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Introduction

In a tense referendum, the British people voted by a narrow margin for the United Kingdom (UK) to leave the European Union (EU) on 23 June. Those in favour of rescinding membership of the EU want to have greater sovereignty and control over their economy, greater control over migration, and to make their own trade agreements. The vote was widely unexpected by the markets. This is an unprecedented development, which is likely to have significant economic, financial, social and political implications in Europe and across the world. This piece analyses the potential implications of Brexit for African economies. The Brexit has come at a time when many African countries are facing serious external and internal pressures which are constraining their economic activities. While Brexit will have negative implications for some African economies on many fronts, it may also bring opportunities. We analyse the effects of this move on African economies from different perspectives.

Financial markets turmoil and contagion effects

In the short term, the Brexit shock has heightened volatility in the global financial markets. The "leave" result was not widely anticipated by the market, prompting marked reactions as investors shifted funds to safe haven assets. Global stocks tumbled on the Brexit outcome, with about USD2 trillion estimated to have been lost globally on 24 June. The FTSE 100 Index plunged as much as 8.7 percent, the largest loss since 2008, while European stocks slid 7 percent in their worst day since 2008. The MSCI's global stock index lost 4.8 percent in the biggest slide since August 2011. The Johannesburg Stock Exchange lost 3.5 percent while the Nigeria Stock Exchange shed 1.4 percent on the announcement of the leave outcome. Gold jumped by more than 8.1 percent to reach $1 358 per ounce on 24 June, reflecting its safe haven appeal. The British pound sterling lost as much as 11 percent of its value, as investors searched for safer assets. The euro was down 2.5 percent raising fears about its future, while the South African rand depreciated by 4.9 percent to reach a cumulative loss of 21 percent so far in 2016[1]. Crude oil retreated as much as 6.8 percent to reach $46.70 a barrel following the shock, raising further concerns for the prospects of oil exporting countries. While many of the stock indices recovered somewhat in the ensuing days after the referendum, market sentiment will likely remain weak and volatile until there is greater clarity about how the Brexit will unfold.

Capital flows

With unstable financial markets after the Brexit, financial conditions could remain tight, slowing capital flows to African countries in 2016, and affecting the financing of large infrastructure and other projects. With heightened risk aversion, cross-border bank lending and bond issuances could be curtailed. The strengthening of the US dollar after the vote could also raise the cost of servicing external debt, especially in frontier economies (e.g. Ghana, Cote d'Ivoire, Angola and Zambia) which accessed Eurobonds in recent years. The Brexit shock will likely further worsen the economic conditions of most African countries in the short term, possibly inducing further credit rating downgrades. There is also a risk of capital flight in African emerging market economies such as South Africa, Nigeria and Kenya, as risk averse investors seek safe havens. This could further weaken their currencies and increase the costs of imports and therefore raise inflation rates. Foreign direct investment from the UK and the EU could also be curtailed or delayed because of Brexit. According to UNCTAD, total FDI flows from the UK to African economies were about 16 percent of total flows to the continent in 2014. Investments are largely in mining and financial services in South Africa and Nigeria.

Trade

In the medium to longer term, Brexit could weaken trade between both the UK and EU on the one hand, and Africa on the other. The possible loss of the UK's access to the EU's single market may force it to negotiate new trade agreements with African countries and regional bodies such as the Southern African Development Community (SADC) and the Economic Community of West African States (ECOWAS). The renegotiations can could take several years, and could significantly reduce trade between the UK and Africa in the interim. Africa's exports to the UK represent about 5% of Africa's total exports, and therefore the continental effects may not be very large. However, some individual countries (e.g. South Africa, Nigeria and Kenya) with very strong trade ties with the UK could suffer in the short to medium term if the UK economy slumps, as expected.

The Brexit may also affect Africa's trade with the EU, although the actual trade agreements are not expected to change. Most trade agreements are through regional trading blocs such the SADC, COMESA and ECOWAS. Just recently (June 2016), the SADC and the EU signed an Economic Partnership Agreement (EPA), which allows free trade with Europe and introduces more flexible "rules of origin," with the aim of promoting the development of regional value

[1] http://www.bloomberg.com/news/articles/2016-06-24/u-k-referendum-roils-global-currencies-from-australia-to-mexico

chains. In West Africa, ECOWAS is the EU's biggest trading partner in Sub-Saharan Africa, with Nigeria, Cote d'Ivoire and Ghana accounting for 80 percent of West Africa's exports to the EU[2]. With Brexit, the EPAs with the EU might not extend easier access to the UK market. Meanwhile, the East African Community (EAC) is due to sign an Economic Partnership Agreement (EPA) with the EU in October 2016. As such, the Brexit move may cause a delay in the signing of this agreement. Some trade renegotiations between the UK and EU may also have negative effects on trade in Africa, for example they may diminish preferential trade agreements, which could negatively affect Africa countries. There are additional concerns about fears of euro-skepticism in other EU countries which could strain Africa's trade with the EU if the bloc's economy weakens further.

Slowdown in UK and the EU economies

Brexit is likely to place increased drag on the UK and the EU economies, and possibly push them into recession. In the run-up to the referendum, UK economic growth decelerated to 0.4 percent in the first quarter of 2016, exports contracted, domestic demand stalled and uncertainty dampened investment[3]. The Brexit shock is likely to compound these negative economic developments and the uncertainty associated with the "leave" outcome could easily tip the economy into recession and weigh down global economic growth. While the impact of Brexit could be very significant for Britain, the direct impact on the global economy could be limited, given the UK's small contribution to the global economy (about 3.7 percent[4]). The slowdown of the UK economy, and the weakening of the pound, might also dampen demand for African exports and reduce investment flows to the continent.

The Euro Area is much more important for the global economy than the UK, as it accounts for about 16 percent of the global economy. As such, its slowdown could weaken the already muted rate of global economic growth, which could affect African countries by reducing demand for their exports, curtailing or delaying investments and weakening global trade. As the UK is the second largest economy in the EU, Brexit could further weaken economic growth prospects in Europe, and potentially marks a period of increased political turmoil, with growing populist and nationalistic movements in the developed countries, that could weaken global trade. This trend could be seen as a symptom of underlying socio-economic malaise resulting from a combination of factors such as a slow-down in productivity, excessive debt, and ageing populations in the developed world. Reduced traded, along with potential financial system strains and greater political uncertainty, could also severely dent business confidence in Europe and significantly reduce investment. Weaker global trade could further weigh down commodity prices and dampen fiscal revenues in commodity exporting countries. This adds pressure to most African countries which are already reeling from the effects of the

[2] http://ec.europa.eu/trade/policy/countries-and-regions/regions/west-africa/
[33] Bank of England, Inflation Report, May, 2016
[4] MRB report, June 2016

commodity price shock and the growth slowdown in China. The Brexit has led to an appreciation of the USD, which if persistent could exert downward pressure on oil prices.

Development assistance from UK and Europe

The Brexit could negatively impact development aid to Africa. At the Gleneagles Summit in 2005, the G-8 countries agreed to increase development aid to developing countries by US$50 billion a year by 2010, with at least half of this commitment going to Africa[5]. Brexit will deprive UK resources for development assistance in the EU, as the UK is one of the biggest contributors to the European Development Fund (EDF) with about GBP 409 million—US$585 million (about 15 percent of contributions to the EDF[6]). Brexit has happened when IDA18[7] replenishment is in process, so this might affect development assistance to Africa. On its own, the UK has a firm commitment to spend 0.7 percent of its gross national income (GNI) on development aid. A slowdown in the UK economy would reduce its GNI in absolute terms and diminish development aid to Africa. Brexit may also mean that Britain's trade deals and aid agreements will have to be renegotiated, which could affect development assistance for Africa.

Opportunities

While the Brexit could pose challenges for the UK, Europe and Africa on many fronts, it may also create new opportunities.

New opportunities and new markets: The move may allow Britain to look for new opportunities and new markets. African resources and markets present considerable growth potential which Britain may want to tap. Africa has vast mineral resources, large areas of good arable land (about half of the world's unutilised arable land), and expanding markets buoyed by growing populations, rising middle classes and increasing urbanization. African countries continue to grow faster than they have in the past 40 years, and faster than most other regions. As opportunities for UK investors are diminished in Europe and elsewhere, the UK may want to turn to Africa.

Renewal of ties with former colonies: As it moves out of the EU, Britain might renew or strengthen political, trade and investment ties with its former colonies in Africa. In many countries such as South Africa, Nigeria, Ghana and Kenya, such ties are already strong. However, for some countries such as Tanzania, Zambia, and Zimbabwe, a lot has to be done to reclaim trade opportunities taken up by China in recent years.

Agricultural Policy: The UK has been a critic of the EU's Common Agricultural Policy (CAP), which allows subsidies to European farmers, presumably because Britain is a net importer of food and does not benefit much from it. The CAP reduced access of African farmers to the

[5] Sow and Sy (2016), The Brexit: What implications for Africa, Brookings Institution.

[6] Overseas Development Institute, 2015

[7] IDA is International Development Association- a collection of development finance contributed by member countries held and managed by the World Bank to help the world's poorest countries to reduce poverty by providing loans and grants for programs that boost economic growth, reduce inequalities, and improve people's living conditions. The current phase under replenishment is the IDA18.

European market because of tariffs on agriculture products. With Brexit, the UK may develop its own trade policy, which could provide opportunities for African farmers to have improved access to the UK market and boost their competitiveness.

Trade Competitiveness: The weakening of the British pound may help to boost competitiveness of some African countries' exports, as long as those countries' currencies do not also weaken (as has occurred in South Africa and Nigeria, for example).

Impact on selected countries

South Africa is the top EU and UK trade partner on the continent and hence is exposed more to the Brexit shock than other African economies. The UK is South Africa's fourth largest export destination, mostly dominated by metals and agricultural goods. To the EU, South Africa's exports topped USD14.2 billion in 2015 and the bulk of these exports have duty-free access to the EU and the UK under the Trade Development Co-operation Agreement[8]. As such, the Brexit may imply a renegotiation of trade terms with the UK, which could take up to two years or even longer. The sectors most at risk would be mining, agriculture and financial services. The negative effect of Brexit on South Africa's trade could also jeopardize trade within the Southern Africa Customs Union countries (Botswana, Namibia, Lesotho, and Swaziland).

Given the strong trade and financial ties between South Africa and the UK, and given that many large South African companies have a dual listing on the London and Johannesburg stock exchanges, the SA rand lost about 4.9 percent of its value immediately after the Brexit news. Such extreme volatility amid deteriorating economic conditions could prompt a ratings downgrade to non-investment grade, which South Africa escaped in recent months. South Africa also relies heavily on foreign capital to finance its wide current account deficit; the sudden attenuation of capital flows could further strain the already fragile economy.

Nigeria is the UK's second largest trade partner in Africa, after South Africa. Trade is currently estimated at US$8.3 billion and is projected to reach US$26 billion in 2020[9]. Trade will be disrupted as trade agreements made under the auspices of the EU will need to be renegotiated. The economy is already reeling under the weight of low oil prices, and a steep decline in oil production in the wake of disruption by the Niger Delta Avengers militants. Nigeria is also planning to issue Euro bonds and the tightening of global financial markets could raise the cost of debt. The UK is also Nigeria's largest source of foreign investment, with assets worth over USD1.4 billion[10]. Diaspora remittances to Nigeria amounted to USD21 billion in 2015[11], with a significant portion (18 percent) coming from the UK. The UK is also one of the largest development assistance donors to Nigeria. As the UK economy slows down further due to Brexit, it could dampen trade, investment, remittances and development assistance to Nigeria. Nigerian stocks, which previously rallied 8.5 percent after the central bank floated the

[8] https://lusakavoice.com/2016/06/29/the-impact-of-brexit-on-africa/
[9] UNCTAD, 2015
[10] National Bureau of Statistics, Nigeria
[11] World Bank, Migration and Remittances Factbook, 2016

naira, slumped 1.4 percent on 24 June. Nigeria recently liberalized its foreign exchange market and fuel sector, removing the peg of the Naira to the US dollar, and removing fuel subsidies. The slowdown of portfolio inflows will hamper the implementation of the country's new foreign exchange mechanism. The UK is also a key partner in Nigerian security, having assisted in drawing international attention to the Islamist Boko Haram insurgency in Nigeria's northeast. The Brexit negotiation process could distract the UK from international security threats, such as those by Boko Haram.

Kenya has strong trade ties with the EU and UK. Bilateral trade between the UK and Kenya is estimated at more than $1.7 billion, with key exports in horticultural products (fresh flowers and vegetables), and agribusiness (tea and tobacco). About one third of the EU's cut flowers come from Kenya. Brexit could cost the Kenya horticulture industry about USD38 million per month[12].There is a lot of British foreign investment in Kenyan agribusiness (tea, tobacco) and in oil and gas, as well as the financial sector.

Conclusion

In the short term, the Brexit is likely to induce increased market volatility and economic uncertainty, which could reduce capital flows as global financial conditions tighten, and reduce trade flows and foreign direct investment to Africa as the global economy slows. In the medium term, the UK's exit from the EU will result in the renegotiation of the UK's trade agreements with the EU and African countries. This could bring positive opportunities for some African economies, especially the former British colonies. Ultimately, the impact of Brexit on African economies will depend on a number of factors, including the time it will take to negotiate the exit, the terms of the negotiation process, how the leadership vacuum in the UK is filled, the adjustment processes, and policy responses to stimulate economies in the face the Brexit.

The Brexit is likely to further weaken economic growth prospects in Europe, and potentially marks a period of increased political turmoil, with growing populist and nationalistic movements in the developed countries, that could weaken global trade. This trend could be seen as a symptom of underlying socio-economic malaise resulting from a combination of factors such as a slow-down in productivity, excessive debt, and ageing populations in the developed world. For investors seeking solid economic returns underpinned by more positive fundamentals, such as youthful and growing populations, rapid urbanization and growth of consumption by expanding middle classes, Africa represents a comparatively attractive investment destination for those willing to seize the opportunities and manage the risks.

[12] http://www.kenyaflowercouncil.org