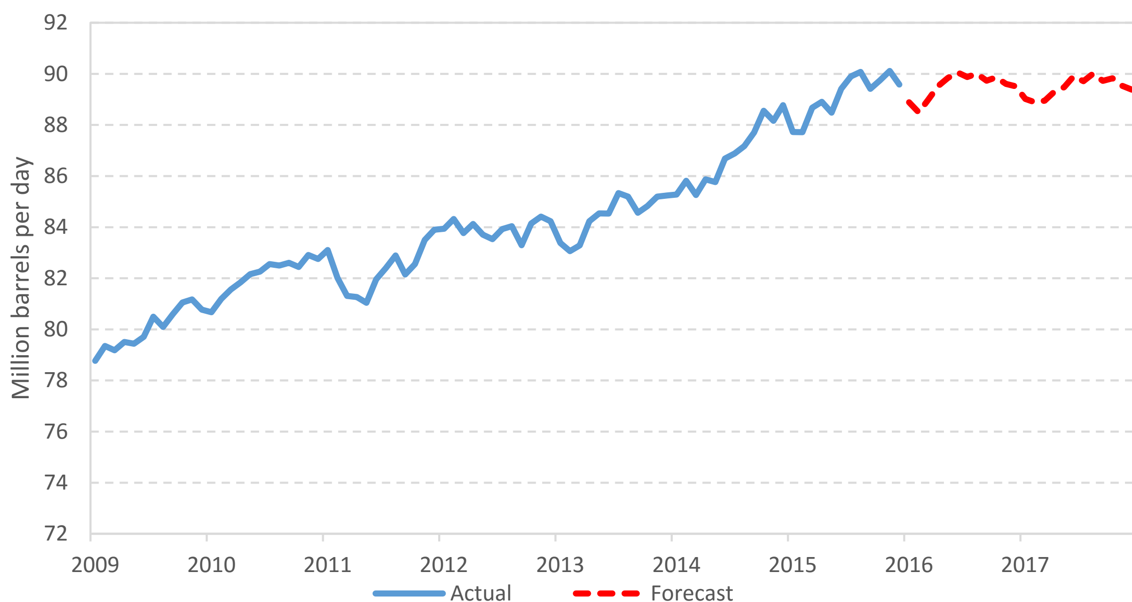
[10] World Bank, Global Economic Prospects, January 2016

[11] http://www.fews.net/

Several major producers are continuing to produce at or near all-time highs (notably Russia, Saudi Arabia and Iraq), while falling US tight oil production is being partially offset by Iran's increasing production and exports in the wake of sanctions on that country having been lifted in January 2016. Iran has indicated that it will not cap its production, and thus the talks of an output freeze are unlikely to have a major impact on prices in the near future. According to the IEA, global oil supplies fell by 180 kb/d in February, to 96.5 mb/d. Production stood 1.8 mb/d above a year earlier, as a slight decline in non-OPEC was more than offset by OPEC gains. Non-OPEC production is forecast to decline by 0.75mb/d in 2016, to 57.0 mb/d. The EIA expects non-OPEC production to decline by 0.4 mbpd in 2016 and a further 0.5 mbpd in 2017, led by falls in US output. OPEC crude oil production is forecast to increase by 0.7 mbpd in 2016 and by 0.4 mbpd in 2017, with Iran responsible for most of the increase as it ramps up production following the lifting of US and EU sanctions.

Figure 4: Oil Production and Forecasts



Source: EIA, USA

The continuing slow-down in the rate of global economic growth is contributing to somewhat weaker oil demand, especially in the last few months. Another contributing factor has been the relatively mild winter in the northern hemisphere, which has reduced demand for heating oil. Oil demand is projected to rise by about 1.2 million b/d this year, down from a 1.8 mb/d increase in 2015, as a result of slower global economic growth, and especially the Chinese economy. Chinese oil demand is expected to grow modestly this year, by about 300-400 kb/d. The EIA also forecasts that global consumption of petroleum and other liquids will grow by 1.1 million b/d in 2016, which is lower than its previous estimate due to reduced expectations for global economic growth[12]. OPEC is slightly more bullish, anticipating world oil demand growth of 1.25 mb/d in 2016.

[12] EIA Short-Term Energy Outlook, March 2016

Supply has proved to be more resilient to low prices than anticipated (i.e. more price inelastic). This is partly because of lags between investments in new oil fields and when production comes online. Similarly, oil demand has been surprisingly unresponsive to the huge drop in prices (i.e. price inelastic). Usually, a price fall of this magnitude would have given a stimulus to the world economy, but this impact has apparently been outweighed by negative consumer and investor sentiment and the slow-down in the Chinese economy.

The recent oversupply in world oil markets is expected to persist over the coming year. Global oil inventories are expected to grow by an average of between 1 and 1.6 million b/d in 2016. OPEC is not planning to increase their official production target, although Iran indicated that they will not limit their output. The US oil rig count has continued its decline, reaching a low of 386 units in the second week of March, down from 1,600 active rigs in October 2014. The EIA currently forecasts that Brent crude will average $34/bbl in 2016 and $40/bbl in 2017, a marked fall compared to its December forecast of $56/bbl for 2016. The EIA expects global oil inventories to grow by an average of 1.6 million b/d in 2016 and by 0.6 million b/d in 2017, that is the oil glut is projected to continue until the third quarter of 2017. Oil prices are not expected to begin to recover significantly until 2017 when the gap between supply and demand narrows. The recent attenuation of conflict in Syria has somewhat reduced the immediate threat to oil production in the region. Nevertheless, continued conflict and instability in several major oil exporters (e.g. Iraq, Nigeria and Venezuela) presents an ongoing supply-side risk. We expect the recent lows in oil prices to hold, as excess supplies continue to weigh down on prices.

The collapse in oil prices is significantly affecting oil exporting countries. Most of these countries (e.g Republic of Congo, Angola, Chad, Equatorial Guinea, Venezuela, Saudi Arabia, etc.) rely on oil revenues for between 50-90 percent of their government revenues. The drop in prices is weighing on growth prospects and forcing many governments to curtail spending and increase borrowing. Cuts in social spending are in turn putting increasing political strain on some countries (e.g. Saudi Arabia and Venezuela) and thus adding to risks to future oil output in these producers. Several OPEC member countries are experiencing large budget deficits as oil revenues plummet. Norway has announced that it will make the first ever withdrawal from its Sovereign Wealth Fund in order to cover shortfalls in its government budget. Lower prices are also negatively affecting economic activity even in non-oil sectors through forward and backward linkages and putting pressure on current accounts and exchange rates. Corporate earnings have also fallen sharply, while investment spending (exploration and new projects) is being curtailed and raising debts. The global oil and gas industry's debts almost tripled between 2006 and 2014, from about $1.1 trillion to $3 trillion. Because of the tight link between oil prices and corporate bond spreads, the lower prices are also depressing investor sentiment.

Financial Markets

After a tumultuous start to 2016, global financial market conditions have calmed down. The markets were rattled by continuous worries about the state of the Chinese economy, collapsing oil prices and tightening of US financial conditions at the end of 2015.[13] Stock markets were

[13] MRB Partners Report, 31 March 2016.

the most turbulent. The Shanghai Composite index fell by about 25 percent in January, but has since regained about 13 percent. However, the Shanghai index is still down 42 percent from its peak in June 2015. The Dow Jones Industrial Index shed 10 percent of its value in January, but has subsequently recovered to the level seen in late December. The MSCI emerging markets index, which slumped by 3.3 percent in January, leapt up by 11 percent in February and March.[14] China is still experiencing capital outflows, although these have slowed down recently. The outflows reflect concerns about continued weakness in the Chinese economy, fears about Yuan devaluation as well as Chinese companies buying companies abroad. The collapse in commodity prices and the surge in the U.S. dollar over the past 18 months were very disruptive on many fronts. However, the calming down of the conditions should help investors regain some confidence.

At its regular meeting in March, the US Federal Reserve Bank kept the target range for its benchmark interest rate constant at 0.25 percent to 0.50 percent. However, the Fed signalled a slowdown in its anticipated interest rate hike programme for the remainder of 2016, indicating that it expects two quarter-point hikes as opposed to the four increases that were foreseen in December 2015. The Fed cited an uncertain global economic outlook and a low risk of inflation. On the upside, the Fed foresees continued gains in the job market, and expects the US unemployment rate to decline to 4.7 percent by the end of the year. However, with core inflation reaching 2.3 percent, the real interest rate in the US is effectively minus 2 percent. The Fed reiterated its cautious optimism on the outlook, while providing a more realistic profile for rate hikes in the coming year, and also lowered its expected long-term equilibrium policy rate. We expect the Fed to stay on its glacial rate-hiking path in the medium term.

The Bank of England maintained interest rates at historic lows of 0.5 percent, but remained concerned about weak inflation and an uncertain outlook for the UK economy, especially in the context of the ‘Brexit’ referendum scheduled for June. Meanwhile, the central banks of Denmark, Sweden, Switzerland, the EU and Japan maintained negative interest rate policies that were implemented in 2015. The ECB Governing Council extended the policy easing, to combat low inflation and stimulate credit growth in the euro area economy. Elsewhere, in emerging markets, the South African Reserve Bank raised its repo rate by 25 basis points in March after a hike of 50 basis points in late January in a bid to dampen inflationary pressures induced by depreciation of the rand. Brazil’s central bank has kept its rate steady since the last increase in July 2015, while the Mexican central bank raised its benchmark rate by 50 basis points in February[15]. Uneven economic growth and aggressive monetary easing by global central banks have kept US bond yields low.

With the exception of China, the BRICS emerging market economies are struggling to maintain investment grade credit ratings. South Africa’s sovereign credit rating was downgraded by Moody’s in December, to BAA2 from BAA1, while S&P and Fitch downgraded it to BBB- in December, one grade above junk status. Brazil is rated at junk status by all three ratings agencies. Fitch has Russia just above junk status at BBB-, while the other two agencies rate its

[14] https://www.msci.com/emerging-markets
[15] http://www.cbrates.com/

debt at junk grade. All three countries are experiencing negative or very low (in the case of SA) economic growth, as well as political risk (internal in the case of Brazil and SA, geopolitical in the case of Russia). India has its head just above water, with a BBB- rating from S&P and Fitch, and an equivalent BAA3 rating from Moody's. In Africa, sovereign bonds have continued to widen over uncertainty about government policies and slowdown in the economies. This also reflects re-assessment of risk of sovereign bonds to account for growing vulnerabilities. Spreads are higher in countries where market confidence is weakest.

The outlook for global financial markets remains clouded by uncertainties. The major risk is high levels of sovereign, corporate and household debt in many countries in the context of a low growth environment and lower commodity prices. Even unconventional monetary policies are having limited impacts in stimulating demand, while most governments remain reluctant to use expansionary fiscal policy and thus risk even higher public debt levels. Economic activity in high income countries, global trade developments, China's rebalancing process and stability or volatility in oil prices will also shape the prospects.

Key risks to monitor

The outlook is largely subject to downside risks emanating from the slowdown in large emerging market economies, China's rebalancing, lower commodity prices and prospects of financial tightening. African countries are also clouded by risks related to political uncertainties and security threats and El-Nino-induced drought.

Continued strains in some large emerging market economies remains a risk in the short to medium term. The recessions in Russia and Brazil remain a drag to global trade, while a sharper-than-expected slowdown in China could result in further weakening in commodity prices, and dampen growth and investment prospects in many countries. Also, with more international spillovers through trade, asset prices and financial flows, the effects on global financial markets cannot be underestimated.

As a result of demand and supply factors, the risk of a further drop in commodity prices is possible. This will dampen growth prospects for many commodity exporting countries especially in less diversified economies. Commodity markets pose two-sided risks. On the downside, further declines in commodity prices would worsen the outlook for already-fragile commodity producers, and increasing yields on energy sector debt threaten a broader tightening of credit conditions. On the upside, the decline in oil prices may provide a stronger boost to demand in oil importers than currently envisaged, including through consumers' possible perception that prices will remain lower for longer. For many commodity exporters, sizeable fiscal and current account deficits could lead to currency pressures, higher inflation, and lower business confidence. If oil prices remain very low, oil-exporting countries may be required to undertake deeper fiscal adjustments with sharper expenditure cuts.

Although volatility in the global financial markets has subsided, possible renewed tensions in is a risk to watch. As some of the triggers remain visible, tensions may not be over yet. The deterioration in global liquidity conditions could further push up financing costs and result in cut-offs of capital flows and curtail bank lending. A sudden rise in global risk aversion may

lead to sharp further currency depreciations and possible financial strains in vulnerable emerging market economies, which could create broader contagion effects especially in an environment of market volatility. This would affect corporate financing and balance sheets. Investors need to continue to monitor weak links in the world economy, especially commodity contagion and imbalances in major financial centers.

An escalation of ongoing geopolitical tensions and security and political risks, especially in Syria, Russia, Iraq and parts of Africa, are important risks to watch. The Islamic State insurgency is growing and the recent attacks in Brussels is further complicating the migrant crisis in Europe, amid differences among members on how to deal with it. Boko Haram insurgencies are posing significant security risks to Nigeria, Cameroon, Chad and Niger, while terrorist threats remain a concern for Kenya, Mali and Cote d'Ivoire. These risks are affecting economic activity, disrupting global trade, financial, and tourism flows, and dampening both business and investor sentiment. Planned elections to monitor in Africa in 2016 are in Cape Verde, Chad, Comoros, DRC, Equatorial Guinea, Gabon, Gambia, Ghana, Niger and Zambia.[16]

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 40 million people could face food shortages in 2016.[17] Food deficits will necessitate imports, and fuel inflation in many of the affected countries.

Policy implications

In light of the above-mentioned challenges and risks, various policies are needed to respond to growing vulnerabilities and constraints, and to promote growth. Policy responses would vary between commodity or oil exporters and oil importers. Oil and commodity exporters may need to strengthen their monetary policy frameworks, to prevent inflationary pressures which are induced by currency depreciations amid declining exports revenues. Oil importers, which are benefiting from lower oil prices and facing reduced inflationary pressures, could find room to cut interest rates to support economic activity. Allowing for exchange rate flexibility could also be helpful in facilitating smooth adjustment to external shocks in emerging market and developing economies.

Commodity exporting countries could also respond by fiscal tightening. As oil and commodity prices are expected to remain at low levels for some time, it is important for commodity exporters to adjust to this 'new normal' of low commodity prices. Reducing public expenditures while raising their efficiency and strengthening fiscal institutions, and increasing non-commodity revenues would facilitate the adjustment to lower fiscal revenues.

Oil or commodity exporting countries with subsidies could take the opportunity to reform their taxes and subsidies. This could lesson spending pressures and help to build fiscal space for future cyclical downturns, or expansion of infrastructure investment. Policies to broaden the

[16] National Democratic Institute: https://www.ndi.org/electionscalendar
[17] IRIN NEWS: http://www.irinnews.org/report/102317/an-unwanted-guest-el-niño-and-africa-in-2016

revenue base, for example by bringing small enterprises into the tax net and strengthening tax administration, could be critical in these efforts.

Addressing infrastructure deficits, especially power supply, should be a policy priority, considering that it is a big constraint to growth prospects for many African countries. There is a need to invest in new power generation capacity, especially incentivising private investment in energy and helping to build resilience in the power sector.

The recurring commodity price shocks and the consequential macroeconomic volatilities underscores the need for African countries to look into the long term and improve value addition on their tradables. There is an urgent need for African countries to speed up the adoption and implementation of structural transformation and diversification policies to insulate their economies from external shocks. African countries could take advantage of globalization to integrate and tap into global trading networks, even though the pace of world trade growth has slowed.

Conclusions

The global economic prospects remain uncertain in 2016 in the wake of economic weakening in major emerging market economies, which could overshadow the growth impetus of high income countries. 2016 opened with heightened turbulence in the global financial markets amid continuous worries about the state of the Chinese economy and collapsing oil prices and tightening of US financial conditions at the end of 2015. The volatility has since subsided somewhat. The weakening of oil prices in recent months reflects high levels of production by key producing countries and tepid global demand. Oil prices have recovered slightly in March but are not expected to rise significantly until 2017 when the gap between supply and demand narrows. Other commodity prices remain depressed, dampening growth prospects in many countries. A marginal increase of world growth and growth in developing and emerging market economies is anticipated in 2017, as commodity prices stabilize, and high income countries further solidify their growth. Growth in Sub-Saharan Africa will remain below potential in 2016, as commodity prices remain at low levels.

The macroeconomic outlook is overshadowed by downside risks emanating from the slowdown in large emerging market economies, China’s rebalancing, lower commodity prices and tightening of global financial conditions. Global financial markets remain uncertain amid diverging monetary policy stances of major central banks, market sentiment, China’s rebalancing process and the direction of oil prices. For African countries, the outlook is also subject to political uncertainties and security risks related to insurgencies and terrorism and El Nino induced drought. Various policies are needed to respond to growing challenges and constraints and to promote macroeconomic stability and growth. The recurring commodity price swings and the resultant macroeconomic volatilities is a wake-up call to many African economies to accelerate economic diversification and insulate their economies from external shocks.