Strong consumer spending supported by decent income growth and improved financial conditions was not enough to allay the powerful headwinds that dominated the end of the 2010s: escalating global trade tensions, heightening geopolitical tensions, and fear of a no-deal Brexit. Even though equity markets set records after the 2018 year-end rout following the sharp sell-off of global risk assets, the International Monetary Fund revised down its global growth estimate to 2.9% in 2019 from 3.6% the year before—the lowest rate of expansion since the 2008 financial crisis.[1]

The sharp global slowdown was attributed to three demand-side factors: the fading sugar-high of the US fiscal stimulus; continuous monetary policy tightening initiated the year before by the US Federal Reserve; and escalating trade tensions. The US-China trade war was perhaps the most important policy-induced shock of 2019, when the escalation of tariffs and supply chain disruptions led to a sharp contraction in global demand and trade. Global trade volumes slowed to an average growth rate of 1.2% in 2019 from 4.6% in 2017, far exceeding the slowdown that would be fully attributed to the ongoing maturation of global value chains.[2]

The decelerating trade intensity of global growth was particularly high across advanced and industrialised economies. This has been exacerbated by a slowdown in the trade-intensive manufacturing sector and decline in the production of capital and intermediate goods. In the face of rapidly declining trade intensity of global growth, the US Federal Reserve opted for a major policy reversal. The central bank pivoted away from consistently increasing its benchmark rate (raising it by 100 basis points in 2018), to three rate cuts of 75 basis points in the second half of 2019, which were intended to offset the risk of an exogenous recession triggered by the trade war. Other major central banks followed suit to ensure monetary convergence and mitigate the risk of growth deceleration and global volatility.

Exhibit 1: Contribution to Global Growth and Trade

	Contribution to global growth			Contribution to global trade		
	2017	2018	2019	2017	2018	2019
EU	10.9%	10.1%	9.2%	33.3%	33.2%	33.3%
US	11.7%	13.7%	13.8%	11.0%	10.8%	11.0%
China	27.2%	27.4%	32.7%	11.7%	11.9%	11.8%
India	11.7%	11.7%	13.5%	2.1%	2.1%	2.1%
Others	38.5%	37.1%	30.8%	41.9%	42.0%	41.8%

Source: IMF Direction of Trade Statistics, Afreximbank Research

In that challenging global economic environment dominated by two conflicting policy-induced shocks—the contractionary beggar-thy-neighbour policy which led to a sharp decline in the trade intensity of global growth and growth-enhancing monetary policy easing following the regime change by major central banks—global growth decelerated only marginally in most advanced and developing market economies, even though the synchronised growth deceleration in four of the largest economies and trading blocs (China, the European Union, India and the US) should have resulted in a sharper growth

[1] See IMF 2020, "World Economic Outlook Update: Tentative Stabilization, Sluggish Recovery?", International Monetary Fund (IMF), January 20, 2020.

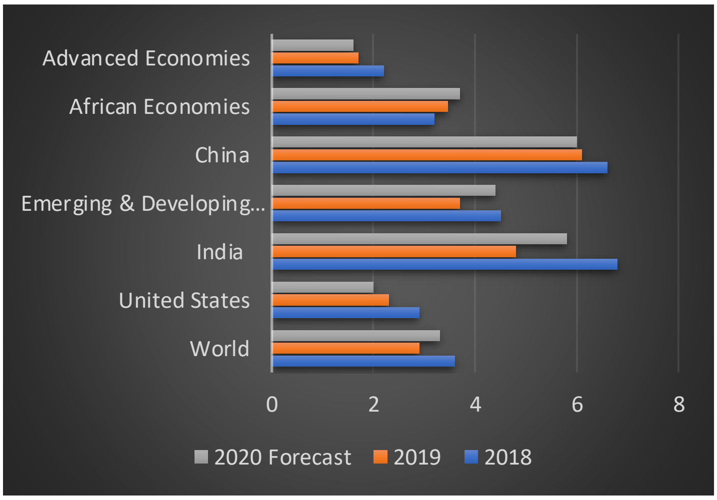
[2] See WTO 2019, "Trade Statistics and Outlook: WTO lowers trade forecast as tensions unsettle global economy", October 2019.

deceleration (see Exhibit 1). Together these four economies accounted for about 70 percent of world GDP growth in 2019 and China alone accounted for 33 percent.

The synchronised growth deceleration among these leading drivers of global output was a major departure from previous episodes of global growth dynamics, in which robust growth rates in emerging and developing market economies like China and India consistently made up for lacklustre growth in advanced economies. Last year India suffered a sharp growth deceleration, with output falling by 2 percentage points to 4.8%, owing to subdued domestic demand amid stress in the nonbanking financial sector and a decline in credit growth.

African economies expanded by 3.5% in 2019, slightly up from what the region achieved the previous year, but down by around 0.3 percentage points from earlier predictions when tightening monetary policy was the only demand-side constraint on the horizon. African economies are expected to strengthen in the near term and achieve an average growth rate of 3.7% in 2020 (see Exhibit 2). This will again position Africa as the second fastest-growing region of the world after Asia.

Exhibit 2: Real GDP Growth by Region & Selected Countries (%)



Source: IMF World Economic Outlook, Afreximbank Research

The improved growth forecast is supported by a combination of idiosyncratic and external factors. Most notable is the broad-based shift towards accommodative monetary policy and a gradual return to a rules-based trading system, which has supported global economic expansion and trade after the conclusion of "phase one" of the US-China trade negotiations. Moreover, the promising growth outlook is buttressed by the rapid and coordinated global response to contain the coronavirus. Albeit still a risk to the global economy several governments have taken bold monetary and fiscal policy measures to curtail its impact.

External drivers of Africa growth

Africa's improving economic outlook is supported by several demand-side policy measures. These are likely to boost global demand and reduce volatility, specifically the risk of capital flow reversals that typically amplify liquidity constraints in emerging and developing market economies.

First among these favourable external factors is policy-makers' commitment to sustain strong rates of economic expansion, drawing on monetary easing in a benign environment where inflation has consistently undershot its target.

Inflation remains largely below institutional targets in advanced economies and has been on a long-term decline in most developing economies. In the US, the level of inflation-adjusted interest is barely positive. Meanwhile, stubbornly subdued inflation has kept the Bank of Japan in a monetary stimulus mode for a prolonged period. With core consumer inflation expected to fall short of its 2% target, the BoJ is set to continue its monetary easing to maintain price momentum and expand output to overcome secular stagnation. Japan's growth rate is projected to shrink further to 0.7% in 2020 from 1% in 2019 and could decelerate even further, especially in the light of any coronavirus-related troubles.

Similarly, core consumer inflation remains deeply negative in Europe, reflecting weak economic growth and labour market slack. Although euro area growth is expected to rise in 2020 (to 1.3%), it remains very low. This anaemic growth is largely due to a sharp decline in industrial production. In Germany, manufacturing remained in contractionary territory in late 2019, with potential for spillovers into 2020.[3] The trade war exacerbated these growth challenges and prompted the European Central Bank to cut interest rates deeper into negative territory and reinstate its bond-buying programme to see off the threat of deflation. Inflation has inched up slightly since then but remains far below the ECB's target of "below, but close to, 2%".

In China, monetary easing was also dictated by growth considerations, especially in the context of the raging trade war. After several cuts to its reserve requirement, the People's Bank of China lowered its short-term lending rates and medium-term benchmark loan prime rate to support growth in the wake of the coronavirus outbreak. Beijing has pledged to roll out more stimulus to mitigate downside risks associated with the health crisis and contain any economic fallout.

Recent high-frequency data show that GDP and current activity indicator estimates are below potential in most countries, and first-quarter growth estimates have been revised down for most major economies.[4] These conditions will probably dissuade central banks from hastily tightening monetary policy, especially in a stubbornly low-inflation environment. But the risk of divergence with the US, where the Federal Reserve remains set on an ultra-loose course, also discourages any hasty unilateral move towards monetary tightening.

The Financial Conditions Index, which provides a comprehensive weekly update on US financial conditions in money markets, debt and equity markets and the traditional and shadow banking systems, ticked down further into negative territory in the last week of February (see Exhibit 3). The index is now below levels recorded in mid-2018. Moreover, the global FCI is at a record low, suggesting that financial conditions have become even looser than at any time over the last two years, a policy stance that is unlikely to be reversed in the short term.

Exhibit 3: Financial Condition Index

Source: Federal Reserve Bank of Chicago

Second among external factors is the low near-term risk of recession, especially in the leading economies and Africa's major trading partners – China, the EU, India and the US.[5] In 2019, these accounted for over 60% of African trade and 58.7% of total African exports (see Exhibit 4). Monetary easing and coordination between central banks has become an insurance against global volatility; it has fuelled sustained growth in asset prices and set the world economy on one of

[3] Especially given that the disruptions caused by the coronavirus has particularly affected the automotive sector.

[4] OECD 2020, "Coronavirus: The world economy at risk", OECD Interim Economic Assessment. March 2020.

[5] Afreximbank 2019, "African Trade Report 2019: African Trade in a Digital World", The African Export-Import Bank.

the longest periods of expansion on record. Other indicators point to further expansion of the current business cycle. Its length has not led to a disproportionate increase of private sector spending relative to income. Across most advanced economies, households and businesses enjoy a strong financial position, with the private sector running a sizable financial surplus.[6]

Exhibit 4: Key African Trade Partners

	Share of total African Trade			Share of Total African Exports		
	2017	2018	2019	2017	2018	2019
EU	30.4%	30.2%	29.7%	31.4%	30.8%	29.6%
US	5.5%	5.3%	4.8%	4.0%	4.2%	4.2%
China	17.6%	18.4%	19.0%	18.8%	18.7%	19.4%
India	6.4%	6.4%	6.6%	4.9%	4.9%	5.5%
Others	40.1%	39.7%	39.9%	40.9%	41.4%	41.3%

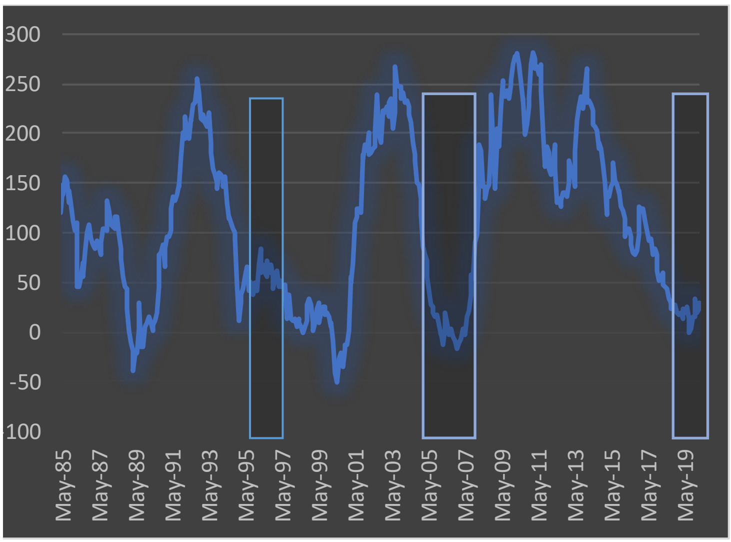
Source: IMF Direction of Trade Statistics, Afreximbank Research

Still, monetary accommodation borne out of the quantitative easing era has shifted the monetary policy stance more towards growth, aided in part by doggedly low inflation. In the process the yield curve once praised for capturing the direction of monetary policy lost its ability to predict economic recession. This is perhaps because QE, which was intended to depress long-term bond yields below an economic neutral rate, has done just that in a low-inflation environment.

Even though long-term rates fell below short-term rates in several advanced economies in 2019 – including in the US, where it turned negative in May and fell below negative 50 basis points in August (see Exhibit 5) – the inversion did not necessarily presage an imminent economic downturn. Instead it reflected a structural decline in the term premium and the flattening of the Phillips curve in the context of the weakening relationship between labour market slack and wage growth. Unlike previous episodes, the latest inversion of the US yield curve coincided with an exceptional subdued term premium that has been declining since the financial crisis, perhaps as a result of demand pressures from price-inelastic institutional and public investors such as central banks and pension funds.

Third, the easing of global trade tensions after the conclusion of "phase one" of the US-China trade negotiations should boost growth and trade for both countries and ultimately reinvigorate global demand. The trade war waged by President Donald Trump's administration exacerbated the process of growth deceleration, pivoting major economies away from synchronised growth acceleration towards synchronised deceleration. It has decreased real exports in the two belligerent nations and beyond. Indirectly, it has undermined growth prospects in other countries through weaker demand for their exports, supply-chain disruptions, lower investment and feebler economic growth.

Exhibit 5: The US yield curve (2-year minus 10-year bond yields)



Source: Bloomberg, Afreximbank Research

The costs to the US and China outweighed any gains they could possibly have derived from trade diversions to avoid tariffs. According to Goldman

[6] See Jan Hatzius, Daan Struyven and Ronnie Walker, "A Beak in the Clouds", Global Economics Analyst, November 2019.

Sachs, the trade war subtracted around 0.4 percentage points from quarterly annualised growth in the US and 0.6 percentage points in China.[7] The return to a rules-based trading system after the conclusion of "phase one" negotiations could raise investment and growth to levels commensurate with the deceleration of growth caused by the trade war in a symmetrical correction. Following that assumption, Africa's deepening trade ties with China (now its single largest-trading partner) could position the region as one of the main beneficiaries of growth acceleration arising from the US-China truce.

These deepening trade ties have allowed Africa to vary its exports' destinations as well as diversify its risk exposure away from growth volatility emanating from a single country or region. They have enabled Africa to surf on China's strong investment and economic performance to sustain its own growth momentum. Evidence points to large spillovers of China's investment growth to Africa through trade channels, with a 1 percentage point increase in China's domestic investment growth associated with a 0.6 percentage point increase in Africa's export growth.[8] This positive correlation suggests that the combination of fiscal expansion and monetary easing measures undertaken by China to boost investment and domestic demand should support further trade and economic expansion in Africa, especially in the light of progress in restoring factory output after weeks of coronavirus-related disruptions.

The projected speedy recovery is amplified by the shift towards global co-operation to contend with the outbreak. The coronavirus has swelled into a pandemic demanding a coordinated international response to protect individual health and global prosperity. In this regard, bold monetary and fiscal policy measures initiated by authorities around the world to contain the virus and set the global economy on a strong recovery path are encouraging. The blend of monetary easing and fiscal stimulus announced by several countries should restore some of the missing demand and re-energise the supply-side of the growth equation over time.

Internal drivers of Africa's growth resilience

On the internal front, the predicted growth acceleration and continued resilience of African economies reflects the region's improving growth fundamentals, especially strengthening investment and domestic consumption. These have been bolstered by softening inflation, rising urban populations, growth acceleration in both large and small non-resource intensive economies, and increasingly favourable business environments. Meanwhile, the commitment to macroeconomic stability has become the anchor of economic management across the region. A growing number of countries are undertaking difficult economic reforms to improve the business environment and boost private investment.

In oil-rich central African countries that were hit hard by the end of the commodity super-cycle and continue to be affected by global volatility in commodity markets, governments are executing reforms to mitigate external and internal imbalances.[9] While fiscal consolidation, subsidy cuts and diversification of sources of growth are the common denominator among these reforms, there are variations across countries. Angola's reforms emphasise the implementation of a

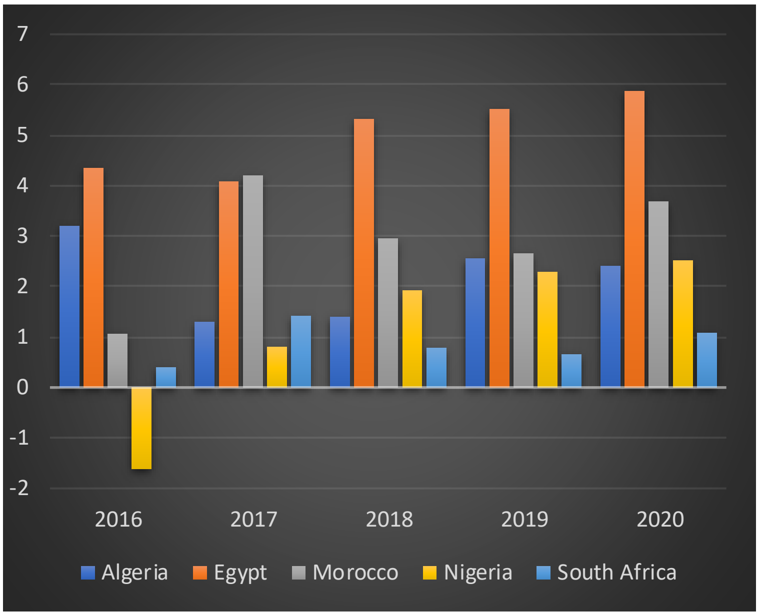
[7] See Jan Hatzius, Daan Struyven and Ronnie Walker, "A Beak in the Clouds", Global Economics Analyst, November 2019.
[8] See Paulo Drummond and Estelle Xue Liu, "Africa's Rising Exposure to China: How Large are Spillovers through Trade?", IMF Working Paper, WP/13/250.
[9] See Hippolyte Fofack 2019, "Overcoming the colonial development model of resource extraction for sustainable development", in Africa. Africa in Focus. Washington, DC: The Brookings Institution. https://www.brookings.edu/blog/africa-in-focus/2019/01/31/overcoming-the-colonial-development-model-of-resource-extraction-for-sustainable-development-in-africa/.

medium-term fiscal framework with spending rules and a well-designed fiscal stabilisation fund to reduce procyclicality in spending.[10] In several other countries governments are stressing the adoption of a market-clearing exchange rate, the goal being to unwind exchange rate restrictions gradually and enhance convergence between official and parallel rates. Some countries are relying on macroprudential reforms to mitigate systemic risks to the financial sector, while others are lowering policy rates to address supply-side constraints and raise aggregate output.

Average inflation fell by 2 percentage points in 2019 and continues to trend downwards across the region. The fiscal balance has improved as well. Since 2017 the weighted average deficit-to-GDP ratio has decreased by more than 1 percentage point to less than 4.8% in 2019 amid the adoption of value-added tax in a growing number of countries and rising tax rates and non-tax revenues. These developments are bolstering investor confidence and sustaining the economic recovery in a region where growth is increasingly broad-based and resilient, even in the face of global headwinds.

Against the global trend of synchronised growth deceleration, economic growth accelerated in several small and large African economies. Egypt and Kenya posted some of the strongest rates of expansion, with both exceeding 5.5% (see Exhibit 6). More than 25 African countries recorded growth acceleration in 2019, and around 35 are forecast to enjoy more this year. Around 55% are projected to grow by more than 5% over the forecast period. Rates of expansion in some countries are expected to decline, yet these remain among the fastest-growing economies in the world. This is the case for Ethiopia and Côte d'Ivoire, whose economies are projected to expand respectively by 7.2% and 7.29%, down only marginally from 7.44% and 7.49% last year.

Exhibit 6: GDP growth of Africa's five largest economies (%, 2016-20F)



Source: IMF World Economic Outlook, Afreximbank Research

Over the last few years Africa has been home to some of the fastest-growing economies in the world (see Exhibit 7). Five African countries are included among 2020 consensus forecasts for the top-10 fastest-growing economies in the world. These include South Sudan, Rwanda, Côte d'Ivoire, Ethiopia and Senegal, with each projected to achieve an annualised growth rate greater than 6.7% in 2020. At 8.2%, South Sudan is expected to be the fastest-growing economy on the continent for the second consecutive year and the second fastest-growing in the world after Guyana.

[10] See IMF 2018, "Angola: Staff Report for the 2018 Article IV Consultation", International Monetary Fund.

Exhibit 7: Top ten Fastest-Growing Economies in the World (GDP Growth)

2018		2019		2020 Forecast	
Libya	17.9%	Dominica	9.4%	Guyana*	85.6%
Eritrea	12.2%	South Sudan	7.9%	South Sudan	8.2%
Rwanda	8.6%	Rwanda	7.8%	Rwanda	8.1%
Ireland	8.3%	Bangladesh	7.8%	Bangladesh	7.4%
Bangladesh	7.9%	Côte d'Ivoire	7.5%	Côte d'Ivoire	7.3%
Ethiopia	7.7%	Ghana	7.5%	Bhutan	7.2%
Cambodia	7.5%	Ethiopia	7.4%	Ethiopia	7.2%
Maldives	7.5%	Nepal	7.1%	India	7.0%
Côte d'Ivoire	7.4%	Cambodia	7.0%	Cambodia	6.8%
Antigua and Barbuda	7.4%	Mauritania	6.6%	Senegal	6.8%

* Guyana is poised to start oil production in 2020
Source: IMF World Economic Outlook, Afreximbank Research

These are the dividends of governments' far-reaching pro-investment reforms that support expanding manufacturing output, services on the production side and household consumption, fuelled in part by a steady inflow of remittances on the demand side. But the projected economic expansion is also buoyed by strengthening domestic investment in a context of improved external financing conditions, the clearance of domestic arears and supportive monetary policies. Across Africa, countries are taking advantage of declining yields on long-term debt instruments and narrowing spreads to expand infrastructure networks.

A growing number of African countries are making a shift in the formulation of monetary policy to pursue the dual objectives of price stability and growth. For instance, to boost lending to the real economy and expand industrial output, the Central Bank of Nigeria set a minimum loan-to-deposit ratio of 65% for the banking sector. These policies could bolster growth among small and medium-sized enterprises and accelerate the diversification of exports and sources of growth. The improving macroeconomic environment and market sentiment is enabling central banks to draw on monetary levers to boost domestic demand and investment. Decreasing inflationary pressures allowed monetary authorities to cut interest rates by 150 basis points in Egypt, by 50 basis points in Nigeria and Namibia, and by 25 basis points in Botswana. With inflation set for a long-term decline, more rate cuts could yet be undertaken, especially in the global context of convergence towards easier monetary policy.

In a major shift away from excessive dependency on consumption, investment and net exports have become leading drivers of growth. An analysis of Africa's GDP growth shows that the contribution of these new forces has been increasing over time and set a new record in 2019, when for the first time in more than a decade investment expenditure accounted for more than 54% of aggregate GDP growth.[11] It seems to be the case that, as supportive policy measures are implemented to alleviate supply-side constraints, a growing number of African corporates are taking advantage of the opportunities associated with expanding economies of scale to align domestic production and demand. These businesses are at the vanguard of Africa's diversification from agricultural products to higher-value goods in manufacturing and services. They are increasingly active in strategic industries, including telecommunications, finance, oil & gas and basic materials.

But these entrepreneurs are likewise taking advantage of expanding economic infrastructure, specifically the development of "special economic zones" (SEZs). These geographically defined areas serve as development magnets that shift the distribution and allocation of foreign direct investment away from primary commodities and natural resources towards manufacturing and industrial production. The number of African SEZs has grown significantly over the last decade – 237 were operating in 2019, along with 200 single-enterprise power zones (so-called "free points"). There are SEZs in 38 African countries, led by Kenya, Nigeria and Ethiopia, which account for around half.[12]

The development of SEZs has promoted the industrialisation process and expansion of manufacturing output in several countries, including fast-growing Ethiopia and Rwanda, two economies firmly on an export-diversification trajectory. Though Africa's SEZ figures pale in comparison to those of Asia (where more than 4,000 operate), the impressive growth recorded across the region augurs well for ongoing efforts to build an Asia-like export-led growth development model. This will accelerate the process of industrialisation and bolster the manufacturing revolution needed to fast-track the diversification of African exports. As more countries adopt that model, Africa will become less exposed to global volatility, commodity cycles and long-term deterioration of commodity terms of trade, which have been the main constraints to long-run growth and the region's effective integration into the global economy.

SEZs are supporting the development of regional value chains, strengthening forward and backward linkages in a part of the world where intraregional sourcing remains very low, less than 15%. That is significantly below that of Southeast Asia, where intraregional sourcing accounts for more than 80% of exports in industries such as motor vehicles, textiles, apparel, computers, electronics and optical products.[13] Beyond facilitating the sourcing of intermediate goods, the development of regional value chains will boost intraregional trade and mitigate the impact of global shocks and volatility, putting Africa on a long-run growth trajectory.

The region's improved growth forecast is also informed by the tremendous development potential associated with the African Continental Free Trade Agreement (AfCFTA) – trading under the agreement is scheduled to start on 1 July. Although intraregional trade has been an efficient absorber of adverse global shocks in other parts of the world, its capacity to date to insulate Africa

[11] See African Development Bank 2020, African Economic Outlook.
[12] See UNCTAD 2019, "World Investment Report 2019: Special Economic Zones", United Nations Conference on Trade and Development (UNCTAD).
[13] See AUC/OECD 2019, "Africa's Development Dynamics: Achieving Productive Transformation.

from exogenous and policy-induced shocks has been undermined by the segmentation of African markets.

This has made it difficult for companies to spread the risks of investing in smaller markets across the region and constrained the expansion of output and the growth of intraregional trade. Despite a relative increase over the last decade, intraregional trade still accounts for just 16% of total African trade, against 67% in Europe and 54% in Asia. The AfCFTA – which established the largest free trade area in the world by membership, with a market of 1.2 billion consumers and combined GDP of US$2.5 trillion – has been touted as a game-changer. It has the power to defragment Africa, enhance competitiveness and boost productivity. Preliminary estimates show that intra-African trade could increase by half within a decade of the agreement's implementation or even double if trade facilitation, rather than just tariff liberalisation, is undertaken.[14]

Rising investment and infrastructure development are boosting labour productivity and accelerating structural transformation in a region where rapid urbanisation is propelling demand for manufactured goods. These account for a growing share of intra-African trade and are set to expand even more during the AfCFTA's implementation. The combination of improving productivity and economies of scale associated with economic integration is sustaining the competitiveness of African corporations, which are expanding their industrial and geographical footprint across the region. The improving economic environment is also attracting more multinational companies and changing the composition of FDI towards labour-intensive manufacturing industries as corporations take advantage of increasing efficiency and economies of scale.

[14] See Hippolyte Fofack, "A competitive Africa: Economic integration could make the continent a global player", IMF Finance and Development, December 2018.

Risks to Africa's growth outlook

Until recently, the downside risks facing Africa have been rooted in constraints emanating from demand-side factors, especially in the light of the proliferation of beggar-thy-neighbour trade policies. But the coronavirus outbreak has added another challenge – a supply shock. The temporary closure of factories and disruption of commerce and supply chains that underpin modern manufacturing in the globalization era have led to a sharp contraction in global demand for natural resources: the price of Brent crude has dropped almost 50% since early January, falling close to US$35 per barrel in the first week of March. These developments could heighten macroeconomic volatility and widen external and internal imbalances in a region where natural resource exports still account for the lion's share of fiscal revenues and foreign exchange earnings.

If coronavirus-related uncertainty persists deep into the second quarter and precipitates sharp growth deceleration in major economies like China, the EU, India and the US, Africa's economic outlook will suffer. Following the global trend, growth in the region could decelerate on the back of falling investment and commodity prices as well as contracting global demand. The falling global demand for commodities and sustained deterioration of commodity terms of trade could widen trade deficits and undermine countries' efforts to remain on a path of sound fiscal and debt sustainability.

However, the supply shock created by the coronavirus may yet take a "V-shape" – a short-lived hit in which outbreaks are rapidly contained and prove to be relatively mild. In that case, the supportive monetary and fiscal measures adopted by major governments as part of a coordinated global response could quickly restore market confidence and engender a speedy recovery.

Fiscal policies, such as delaying tax payments, could shield households and companies from a sudden drop in income, while fiscal stimulus and monetary easing could boost confidence and accommodate the recovery of demand. Such measures could reignite the global production engine to close the output gap and respond to surging global demand, drive demand for commodities and lift prices.

This assessment of Africa's growth prospects has been prepared by Hippolyte Fofack, Chief Economist at the African Export-Import Bank (Afreximbank). The document provides analyses of the Research Department and does not purport to reflect the views of Afreximbank.

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